JUTA

EIGHTH EDITION



General Principles of

Commercial Law

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1.1 A short history of the law

Law is a social science; it has to provide for the changing needs of a developing community and consequently is inseparably bound up with the community it has to serve. For a thorough understanding of the law it is essential to have a knowledge not only of the community in which it functions, but also of its history and of the factors which led to its origin and development. This is why every study of the law includes a study of the history of the law. Another reason is that a knowledge of legal history helps to evaluate probable trends of future development.

South African law, unlike, for example, most European continental legal systems, is not codified (that is, recorded in one comprehensive piece of legislation). The law applying in the Republic is drawn from various authoritative sources. The principal sources are statutes and decided cases, but sometimes a judge or other jurist has to go further back in history to solve a legal problem, and turns to Roman law or the works of the writers on Roman-Dutch law to shed light on the problems. Roman law and Roman-Dutch law are also recognised sources of the law.

South African law today is the product of different sources. First, it has its origins in Roman law. Secondly, during the fifteenth and sixteenth centuries, Roman law became fused with Dutch customary law — hence the term Roman-Dutch law — and it was this law that Van Riebeeck brought to South Africa. Thirdly, as can naturally be expected in view of the country's history, English law exerted a considerable influence on Roman-Dutch law.

Each one of these historical sources will be dealt with very briefly.

1.1.1 Roman law

Roman law traditionally spans the period from 753 BC to AD 568. At the beginning of this period, Rome was a small, relatively primitive state with most of its population living on farms around the city. Its economy was based mainly on

agriculture, with no trade to speak of. The nucleus of the community was the family with the oldest male ascendant at its head. Not only was he the sole owner of all the family property, whether acquired by himself or his dependants, but he was also the holder of all power, including the power of life and death, over the members of his family and his slaves. The law was correspondingly primitive.

Rome, however, developed rapidly until it stood at the head of a vast empire which extended over virtually the entire Western Europe and large portions of Africa and Asia. Obviously, the law had to adapt to and make provision for these changed circumstances, and, in consequence, a highly sophisticated legal system, capable of dealing with the exigencies of increasing wealth, expanding trade and an influx of foreigners, evolved.

From AD 291 attempts were made to codify Roman law and these attempts culminated in a codification known as the *Corpus Iuris Civilis*, which appeared during the reign of Emperor Justinian in the sixth century. Today, this work is still the primary authoritative source on which South African courts draw when reverting to Roman law to solve a legal problem.

1.1.2 Roman-Dutch law

The Roman Empire declined and fell in AD 476 but this did not mean that Roman law disappeared. During the Middle Ages, traces of Roman law remained for two reasons. In the first place, every person, wherever such person might be, was judged according to the law of his or her own tribe or country and, therefore, former Roman citizens were treated according to Roman law. In the second place, the church exerted great influence during this period and canon law was based mainly on Roman law; this, of course, contributed to the preservation of Roman law.

During the fifteenth and sixteenth centuries, particularly, Roman law was received in the Netherlands and became mixed with the existing Dutch customary law.

The works of Roman-Dutch jurists, the statutes of Holland (as far as they are still in force) and the collections of old Dutch opinions and court decisions, form the source of present-day South African law.

1.1.3 English law

In 1652 Jan van Riebeeck brought Roman-Dutch law to the Cape, but the administration of justice during the seventeenth and eighteenth centuries left much to be desired. After 1814, the year in which the Cape was formally ceded to Great Britain, the existing Roman-Dutch law remained in force but various factors contributed to a reception of English law. The direct and indirect influence of English law was encouraged. Appeal to the Privy Council in London was instituted, the jury system was introduced, and the Orphan Chamber was replaced by the Master of the Supreme Court. English law was often directly drawn on for new legislation: for example, a code of criminal procedure was introduced in 1826; the entire English law of evidence was introduced in 1830, and the English system

of the administration of estates in 1843. Simultaneously, a gradual infiltration of the English legal terminology and manner of thinking took place, resulting in a strong and adaptable system of law.

The year 1910 was a milestone in the development of South African law. That year saw the establishment of a Union Parliament, a uniform system of statute law for the whole country, and the establishment of the Appellate Division to ensure more or less uniform decisions for the Union. The Privy Council was of comparatively little importance after 1910 and was abolished as the highest court of appeal for South Africa by Act 16 of 1950.

1.2 Sources of the law

South African law is derived from a number of sources. Some sources are authoritative while others merely have persuasive authority. Courts are bound by authoritative sources, whereas those of persuasive authority may lead a court to apply or interpret a legal rule in a particular way. The sources of South African law, in the order in which they are usually consulted, are the following:

1.2.1 Statute law or legislation

1.2.1.1 General

Legislation is the making of law by a competent authority. Today, legislation is the most important source of the law. The law is to be found in statutes enacted by Parliament and provincial legislatures, and by proclamations, regulations and by-laws enacted by subsidiary legislative bodies such as the President, ministers and municipalities.

There are even certain Dutch statutes which still apply in South Africa, namely, pre-1652 legislation. Dutch legislation of the period 1652-1806 applies only if it has been ratified and accepted by South African law. Dutch legislation passed after 1806 does not apply here. There are only a few Dutch statutes which are still in effect in South Africa; the legislature has repealed many of these statutes and replaced them with new legislation. An example of such a statute which still applies is a law of 1658 concerning the lease of immovable property (this law is referred to again in chapter 14).

English statutes never applied here, unless the legislation had been especially promulgated by the British Parliament to apply to the Union of South Africa or the colonies.

Some of the laws of the four pre-1910 provinces still apply today in so far as they have not been repealed or amended by Parliament or by the provincial legislatures.

1.2.1.2 The Constitution

The most important source of law in South Africa is the Constitution of the Republic of South Africa, 1996. Previously, we had a supreme Parliament. This

meant that any law passed by Parliament was valid, irrespective of its contents. We now have a system of constitutional supremacy under which the Constitution is the supreme law of the Republic. This means that if Parliament were to pass a law that offended against the provisions of the Constitution, it would be invalid. Not only new legislation but also existing law that is inconsistent with the Constitution can be declared invalid by a superior court.

The preamble to the Constitution states that it was adopted so as to —

(a) heal the divisions of the past and establish a society based on democratic values, social justice and fundamental human rights
(b) lay the foundations for a democratic and open society in which government is based on the will of the people and every citizen is equally protected by law
(c) improve the quality of life of all citizens and free the potential of each person, and
(d) build a united and democratic South Africa able to take its rightful place as a sovereign state in the family of nations.

The primary method of giving effect to these ideals is through the Bill of Rights, contained in Chapter 2 of the Constitution. The Bill of Rights is the cornerstone of democracy in South Africa and confirms the democratic values of human dignity, equality and freedom. The Bill of Rights applies to all law and binds all three branches of government (the legislature, the executive and the judiciary) and all organs of state. The state is required to respect, protect, promote and fulfil these rights.

The Bill of Rights deals with first-generation rights (most of which are negative rights that take power away from the state by imposing a duty not to act in a certain way, for example not to torture or not to discriminate), and with second-generation rights (positive socio-economic rights that impose an obligation on the state to provide all members of society with certain basic necessities). First-generation rights include the rights to equality, human dignity, life, and various freedoms of the person — of religion, of expression, of movement and trade. Second-generation rights include the right to housing, health-care, food and water, social security and education.

None of these rights is absolute in the sense that it always applies. Rights can be limited in special circumstances, which are that —

- The limitation must take place by law of general application.
- It must be reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom.
- It must take into account all relevant factors, including the nature of the right, the importance of the purpose of the limitation, the nature and extent of the limitation, the relation between the limitation and its purpose, and whether there are less restrictive ways of achieving the purpose.

All these circumstances must be met for a limitation to be lawful.

The Constitution also regulates government by setting out the structure of the state and its organs, and by providing for their functions and powers. It deals with

national, provincial and local government, the courts and the administration of justice, public administration, security services, traditional leaders and financial matters of state.

1.2.2 Customary law

Certain rules of conduct are observed because it has become customary in a particular group of people to respect such usages. Customary law does not consist of written rules, but develops from the habits of the community and is carried down from generation to generation.

In modern communities where the rate of development is very rapid, custom has less opportunity to develop into law. Once the need for a particular legal rule arises, the legislature simply steps in and lays down such a rule. Yet, even today it may still happen that custom develops into law. In *Van Breda v Jacobs* 1921 ad 330, a local custom amongst fishermen — that once they have set their lines on a beach where no boats are permanently stationed, for the purpose of catching a shoal of fish seen moving along the coast, no other fishermen are entitled to set lines within any reasonable distance in front of the lines already set — was held to be duly established by the evidence as a valid custom. It appears from this judgment that the following requirements must be met before a customary rule will be recognised as a legal rule:

(a) It must be reasonable.
(b) It must have existed for a long time.
(c) It must be generally recognised and observed by the community.
(d) The contents of the customary rule must be certain and clear.

The court's decision that a particular custom is valid merely recognises the custom as being law and does not give the custom any greater force than it had before. Nevertheless, the validity of the custom is thereby established.

Customary law, also called 'trade usages', also plays an important role in the business and commercial world. It is often alleged that a trade usage exists within a certain trade or business and that the parties to a contract are bound by it. The same requirements as those for proving a rule of customary law apply. For example, a trader who alleges that a customer must pay an installation fee for a television or stove bought from the trader must prove all of the requirements in (a)-(d) above. Where one of the requirements has not been proved, the court will not enforce the usage.

1.2.3 Judgments of the courts

The judgments of the Dutch courts before 1652, judgments of the Cape Council of Justice before 1827, judgments of the courts of the four provinces before 1910, and judgments of the South African courts after 1910 form an important authoritative source of law which is known as case law.

The South African courts are traditionally divided into superior and lower courts.

The superior courts are the Constitutional Court, the Supreme Court of Appeal and the High Court.

The lower courts are those courts which are lower in status than the High Court and which are not required to keep a record of their proceedings. Examples of these are the magistrates' courts, the small claims courts and the different courts of black chiefs and headmen. The jurisdiction of the lower courts is limited: that is, they can adjudicate only on specific matters and only in respect of specific persons.

The most important judgments of the Constitutional Court, the Supreme Court of Appeal and the High Court are reported mainly in *The South African Law Reports and the All South African Law Reports*. Some judgments of the courts in Namibia and Zimbabwe are also reported.

1.2.4 The old authorities

As pointed out above, Roman and Roman-Dutch law played an important role in the development of present-day South African law. The works of the old jurists of Holland are still authoritative in the courts today. Ancient Roman law as set out in the *Corpus Iuris Civilis* still applies as a direct source of South African law. The body of law provided by the old authorities is also known as the common law.

1.2.5 Foreign law

If nothing can be found in one or more of the above sources, a judge will turn to the law of other modern countries for guidance. Foreign law is not regarded as an authoritative source for South African law — it has persuasive authority only. In this connection, the decisions of the English courts immediately come to mind, but it must be emphasised that English law is no authority if South African law makes full provision on the point. The courts will reject South African decisions which in the past have wrongly adopted English law. The decisions of the American courts have sometimes been accepted in South Africa, but, of course, they are not binding. Moreover, where necessary, the courts may have regard to the law of countries on the European continent. The law in many of these countries is based on Roman law and, accordingly, South African and European law correspond to a considerable extent.

Foreign law as a source of law has also been recognised in the Constitution. The Constitution specifically provides that in interpreting the Bill of Rights a court of law must consider international law and may consider foreign law.

1.2.6 Textbooks and law journals

There are numerous textbooks and law journals on South African law. The journals contain articles, case discussions and analyses on a variety of topics. These works are written by lawyers, for example, legal academics, advocates, attorneys and judges. These works have no inherent authority of their own, but if they are methodical and convincing expositions of the law, they may well have a persuasive influence on the courts.

1.3 The courts in the Republic

It has already been pointed out that the courts in the Republic are divided into superior and lower courts. The most important superior courts are the Constitutional Court, the Supreme Court of Appeal and the High Court. The most important lower court is the magistrate's court.

1.3.1 The Constitutional Court

The Constitution Seventeenth Amendment Act of 2012 amended the Constitution to provide that the Constitutional Court is the highest court in all matters. Before this

amendment, section 176(3)*(b)* of the Constitution stipulated that the Constitutional Court could only decide on constitutional matters and issues associated with constitutional matters. After the amendment, the Constitutional Court is no longer a specialist court dealing only with constitutional matters. However, the Constitutional Court still has exclusive jurisdiction as a court of first and final instance on the matters contained in section 167(4) of the Constitution.

The Constitutional Court consists of the Chief Justice of South Africa, the Deputy Chief Justice and nine other judges. The seat of the Constitutional Court is in Johannesburg, but if it appears to the Chief Justice that it is more convenient or practical or in the interest of justice to hold its sitting at a place other than Johannesburg, it may hold such sitting elsewhere. It is important to remember that any matter before the Constitutional Court must be heard by at least eight judges.

1.3.2 The Supreme Court of Appeal

The Supreme Court of Appeal (which, before 1997, was known as the Appellate Division) is a court of appeal for the High Court and its various divisions. Its appeal jurisdiction is unlimited, with the exception of matters within the exclusive jurisdiction of the Constitutional Court. Since it is a court of appeal for the various divisions of the High Court, it has jurisdiction to hear appeals on matters which fall within the jurisdiction of this court. The Supreme Court of Appeal consists of the President of the Supreme Court of Appeal, the Deputy President of the Supreme Court of Appeal and as many judges as are necessary in accordance with the prescribed criteria, and approved by the President. The seat of the Supreme Court of Appeal is in Bloemfontein, although the court may sit elsewhere if it is more convenient or practical to do so by reason of exceptional circumstances.

1.3.3 The High Court

The Superior Courts Act 10 of 2013 came into operation on 23 August 2013. This Act created a single High Court in South Africa, with various divisions constituted in terms of section 6 of the said Act. In other words: section 6 of the Superior Courts Act stipulates that there is only one High Court in South Africa, with the following divisions:

- Eastern Cape Division, with its seat in Grahamstown

- Eastern Cape Local Division, with its seat in Bhisho
- Eastern Cape Local Division, with its seat in Mthatha
- Eastern Cape Local Division, with its seat in Port Elizabeth
- Free State Division, with its seat in Bloemfontein
- Gauteng Division, with its seat in Pretoria
- Gauteng Local Division, with its seat in Johannesburg
- Gauteng Division, with its seat in Pretoria (BUT functioning as Limpopo Division, with its seat in Polokwane)
- Gauteng Division, with its seat in Pretoria (BUT functioning as Limpopo Local Division, with its seat in Thohoyandou)
- Gauteng Division, with its seat in Pretoria (BUT functioning as Mpumalanga Division, with its seat in Nelspruit)
- KwaZulu-Natal Division, with its seat in Pietermaritzburg
- KwaZulu-Natal Local Division, with its seat in Durban
- Northern Cape Division, with its seat in Kimberley
- North West Division, with its seat in Mahikeng
- Western Cape Division, with its seat in Cape Town.

Each division of the High Court consists of a Judge President and one or more Deputy Judge Presidents. Moreover, each division of the High Court consists of as many judges as are necessary in accordance with the prescribed criteria, and approved by the President.

The High Court has original jurisdiction and can hear any matter which arises within its area of jurisdiction. The High Court is the only court that has jurisdiction to give judgment on the following matters: divorce proceedings, the status of a person in respect of mental capacity, applications for the sequestration of a person's estate, the liquidation of a company, and the validity or interpretation of a will. The High Court also has jurisdiction in respect of certain constitutional matters: for example, it may decide whether any fundamental right entrenched in the Constitution has been violated.

1.3.4 Other courts of importance in the southern African context

Other courts may be important in the southern African context because of their Roman-Dutch legal heritage. Some of the judgments of these courts are also reported in *The South African Law Reports*:

(a) The Supreme Court (an appeal court) and High Court of Zimbabwe. The seats of these courts are in Harare.
(b) The Supreme Court (an appeal court) and High Court of Namibia. The seats of these courts are in Windhoek.

1.3.5 Officers of the superior courts

A registrar is appointed in each of the superior courts. The registrar and his or her assistants are responsible for the smooth functioning of the court. The registrar's

duties include the issue of process (summonses, warrants, et cetera), the enrolment of cases, the issuing of orders of court and the maintenance of records.

A number of sheriffs are appointed for each of the divisions of the High Court. It is the duty of the sheriff to serve process and to execute judgments and orders of court.

In some divisions of the High Court, there is a Master's office presided over by a Master. The Master has various administrative and quasi-judicial functions mainly concerning deceased and insolvent estates, the liquidation and judicial management of companies, and the affairs of persons under legal disability, for example minors and mentally disordered persons.

Brief mention must be made of legal practitioners. The legal profession in the Republic is divided into two main classes, namely, advocates and attorneys. The chief distinction between these classes is that advocates mainly appear in the Constitutional Court, the Supreme Court of Appeal and the High Court, whereas attorneys, apart from giving assistance in all sorts of non-litigious matters such as drawing up contracts and wills, mainly practise in the magistrates' courts. Moreover, an attorney can also be a notary (which means he or she can draw up and attest antenuptial contracts and other notarial deeds) and a conveyancer (which means he or she is entitled to prepare deeds of transfer of immovable property, certificates of title, mortgage bonds, et cetera for registration in a Deeds Office).

1.3.6 Magistrates' courts

Magistrates' courts are to be found in most towns in the Republic, but a magistrate has a very limited jurisdiction in comparison with that of the superior courts. A magistrate may not hear any of the matters which fall exclusively within the jurisdiction of the superior courts. The clerk of the court exercises more or less the same functions in the magistrate's court as does the registrar in the superior court, and the sheriff (previously messenger) of the magistrate's court has duties similar to those of the sheriff of the various divisions of the High Court.

1.3.7 Small claims courts

The small claims courts are intended to resolve minor civil claims in a prompt, affordable and simple manner without legal representation for the parties. Anyone — except juristic persons such as companies, close corporations and associations — may institute a claim. Sections 15 and 16 of the Small Claims Courts Act, 1984, provide that the small claims courts have jurisdiction to hear any civil matter to the amount of R15 000. It is important to remember that there are some matters that cannot be taken to the small claims court even if they involve amounts of R15 000 or less. Examples of these matters are —

- divorces
- matters concerning a will
- malicious prosecution
- wrongful imprisonment

- breach of promise to marry.

There is no magistrate or judge in a small claims court, since these courts' presiding officers are commissioners who are usually practising advocates or attorneys who act as commissioners at no cost. The parties in small claims court matters are not allowed legal representation when appearing before the court, but advice can be obtained from paralegals. Attorneys (lawyers) may only be used to prepare a party's case.

No appeal may be filed against the judgment or order of the small claims courts. However, the court proceedings may be referred to the High Court for review. Such a review will only be done on the following grounds: absence of jurisdiction by the court; bias, malice or corruption on the part of the commissioner, and gross irregularity pertaining to the proceedings.

1.4 The doctrine of *stare decisis*

1.4.1 Introduction

The judgments of superior courts are, as is evident from the above, one of the most important sources of the law. Consequently, their operation and effect on South African law must be examined.

Theoretically, the function of a judge is to state, interpret, and apply the existing law but not to make new law. Nevertheless, the effect of a judicial decision which gives a new interpretation to a statutory provision, or which abstracts, extends or adapts a common-law principle, is, in many cases, to create law. Law so created is termed 'judge-made law'. Because a later court does not depart lightly from the decisions of an earlier court, this judge-made law becomes an established legal rule.

The conclusion should not be drawn that a court or a judge purposefully sets out to create law. It remains the task of the judge merely to apply the law. If a judge is forced to conclude that the law is silent on the particular matter before him or her and that indeed no applicable principle exists, or that the statutory provision is manifestly wrong or completely antiquated, a new principle cannot be created, or an old principle replaced with a better one, however firmly the judge may believe this to be desirable. This task the judge must leave to the legislature. However, a principle of the common law can, in fact, be abrogated by disuse if it is no longer in accordance with modern views, and a judge may decide that such a principle no longer applies.

1.4.2 Application of the doctrine

Literally, the phrase *stare decisis* mean 'the decision stands'. Obviously, when a court gives a decision, the parties to the dispute concerned will be bound by the decision. But what is the effect of this decision on similar disputes which may arise in the future? Will the court, when it has to decide this new dispute, have to follow

the previous decision or will it be free to formulate its own principles and to ignore the previous decision?

Take, for instance, a new Act which has been passed by Parliament. It could happen that a dispute arises on the meaning of a certain word or phrase in that Act. A court is called upon to adjudicate this dispute and it interprets the word or phrase in a certain way. Its decision is then binding on the parties who brought the dispute before the court, but what would the position be if this same word or phrase had to be interpreted later by another court? Strict adherence to the doctrine of *stare decisis* would mean that the later court would be bound by the earlier decision regardless of whether or not the earlier decision could be regarded as correct. This approach would lead to legal certainty, but it would sometimes be attained at the expense of a fair decision. At the other extreme the view exists that each case should be decided on its own merits and that earlier decisions

on the point in question should be ignored. While this approach would possibly lead to fairer decisions in some cases, it would also lead to legal uncertainty — which has grave disadvantages.

Not surprisingly, South African courts observe neither of these extremes and follow a middle course in this regard.

A court is bound by its own decisions unless and until they are overruled by a superior court. But it is conceivable that circumstances may arise which would render it possible for a court to override its own legal opinion. Such exceptional circumstances would be where the previous decision is clearly shown to be wrong.

That court decisions are binding in this manner has never been laid down by statute. Accordingly, the rule of *stare decisis* is itself an example of how the courts operate to create law. Nowadays the courts are bound by earlier decisions simply because they laid down the rule of *stare decisis* in earlier cases and adopted it in subsequent judgments.

As emerges from the above, *stare decisis* applies in South African law, but in appropriate cases it is possible to depart from the decision of an earlier, and even of a superior, court.

1.4.3 The doctrine of *stare decisis* and the hierarchy of courts

The position may be summarised as follows:

(a) Every court is bound by the decisions of the superior court within its area of jurisdiction, unless the decision of the superior court is based on so obvious an error, such as failure to take into account a statutory provision, that there can hardly be any difference of opinion on the matter. Thus, a division of the High Court, whether it is a full bench consisting of three judges, a bench of two judges or only of one, is bound by the decisions of the Constitutional Court and the Supreme Court of Appeal; a bench of two judges is bound by a decision of the full bench, and a single judge by the decisions of a bench constituted in either of the two ways mentioned above.

(b) Every court is bound by the decision of a court of concurrent status within its own area of jurisdiction, unless it is convinced that the earlier decision was

incorrect, even though the matter may permit a difference of opinion. Thus preceded the Supreme Court of Appeal is bound by its previous judgments (even a bench of five judges, by a bench of three), unless persuaded that the earlier judgment or line of decisions was patently wrong. A full bench of the High Court is similarly bound by an earlier full-bench decision, a bench of two judges by an earlier decision of a two-judge bench, and a single judge by an earlier decision of another single judge. A departure from an earlier decision takes place only on very good grounds.

(c) One division of the High Court is not bound to follow the decisions of other divisions of the High Court, since they belong to different areas of jurisdiction. Hence, a single judge of the division of the High Court in Johannesburg is not bound to follow the decision of the full bench of, for example, the division of the High Court in Bloemfontein. Nevertheless, a court, no matter how it may be constituted, will not depart from the decision of another division of the High Court without good reason, since a great deal of persuasive authority attaches to such a decision.

(d) Magistrates' courts are bound by the judgments of the Constitutional Court, the Supreme Court of Appeal and the High Court. If the judgments of the divisions of the High Court are conflicting, a magistrate should follow the decision of the division of the High Court in whose jurisdiction that magistrate's court falls. In general, one magistrate does not necessarily follow the judgments of another magistrate, if for no other reason than that the judgments of magistrates' courts are not reported.

1.5 Interpretation of statutes

Statutory interpretation is used when the meaning in law of an Act of Parliament or another piece of legislation must be determined. Words can be ambiguous or imprecise, despite careful drafting of the Acts, and then various theoretical rules and methods are used to interpret what the statute seeks to achieve. This is not vague guesswork or a subjective interpretation of what the law should be. Rather, this exercise has been defined as a dynamic and functional process through which the text of the legislation and the contextual factors surrounding it are objectively researched to determine the purpose of the legislation and give effect to it in the light of the principles prescribed by the Constitution.

1.5.1 The relationship between the *stare decisis* rule and the interpretation of statutes

South Africa's tripartite separation of powers has the result that, theoretically, Parliament makes laws while the judiciary applies them. But nothing is ever quite that clear-cut. A study of the *stare decisis* rule will have shown that one of the sources of law is the decisions of the judiciary on what the law is. So an interpretation by a court of the meaning of a piece of legislation, coupled with the precedent system, means that other courts are bound by that legislation as

interpreted by the court, until a superior court places a different interpretation on it, or the legislature amends it. This does not mean that the courts determine statute law — their function is to interpret and apply a statute without amending or altering its provisions. It does, however, mean that a lower court applies a higher court's interpretation of the wording of an Act, rather than applying the wording of the Act itself.

1.5.2 The influence of the Constitution on the interpretation of statutes

Before the advent of the Constitution, statutes were interpreted according to the provisions of the Interpretation Act 33 of 1957 and set rules and principles deriving from common law. The Constitution is now the fundamental and supreme law of the country, and any statute that conflicts with the Constitution, whether promulgated before or after

the Constitution, can be declared invalid. The Constitution also sets out guidelines for interpreting statutes so as to determine whether they conflict with the Constitution. Most importantly, section 39(1) states that, when interpreting the Bill of Rights, a court must promote the values that underlie an open and democratic society based on human dignity, equality and freedom; must consider international law; and may consider foreign law. Courts are instructed to look outside the words of a specific statute when trying to determine its purpose and meaning. The values and norms on which the Constitution is based must now be taken into account.

Section 39(2), then, provides that, when interpreting any legislation, a court must promote the spirit, purport and objects of the Bill of Rights. In addition, section 233 states that, when interpreting any legislation, every court must prefer any reasonable interpretation that is consistent with international law over any alternative and inconsistent interpretation.

1.5.3 General principles

Two of the most important other principles when interpreting legislation are:

(a) The meaning of a provision must be determined by its language and its context in the legislation read as a whole.

(b) Any reasonable interpretation of a provision that is consistent with the purpose and scope of that legislation must be preferred over any alternative interpretation that is inconsistent with its purpose and scope.

1.5.4 The Interpretation Act 33 of 1957

The Act applies to the interpretation of every law. It contains general definitions of terms frequently used in legislation, rules about gender (the masculine includes the feminine), numbering, calculation of time, measurements of distance and the commencement and repeal of legislation.

1.6 Court judgments

1.6.1 *Ratio decidendi*

The most important part of a judgment is what is called the *ratio decidendi*. *Ratio decidendi* literally means 'the reason for the decision' and it is the *ratio decidendi* of a case which is binding and which is the subject of the doctrine of *stare decisis*. As indicated, the actual parties to the case are bound by the decision. But if entirely different parties involved in a similar set of facts come before the courts, the courts will, as a general rule, follow the previous decision and its *ratio decidendi*. In other words, when it is said that a decision is binding, this does not mean that every sentence uttered by the judge in deciding the case must be considered as imposing a rule of law.

The first step is to determine the material facts on which the judge based the decision. This is not such a simple task, but once the facts have been determined, the *ratio decidendi* is the conclusion reached by the judge based on these material facts and by excluding the immaterial ones.

1.6.2 *Obiter dictum*

The *ratio decidendi* is binding on subsequent courts. Any statement which falls outside the *ratio decidendi* is known as an *obiter dictum* (or incidental remark). It may be encountered when the principle of the case is formulated by the judge more broadly than is necessary to cover the facts; when the judge makes an incidental remark; postulates and answers a hypothetical question; raises an analogous case, or gives an illustration. Suppose the hypothetical question actually occurs at a later date. Is the next judge bound by the opinion expressed by his or her predecessor? The answer to this is no. Any remark which is irrelevant to the immediate settling of the dispute is *obiter* (by the way). It does not form part of the *ratio decidendi* and is not binding on subsequent courts, because it cannot be ascertained whether this particular point was properly argued and whether its full implications were properly considered. One could also say that the reasons given by a judge in a minority judgment are *obiter*, since they are not an essential link in the process which leads to the ultimate conclusion. Any *obiter dictum*, although not binding, may, of course, have strong persuasive authority. Once such an *obiter dictum* is actually applied by a later court, it thereby becomes the *ratio decidendi* of the later decision and thus becomes binding.

1.6.3 Distinguishing

A judge distinguishes one case from another by deciding that the *ratio decidendi* of a previous decision is not binding on the case before him or her and, therefore, that the *ratio decidendi* of the first case does not apply. It is thus a technique which is used by a judge to avoid the binding force of an earlier *ratio decidendi*.

This may be done in various ways. The later court may, for example, be of the opinion that the earlier court formulated a principle too broadly; that the

consequences are unacceptable, and, thus, that the facts of the later case are not covered by the principle. The later court may also find that the earlier court did not take sufficient account of a fact which would have led to a different *ratio decidendi*, and, for this reason, may not follow the earlier decision. Or the later court may accept the earlier court's views and *ratio*, but may encounter a material fact which was not present in the earlier case, or find a fact in the earlier case missing from the later case; hence, the two cases would not be identical. It is only when two cases are identical regarding the material facts and the points in issue that it is impossible to distinguish the one from the other.

1.6.4 Typical aspects of a judgment

In order to illustrate the most important aspects of a judgment we refer to a case published in *The South African Law Reports — National Sorghum Breweries Ltd v Corpcapital Bank Ltd* 2006 (6) SA 208 (SCA). The name of the case contains certain information. The applicant, claimant or appellant in the case is National Sorghum Breweries Ltd. The letter '*v*' stands for versus, meaning 'against'. The name of the defendant or respondent, that is, the party against whom the case is brought, appears after the letter '*v*' — in this case, Corpcapital Bank Ltd. This is followed by the numbers 2006 (6), which mean that the case is reported in the sixth part of the 2006 law reports. 'SA' means that the case is reported in *The South African Law Reports*, while '208' denotes the page number on which the case is reported. '(SCA)' means that the case was heard in the Supreme Court of Appeal in Bloemfontein/Mangaung. Sometimes, when a case is cited, more numbers (for example [5] or 210D) are quoted after the division of the court. This number refers to the specific paragraph or page in the report where a particular statement appears.

G NATIONAL SORGHUM BREWERIES LTD v
CORPCAPITAL BANK LTD

SUPREME COURT OF APPEAL

MPATI DP, NUGENT JA, JAFTA JA, COMBRINCK AJA and MAYA AJA

H 2005 November 21 2006 February 23 Case No 50/2005

Contract—Interpretation—Particular situations—Cession—Subsequent cession of rights in terms of earlier agreement not constituting variation of earlier agreement and thus not governed by non-variation clause contained in latter.

I

In an action by the respondent as cessionary of rights enforceable against the appellant in terms of various lease agreements, the appellant raised

the defence that the rights concerned had not been validly ceded to the respondent. It did so on the basis that the two cessions upon which the respondent relied each constituted a variation of an earlier agreement which contained a 'non-variation clause' and the cession, in each case, failed to comply with the formalities prescribed by that clause. The High Court dismissed the appellant's defence. The Court of Appeal found the cessions not to constitute variations of the earlier agreements, and thus not to be governed by the 'non-variation clauses' and, consequently, that the defence had been correctly dismissed. (Paragraphs [15], [16] and [18] at 212H–213D and 213F.)

The decision of Cachalia J, in the Witwatersrand Local Division, in *Corpcapital Bank Ltd v National Sorghum Breweries Ltd*, confirmed.

Annotations:

Reported cases

Aussenkehr Farms (Pty) Ltd v Trio Transport CC 2002 (4) SA 483 (SCA): not followed

Traub v Barclays National Bank Ltd; Kalk v Barclays National Bank Ltd 1983 (3) SA 619 (A): referred to.

Appeal from a decision in the Witwatersrand Local Division (Cachalia J). The facts appear from the reasons for judgment.

G I Hoffman SC (with *A Kemack*) for the appellant.

A O Cook SC (with *E F Dippenaar*) for the respondent.

Cur adv vult.

Postea (February 23).

Jafta JA:

[1] As a general rule, a creditor is free to cede its rights in whatever form it chooses. It does not need its debtor's consent nor is it necessary for it to give notice to the debtor. But this power can be restricted by means of a contract to which the creditor is a party. In that case the creditor would be required to comply with the terms of the restriction when ceding its rights. The issue in this appeal is whether the creditors' powers to cede rights were restricted by non-variation clauses contained in contracts they had concluded with third parties.

[2] The respondent, Corpcapital Bank, instituted an action against the appellant (which I will refer to as the defendant) in the Johannesburg High Court for the recovery of damages arising from the alleged breach of various lease agreements. Corpcapital Bank was formerly known as Fulcrum Science and Technology Bank Ltd and was, at times, referred to simply as Fulcrum Bank, but, for convenience, I will refer to it throughout this judgment as Corpcapital Bank.

[3] Corpcapital Bank instituted the action in its capacity as the cessionary of the rights in various lease agreements (referred to in the evidence as 'full maintenance rental agreements') that were concluded between the defendant and a company called Afinta Financial Services (Pty) Ltd (Afinta Financial Services). In terms of those agreements the latter company leased vehicles to the defendant. The defendant challenged Corpcapital Bank's right to sue, contending that the rights of Afinta

A Financial Services had not been validly ceded. The Court *a quo* (Cachalia J) was asked to determine that issue separately from the other issues. It dismissed the defence with costs and the defendant appeals against that order with the leave of the Court *a quo*.

[4] The facts are briefly these. Afinta Financial Services carried on a B vehicle leasing business and leased vehicles to various customers, including the defendant. In February 1999 Afinta Financial Services and Corpcapital Bank Ltd became parties to a joint venture that was to continue the leasing business. The joint venture was to be conducted through the medium of a company called Afinta Finance Ltd (Afinta C Finance) that was owned by the joint venturers.

[5] The joint venturers agreed that at the outset Afinta Financial Services would transfer certain of its existing lease agreements to Afinta Finance and that it would thereafter direct all new business to Afinta Finance. The business was to be financed by loans to be made to Afinta D Finance by Corpcapital Bank that were to be secured by a cession to Corpcapital Bank of the debtors of Afinta Finance.

[6] To that end the various parties signed two standard-form agreements referred to as 'Master Cession Agreements' on 26 February 1999. One purported to be a cession from Afinta Financial Services to Afinta E Finance. The document, however, reflected a cession *in securitatem debiti* when the intention was to effect an out-and-out cession. The other cession between Afinta Finance and Corpcapital Bank correctly reflected a cession *in securitatem debiti* as intended by the parties. Both agreements were substantially the same and provided for the cession from the cedent to the cessionary of F

'the [lease agreements] listed on a document completed and signed by the cedent in the form of the schedule annexed hereto as annexure A'.

Each agreement contained a non-variation clause in the following terms:

'1. No variation, alteration, consensual cancellation, addition to or novation of G this cession and no waiver by [the cessionary] of any of its rights hereunder shall be of any force or effect unless reduced to writing and signed by [the cessionary's] authorised representative and [the cedent or the cedent's] duly authorised representative.'

[7] The lease agreements that were to be transferred at the outset had to meet the credit criteria of Corpcapital Bank. For purposes of identifying H such agreements, a firm of auditors was appointed to conduct a due diligence investigation, which was completed only in June 1999. By then, Afinta Financial Services and Afinta Finance were no longer satisfied that the master cession they had signed on 26 February 1999 was an appropriate instrument for achieving their purpose, probably because they realised that the master cession had been a cession *in securitatem* I *debiti* and not an out and out cession. As a result, a new agreement (which they referred to as a 'sale' agreement) was concluded by Afinta Financial Services and Afinta Finance on 14 July 1999.

[8] The sale agreement provided in clause 1 as follows:

J '[Afinta Finance] hereby purchases from [Afinta Financial Services] all right,

title and interest in and to the Vehicle Finance debts set out in column F of annexure A hereto ("debts") and all of its claims and rights of action against the debtors set out in column D of annexure A hereto ("debtors") including the cession and transfer of all rights in and to the debts.'

It also incorporated, by reference to another agreement that the parties had concluded, a non-variation clause in the following terms:

'1. No amendment or consensual cancellation of this agreement or any provision or term thereof or of any agreement or other document issued or executed pursuant to or in terms of this agreement and no settlement of any disputes arising under this agreement and no extension of time, waiver or relaxation or suspension of any of the provisions or terms of this agreement or other document issued pursuant to or in terms of this agreement shall be binding unless recorded in a written document signed by the parties.'

[9] Attached to the sale agreement as annexure A was a list of about 80 lease agreements that had been concluded between Afinta Financial Services and its customers, included among which were 11 lease agreements with the defendant.

[10] Subsequent to the conclusion of the sale agreement some debts that had been 'sold' were found to be irrecoverable and, by agreement between Afinta Financial Services and Afinta Finance, a list was prepared of other lease agreements that were to be ceded in their stead. Later, a further list was compiled under similar circumstances. Those lists between them reflected seven further lease agreements with the defendant. Neither of the lists was signed by either Afinta Financial Services or Afinta Finance.

[11] Earlier I pointed out that a 'master cession' was signed by Afinta Finance and Corpcapital Bank on 26 February 1999, in contemplation of the cession of debts from the former to the latter as security for loans that were to be advanced by Corpcapital Bank. Because the rights that were to be transferred by Afinta Financial Services to Afinta Finance at the outset—and thereafter ceded to Corpcapital Bank—had yet to be identified, the master cession naturally did not reflect any ceded debts at the time the document was signed. But once the relevant lease agreements had been identified, and Afinta Financial Services had purported to transfer them to Afinta Finance, various schedules were prepared purporting to record a cession of the rights in those agreements to Corpcapital Bank pursuant to the master cession. In February 2000 those schedules were consolidated into a single schedule. It is not disputed that the consolidated schedule was signed on behalf of Afinta Finance, but it was not signed by or on behalf of Corpcapital Bank. Amongst the lease agreements reflected on the schedule were the 18 lease agreements with the defendant to which I referred earlier and those lease agreements are the subject of the action with which this appeal is concerned. It is alleged that the defendant breached the agreements, with resultant damage, which Corpcapital Bank seeks to recover as cessionary.

[12] The argument advanced on defendant's behalf, both in this Court and the Court below was that there was no valid cession of debts from

A Afinta Financial Services to Afinta Finance in respect of the seven lease agreements that were not reflected in the original annexure to the 'sale' agreement because, so it was contended, the purported addition of those lease agreements constituted a variation of the 'sale' agreement that did not comply with the formalities of the non-variation clause in the sale
B agreement. Moreover, it was argued on behalf of the defendant that there was no valid cession by Afinta Finance to Corpcapital Bank of the rights arising from any of the 18 lease agreements because the later addition of the schedule constituted a variation of the master cession that similarly did not comply with the required formalities.

C [13] The Court *a quo* found that the purported cession to Afinta Finance of the seven lease agreements, and the purported cession to Corpcapital of all 18 lease agreements, constituted amendments of the 'sale' agreement and the master cession, respectively. It went on to find, however, relying on a remark to that effect in *Aussenkehr Farms (Pty) Ltd v Trio Transport CC* 2002 (4) SA 483 (SCA) at 494A,[1] which the learned Judge
D considered to be binding upon him, that the non-variation clauses in each case could not be relied upon by a third party (the defendant) where 'the parties to the agreement (the cedent and the cessionary) were not relying on the provisions of their contract requiring written variations or amendments'. In the circumstances, the learned Judge concluded, it was
E 'not open to the defendant to attack the *consensus* achieved by Afinta Finance and Afinta Financial Services (and, similarly, the *consensus* achieved between Afinta Finance and Corpcapital Bank) and, as a third party, to insist upon formalities between them'.

F [14] I have some doubt that contractually created rights and obligations may vary depending upon the perspective from which they are viewed. The remark to that effect in *Aussenkehr Farms*, which the learned Judge relied upon, was clearly *obiter*, and may also have overlooked the earlier decision of this Court in *Traub v Barclays National Bank Ltd; Kalk v Barclays National Bank Ltd* 1983 (3) SA 619 (A) at 631E–633A in which
G the topic was more extensively considered, albeit in another context. But it is not necessary to consider that issue further in the present case because, in my view, the Court *a quo* erred, in any event, in relation to the construction of the various agreements.

[15] The 'sale' agreement between Afinta Financial Services and Afinta
H Finance regulated the transfer of the rights in the lease agreements referred to in the annexure (annexure A). Their later agreements—concluded by their conduct in preparing the two further lists when seen in the context in which they did so—to transfer the rights in seven further leases did not purport to amend any of the terms of the former transaction. They were no more than later transactions in similar terms,
I which the sale agreement did not preclude them from concluding, and which required no formalities to be valid. The defendant's reliance on

[1] '. . . (I)f the parties were not contending that a written termination was needed it was not open to the defendant to argue invalidity of the act.'

J

the non-variation clause in the 'sale' agreement was quite misconceived because no amendment to that agreement purported to be effected at all. It follows that the rights relating to all 18 vehicles leased to the defendant were properly transferred to Afinta Finance.

[16] Similarly, the master cession concluded between Afinta Finance and Corpcapital Bank on 26 February 1999 did not purport to preclude the parties from ceding rights in the future. Indeed, the master cession contemplated that future cessions would be effected, and its very purpose was to regulate the terms that would govern those cessions. What was required to effect such future cessions on the terms agreed to in the master cession was no more than that the relevant lease agreements should be listed in a schedule compiled and signed by Afinta Finance, which is what occurred in relation to the 18 lease agreements that are now in issue. The parties did not thereby purport to vary or alter, or even add to, the master cession. On the contrary, they purported only to give the master cession its intended effect.

[17] It was also submitted on behalf of the defendant that Corpcapital Bank's pleaded case did not rely upon cessions effected by the parties subsequent to the conclusion of each of the written agreements. That is not correct. On the contrary, the very case that Corpcapital Bank pleaded was that the relevant cessions were effected subsequent to the conclusion of the respective written agreements. Indeed, it is difficult to see how its case could have been pleaded in any other form.

[18] In the circumstances the Court *a quo* correctly dismissed the defence, albeit on incorrect grounds. The appeal is dismissed with costs, including costs occasioned by the employment of two counsel.

Mpati DP, Nugent JA, Combrinck AJA and Maya AJA concurred.

Appellant's Attorneys: *Lennard Cowan*, Sandton; *Lovius Block*, Bloemfontein. Respondent's Attorneys: *G B Liebmann Behrmann & Co*, Houghton Estate; *Claude Reid Inc*, Bloemfontein.

The case was heard on 21 November 2005 before Deputy President of the Supreme Court of Appeal Mpati, Judges of Appeal Nugent and Jafta, and Acting Judges of Appeal Combrinck and Maya. Judgment was delivered on 23 February 2006. The names of the advocates are also given. The letters 'SC' after the advocate's name stand for *Senior Consultus* and indicate that the advocate is a senior counsel. After this information a somewhat cryptic résumé of the case, the so-called flynote, appears which is of little value except to someone who wishes to find out what the case is about in bare outline. In this instance the case is about the interpretation of a contract. A reader whose subject is commercial law will peruse the report but someone interested in criminal law, for example, will read no further.

The head-note follows in small print. This is a summary of the gist of the judgment, the material facts (if they are of importance), the principle applied, and

what was decided. This summary is made by the editors of the law reports: it has no official status and is only an aid to reading the judgment.

Sometimes the word '*semble*' or '*aliter*' appears, followed by a statement.

'*Semble*' means 'this appears to be the case according to the judgment, although the point has not been settled': for example, because it is *obiter* or because there is strong authority against it. '*Aliter*' literally means 'otherwise', and suggests that the decision would be different if the facts mentioned were either added or fell away. 'Followed' or 'applied', with a reference to the name of a decision, means that that decision was followed with or without a discussion thereof; 'confirmed' means that the case mentioned was accepted as good authority by a court which could have overthrown it; 'approved' that the court accepted the other judgment as good authority without having been in a position to overthrow it, for example, because it was the decision of a different division. 'Overruled' means that a court with the power to overthrow this decision has, in fact, done so, with the result that it can no longer be accepted as good authority, and 'dissented from' indicates that a court without the power to reject the earlier decision nevertheless regarded it as incorrect. 'Not followed' means that a court decided not to follow a decision. The reference to *Aussenkehr Farms (Pty) Ltd v Trio Transport CC* 2002 (4) SA 483 (SCA) serves as an example of this. 'Reversed' means that an appeal has succeeded, and 'distinguished' that a court which would otherwise have been bound by a previous decision has, in some way or other, distinguished it, as described above, and therefore has not followed it. 'Compared and discussed' or 'referred to' simply means that the court brought in another decision by way of analogy, without necessarily expressing an opinion on its correctness. The reference to *Traub v Barclays National Bank Ltd; Kalk v Barclays National Bank* 1983 (3) SA 619 (A) is an example of this.

Following the head-note there is an indication of the type of case, whether it is an appeal, an action, a review, an application, et cetera. This case is an appeal against the decision of Judge Cachalia in the Witwatersrand Local Division (now the Gauteng Local Division, Johannesburg) and his judgment was confirmed by the Supreme Court of Appeal.

This is followed by the words '*Cur adv vult*'. This simply means '*curia advisari vult*', or, the court wishes to consider its decision. This is followed by the word '*Postea*' (afterwards), the date on which the judgment was eventually delivered, and the judgment itself. The judgment ends with the order issued by the judge. If there is more than one judge, the name or names of the judge or judges who concurred (or differed) with the judgment are given, followed by the names of the respective attorneys.

Further reading

AB Edwards *The History of South African Law: An Outline* (1996).

D Kleyn & F Viljoen *Beginner's Guide for Law Students* 4th ed (2010).

Chapter 2
Introduction to the Science of Law

2.1 The term 'Law'
2.2 Private Law

2.1 The term 'Law'

The history of law reflects the history of mankind, because any society has a need for rules to govern relations between people. In modern times this need has become greater and the application of legal rules has become more extensive.

Consider an ordinary day in the life of John Citizen. He has probably purchased, and owns, his breakfast cereal. The name and packaging of that cereal belong to someone, and no one else is entitled to use them. He pays a fare when he goes to work by train. He enters the office or factory at his place of work as an employee. The enterprise for which he works may be a company which has issued shares, the holding of which by the public entails membership of the company and a say in the running of its affairs. Family relationships, and relationships between consumer and trader, employer and employee, citizen and state and numerous other relationships are all affected by the law in one way or another.

The purpose of legal science is to study and evaluate of the aforementioned relationships. This is done by the delimitation and classification of rules relating to a particular aspect. In this regard the meanings attached to the words 'law' and 'right' must be noted. The law refers to a system of rules which apply in a community. A right is any right which a legal subject has regarding a specific legal object and which is protected by law.

2.1.1 The meaning of law

The legal cosmos can be made comprehensible only if it is mapped out, boundaries are drawn, and significant features pointed out. Traditionally, the most important division of law is between public law and private law. It should immediately be clear that this division is not absolute and that a certain amount of overlap will occur.

Public law consists of those legal rules which control the relationships between the state and its citizens. Private law, in turn, consists of those legal rules which govern the relationships between citizens in their dealings with each other. Certain subdivisions can be made within these two categories: for example, public law can be subdivided into international law, constitutional law, administrative law,

criminal law and law of procedure. Private law can be subdivided into the law of persons, family law, law of personality and patrimonial law.

A further category apart from those of public law and private law is that of commercial or mercantile law. It is not easy to define commercial law since the origin and content of the subject can be better explained on historical grounds than it can be determined in principle. The term 'commercial law' usually refers to those legal rules which, although of a divergent origin and nature, nevertheless have in common that they arose from the customs of merchants or which relate to business activity.

Because commercial law cannot be distinguished from other branches of the law on the basis of principle, it is difficult to indicate the subjects which fall under it. The following may be classified under commercial law: contracts of sale, lease and credit agreements, negotiable instruments, insolvency, companies, partnerships, close corporations, agency, security, insurance, contracts of transportation, labour law, intellectual property law, competition law, consumer law and tax law.

The rules of private law which are important for an understanding of commercial law are explained below.

2.1.2 The meaning of right

A right is any right which a legal subject has regarding a specific legal object and which is protected by law. Such a legally protected right is referred to as a subjective right. The nature of legal subjects, 'legal Objects' and 'Subjective Rights' is determined by objective law. The terms 'legal object' and 'legal subject' are often encountered in legal literature. The meaning of these terms will now be discussed in some detail.

2.1.2.1 Legal subjects

A legal subject is a human being or entity subject to the law: a member of the legal community to whom the law applies and for whose benefit the law exists. Every legal subject has legal capacity, that is, the capacity to be the bearer of rights and duties.

But who are legal subjects? First, it should be noted that in law all legal subjects are called 'persons'. Today, the law recognises two categories of persons, namely natural persons and juristic persons. It should also be noted that in law the concepts 'human being' and 'person' are not synonymous. 'Person' and 'legal subject' are, however, synonymous.

(a) Natural persons

The concept of a natural person refers to a human being. Every human being, from a new-born baby to an adult, is a legal subject, and every human being can have rights and duties. For instance, the law protects the physical integrity and honour of a new-born child, and also determines that he or she can inherit property.

(b) Juristic persons

As a result of the requirements of legal and commercial intercourse, the law is obliged to recognise as legal subjects entities other than human beings. This does not mean that these entities acquire the natural personality of human beings or that they have a physical existence, but merely that these entities are recognised as holders of rights and powers and are subject to duties. These entities are elevated by the law to the status of juristic or artificial persons, but not to that of natural persons.

A company, university, municipality, and the state are all examples of juristic persons. One of the features of a juristic person is that it has rights and is subject to duties; another feature is that it has perpetual succession. This means that although the individuals who comprise the juristic person may die, the juristic person continues to exist.

To elucidate the concept of a 'juristic person', the trading company is used as an example. If Bill and Bob establish a company called BB Investments (Pty) Ltd, and Bill and Bob are the only shareholders and directors of BB Investments, this means that legally there are three persons. If the company has two motor cars, this does not mean that Bill owns one and Bob the other. Both cars belong to the company alone. If Tom wants to buy one of the cars, he has to conclude a contract with the company. The company will then be entitled to the purchase price. Bill and Bob will, of course, enter into the contract in the name of the company. Their role in this case is that of representatives of the company. However, they themselves are not the company, since the company is purely an imaginary concept. If Bill and Bob were to die, BB Investments would continue to exist. If Bill sells his share to Tom, the company is still BB Investments. The position is the same in the case of the other juristic persons that have been mentioned. The company is thus a legal reality.

The company is one of the most important kinds of juristic person. The member of a company, or shareholder, has no ownership or other real right in the property of the company. A member or shareholder merely has a personal right to claim a share of the profits of the company if a dividend is declared, or to claim a share of the surplus assets of the company if it is liquidated. Moreover, if a company is caused loss unlawfully, the company, but not individual shareholders, has an action for redress against the person who caused the loss. Conversely, the company is liable for the company's debts and the shareholders cannot be sued for them.

2.1.2.2 Legal object

A legal object is any entity which can be the object of a legal subject's claim to a right. In general, property, intellectual property, aspects of personality and performances can be the objects of a legal subject's claim to a right.

2.1.2.3 Subjective right

The relationship between a legal subject and a legal object, as well as that between a legal subject and other legal subjects, can be termed a right. All rights can in

some or other way be linked to a legal object. The following categories of juridical rights can be distinguished when rights are classified according to the particular legal object:

(a) A real right is a right which a legal subject has to property, such as a book, a pencil or a table. Real rights can be classified as follows:
   (i) Ownership — the most comprehensive real right of all.
   (ii) Servitudes, which are subdivided into:
      - Praedial servitudes — they confer on the holder, in his or her capacity as owner of an adjacent property, a limited right to the property of another, for example the servitude of grazing

- Personal servitudes — they confer on a person, in his or her personal capacity, the right of use and enjoyment of property of which another is the owner, for example usufruct.

(iii) Mortgage and pledge — they confer on their holder (the creditor) a right of security in respect of the property mortgaged or pledged. This right of security entitles the mortgagee or pledgee to have such property sold if the debtor (mortgagor or pledgor) fails to settle the debt secured by the mortgage or pledge.

(b) Intellectual property rights are rights to intellectual property: for example the artist's right to works of art, the writer's right to literary works, the inventor's right to inventions and the designer's right to designs.

(c) Personality rights are rights relating to aspects of personality: for example the physical integrity or reputation of a person.

(d) Personal rights (which should not be confused with personality rights) are rights in terms of which some or other conduct, referred to as 'performance', may be demanded from a person. Performance can consist in giving something, doing something, or refraining from doing something.

2.2 Private law

2.2.1 The law of persons

The law of persons is that part of private law which regulates the conception, the existence, and the termination of the natural person as a legal subject. The law of persons thus determines —

(a) who are legal subjects
(b) how one becomes or ceases to be a legal subject
(c) the various classes of legal subjects
(d) what the legal position (status) of each of these various classes of legal subject is.

It has already been indicated that every human being can be the bearer of rights and duties. Every human being is therefore a legal subject.

At what stage does a human being become the bearer of rights and duties? In other words, when does the legal capacity (that is, the attribute of having rights and

duties in the eyes of the law) of a human being come into existence? The answer to these questions appears to be that a human being and its legal capacity come into existence at birth. The rights of an unborn child are, however, also protected provided that the child is subsequently born alive.

The legal capacity of a person is terminated by death; a deceased person can have neither rights nor duties. Nevertheless, the law protects the body as well as the deceased's former assets. However, the protection is not in the interests of the deceased: the body is protected in the interests of the community, and the deceased's former assets are protected in the interests of his or her creditors and heirs. Thus, in both cases protection is given to the interests of legal subjects, and not to the deceased, who is no longer a legal subject.

Since legal subjects differ from one another, the law is also obliged to draw distinctions between them. For example, minors do not have the same rights as adults. To give recognition to these distinctions, status is accorded to every legal subject. Status is defined as the aggregate of rights and duties which are attached to a person as one of a specific class. Status is a legal condition: it is the position occupied by a legal subject in relation to his or her fellow legal subjects as a member of a particular class in the legal community. It is thus the position enjoyed by a person in the eyes of the law. It determines the extent of the rights and duties a legal subject may have.

Status is conferred by the law. A person's status cannot be changed of his or her own accord, apart from the exceptional cases in which the law allows a change in status to follow on certain steps taken by the person, for example in the case of marriage. It should be noted, furthermore, that status can take various forms. A distinction is drawn between status in public law and in private law. The capacity to vote, for example, arises out of a person's public law status. All South African citizens over the age of 18 are entitled to vote. The capacity to acquire ownership is derived from private-law status.

There are numerous factors which determine the status of a legal subject, such as age, sex, marital status and sanity. The law of persons is concerned specifically with the influence exerted by all these factors on the status of a legal subject.

2.2.2 Family law

The law of the family is that part of private law which has to do with the requirements for the conclusion of a valid marriage, the legal consequences of marriage, the grounds on which a marriage can be dissolved, and the legal relationship between parents and children. The law of the family has nothing to do with the relations between relatives, for example uncles and cousins or in-laws. It is concerned only with the two parties to a marriage (the law of husband and wife) and with the relationship between parents and children (the law of parental authority). The law of the family thus comprises two subdivisions, the law of husband and wife, and the law of parent and child.

2.2.3 Law of personality

Persons have certain rights in respect of their physical being, their dignity and their reputation. Thus, for example, everyone has a right not to be unlawfully assaulted. This right is protected by both criminal law (assault is a crime) and civil law (the assaulted person can sue the perpetrator for damages in delict). Similarly, everyone also has a right not to be insulted or defamed.

The law of personality is concerned with the relations between people concerning their physical and psychical integrity. It ensures that each person has the undisturbed enjoyment of his or her personality property within the limits laid down by the legal order, and, under certain conditions, compels anyone who has infringed this right to pay a sum of money as compensation. From general experience it is known that whoever

says defamatory things about another (infringes the other's right to his or her reputation) may be compelled to pay a sum of money to the injured party. An important right of personality is the right of privacy: every person is entitled to live a private life and if another intrudes on his or her domestic sphere without permission, or displays a photograph of the person, the right to privacy is infringed. Here, an interesting and important question is, when may one do these things? Rights of personality, like all other rights, are subject to limitations. A politician, therefore, cannot complain if he or she is caricatured in a cartoon.

2.2.4 Patrimonial law

Here, the relations involved are between persons as regards their patrimony. A person's patrimony consists of all his or her rights and duties which may be valued in money: it is, therefore, the sum of his or her assets and liabilities.

2.2.4.1 The law of property

The law of property is concerned with the relationships of persons towards material objects. The relationships of persons towards property are controlled by means of the granting and recognition of rights over property. The nature and extent of the legal power enjoyed by a person over property depend on the kind of real right held by that person. The different kinds of real rights confer different powers on their holders. The real right of ownership gives the holder of the right wide powers to use the property, to enjoy it, to destroy it, to sell it, and so forth. On the other hand, the more restricted right of pledge gives the holder of the right only the right to possess the property (which still belongs to the pledger) as security for his or her claim against the pledger. It is, of course, obvious that more than one real right can subsist in the same property. For example, Anna may have the right of ownership over a farm, and at the same time Bheki may have a right of usufruct over the farm, Carol a mortgage over it and Dolores mineral rights in respect of it. Accordingly, the holders of the various rights have certain powers over one and the same property, that is, the farm.

The right of ownership is the cornerstone of all real rights and, at the same time, the most comprehensive right. The right of ownership is also extremely important as far as the law of property is concerned, and a few aspects of this right which

have not yet been mentioned, such as the nature and acquisition of ownership, its protection, and the distinction between ownership and possession, will now be discussed.

2.2.4.1.1 The right of ownership

In principle, the right of ownership confers the most complete power over property. However, this in no way means that ownership confers unlimited or absolute control: an owner may not do what he or she likes with his or her property. The wide powers of the owner — to use, enjoy, destroy, or sell the property, and so on — are restricted by the dictates of public law and the rights of others. Examples of public restriction are sanitary regulations, building regulations, statutory provisions which prohibit the division of land under certain circumstances, traffic rules which the motorist must obey, et cetera. This means, for instance, that the owner of a piece of land cannot build as he or she wishes, or that the motorist cannot drive as he or she likes. Ownership is always restricted in the interests of the community.

An owner's rights may also be restricted by a neighbour's right of ownership. The owner of land, for example, may not excavate the land in such a way that a neighbour's land subsides or caves in. It should, therefore, be noted that although in theory the right of ownership confers comprehensive powers on its holder, it is nevertheless always restricted.

2.2.4.1.1.1 Ownership and possession

It is most important to distinguish clearly between ownership of property and possession of property. In everyday speech there is a tendency to use these two different concepts indiscriminately: for example, 'his possessions'; 'she possesses a house'; 'she is the possessor of a radio' used to mean 'the property of which she is the owner'; 'she is the owner of a house' (or 'she has the ownership of a house'); 'she is the owner of a radio'. Ownership and possession are two quite different concepts in law. A person who has the right of ownership over property is not necessarily the possessor of the property. Abdul, the owner of a motor car, may, for example, lend it to Bambi for a trip to Durban: Abdul has ownership of the car, but Bambi is in possession of it. Or Koos moves out of his house so that Gordon can repair it: Koos is the owner of the house, but Gordon is the possessor.

When is one actually in possession of property? At first glance this seems a fairly simple question. It is, however, a difficult and disputed problem. For present purposes it will be suffice it to say that possession has two elements, namely, the physical and the psychical. A person is in possession of property when he or she has physical control over it and, at the same time, has the required intention of possessing. The intention of possessing, that is, the physical attitude required by the law, is the intention of exercising physical control in one's own interests. In order to have physical control over property, direct and immediate control over it is not required. For example, if Abdul locks his car but takes the key with him he has physical control over the car, although he may be kilometers away from it.

A single example to illustrate the absence of the required intention to possess is the following: If Mpo holds Ned's jacket for a few minutes while the latter works on her car, Mpo has physical control over the jacket, but does not have the intention of possessing it, because she is not exercising the physical control in her own interests, but in the interests of Ned: in other words, she is not holding the jacket for herself, but for someone else. Mpo is therefore not in possession of the jacket.

2.2.4.1.1.2 The acquisition of ownership

The way in which ownership is acquired is considered in this section. The basic distinction encountered in this respect is that between original and derivative methods of acquiring ownership.

(a) Original methods of acquiring ownership

(i) Occupation

The most obvious and probably the oldest method of acquiring ownership is seizure or occupation. If one seizes property belonging to no-one, with the intention of becoming its owner, one acquires the right of ownership over the property: for example, when Andrew catches a wild bird or a fish from the sea, or picks up a fountain-pen someone else has thrown away, and keeps it for himself. Note, however, that one cannot by occupation become the owner of property belonging to another. If Sipho loses his fountain-pen he remains its owner and Tshepo will not be able to obtain ownership of the pen by occupation. However, if Sipho no longer has the intention of being the owner of the pen (he renounces his right of ownership), Tshepo can acquire ownership by appropriation or seizure. Occupation is called an original method of acquiring ownership because the new owner does not obtain the right of ownership from another, but establishes an original right of ownership.

(ii) Prescription

A person can become the owner of property by means of prescription if he or she has possessed it openly as if he or she were its owner for an uninterrupted period of thirty years. For example, if Mandla takes possession of a section of Baba's farm by allowing his cattle to graze on it, he may acquire ownership of that section, provided he has possessed it openly and as if he were the owner for an uninterrupted period of thirty years (section 1 of the Prescription Act 68 of 1969). In this way, an act which was initially unlawful (appropriation of another's property without permission) leads to the acquisition of the right of ownership. The question is why the law allows an owner to lose his or her ownership in favour of another in these circumstances. The most important consideration is that of legal certainty. If an owner allows another to take possession of his or her property for a long period, the impression is created to the outside world that the possessor is actually the owner. The impression that the possessor has the right of ownership

is upheld by the actual conferring of ownership on the possessor. Acquisition of ownership by prescription is an original method of acquiring ownership because the possessor does not obtain the previous owner's ownership, but establishes an original right of ownership after the original owner has lost ownership.

(b) Derivative methods of acquiring ownership

(i) Movable property

The most commonly encountered method of acquiring ownership, however, is by delivery of property. This method is applicable only to movable property, that is, property which can be physically moved from one place to another, for example motor cars, books or furniture. (Immovables are land and everything permanently attached to it, such as houses, trees or fences.) For instance, if Ulla and Fezile agree that Ulla will buy Fezile's car, Fezile remains the owner of the car. Ulla acquires ownership of the car only when Fezile delivers it to her, that is to say, puts her in control and possession of the car. Therefore, the mere entering into a contract of sale or donation does not cause the right of ownership over the property bought or donated to pass to the buyer or beneficiary; the seller or donor must first deliver the property to the buyer or beneficiary: However, it is not sufficient merely for physical transfer to take place. It must also be the intention of both the transferor and transferee that the right of ownership be transferred and acquired. If either party lacks this intention, ownership does not pass. For example, if Peter delivers a pen to Sam under the impression that he is lending it to Sam, and Sam receives the pen believing that Peter is giving it to him, it is clear that, while it is Sam's intention to obtain ownership, Peter certainly does not intend to transfer his right of ownership. Consequently, ownership does not pass to Sam. Delivery is a derivative method of acquiring the right of ownership, because the transferee obtains ownership from the transferor and does not establish an original right of ownership.

(ii) Immovable property

Obviously, the right of ownership over immovable property cannot be acquired by means of delivery, because a farm or plot cannot be transferred physically. Instead of delivery, registration of the transfer at a Deeds Office is required. Thus, if Ivy buys Dora's farm, Ivy acquires ownership of the farm only when it is registered in her name, even though she may already have paid Dora the full purchase price. Registration is also a derivative method of acquiring ownership, because the seller transfers his or her right of ownership to the buyer.

2.2.4.1.1.3 The protection of ownership and of possession

Ownership is protected primarily by granting the owner the remedy known as the *rei vindicatio*. With this action based on ownership the owner may reclaim his or her property from any person who is wrongfully in possession of it. For instance, if David steals Brad's pen and sells it to Cecilia, who thinks David is the owner of

the pen, Brad can reclaim the pen from Cecilia, in spite of Cecilia's good faith. The law thus accords particularly strong protection to the right of ownership. When someone damages or destroys property belonging to an owner, the owner can, in principle, claim damages from the perpetrator.

Just as ownership is protected, so is possession protected. If Lindiwe borrows Ram's car and refuses to give the car back to Ram on his return, and Ram takes his car back by force or against Lindiwe's will, the court will protect Lindiwe's possession by ordering Ram (the owner) to restore possession to Lindiwe. If Lindiwe reclaims possession, Ram's contention that he is the owner of the car will be irrelevant. In an action in which someone asks that the possession he or she has lost be restored, the court is not

interested in who the owner is, but only in the question whether the applicant was wrongfully deprived of possession. It is only when Ram has restored possession to Lindiwe that he, as owner, may claim the car from Lindiwe with an action based on ownership. He himself may not repossess the car against Lindiwe's will. This may sound strange, but there is a good reason for it. In order to prevent persons from using force in taking property claimed by them, mere possession of property is protected in the sense that no one (not even an owner) may deprive someone of possession against his or her will. The remedy with which possession is restored is called the *mandament van spolie*.

2.2.4.1.2 Servitudes

A (right of) servitude is a limited real right over the property of another, which confers on the holder of the right specific powers to use the property in a particular way. Servitudes are subdivided into praedial servitudes and personal servitudes.

(a) Praedial servitudes

The following are a few examples of praedial servitudes: Podile, the owner of a plot, has the right to drive or walk over the plot of her neighbour, Tsepho (the servitude of right of way); Mary has the right to fetch water from Nadia's plot (servitude of drawing water); Xolo has the right to graze his cattle on Mark's farm (servitude of grazing), and so on. In all these cases the owner of a piece of land has certain powers in regard to the adjacent land belonging to another. The land of the owner who is the holder of the servitude is called the 'dominant tenement', and that of the owner who has to permit the exercise of the powers conferred by the servitude is called the 'servient tenement'. Each subsequent owner of the dominant tenement may exercise the servitude, and each subsequent owner of the servient tenement has to permit the servitude to be exercised.

The owner of the dominant tenement may demand that any person, including the owner of the servient tenement, who wrongfully obstructs the former in the exercise of his or her powers, cease such action. If the owner of the dominant tenement has suffered loss, he or she may also claim damages from the servient tenement.

The most common method of acquiring a servitude is by registration of the servitude at a Deeds Office against the title deeds of the dominant and servient

properties. The owners of the two properties normally agree on the granting of the servitude, which, however, only comes into being on registration.

Like the right of ownership, servitudes can also be obtained by prescription. A person may acquire a servitude by prescription if he or she has openly, and as though he or she were entitled to do so, exercised for an uninterrupted period of thirty years the rights and powers which a person who has a right to such servitude is entitled to exercise (section 6 of the Prescription Act 68 of 1969).

(b) Personal servitudes

Usufruct is the most important example of a personal servitude. In everyday speech it is often referred to as a 'life interest'. A usufructuary has the power to use and enjoy the property of another. The usufructuary may take all the fruit and produce of the property. In the exercise of these powers, however, the property may not be destroyed or substantially altered. The usufructuary of a farm may not, for example, chop down trees without replacing them, because if this is done the substance of the property, the farm, would be altered. In practice, the rights enjoyed by the usufructuary are particularly valuable. The property may be cultivated for the usufructuary's own use, or it may be let. However, the usufruct may not be transferred to another, for example by selling it, because usufruct is regarded as being inseparably attached to the person of the usufructuary. Usufruct may be granted for any period of time, but for no longer than the lifetime of its holder. Usually it is granted for the lifetime of the usufructuary, hence the name 'life interest'.

The most important method by which a usufruct over immovable property is obtained is registration. Such registration usually takes place in terms of a testamentary disposition. For example, Thabo, a farmer, may provide in his will that his wife shall have a 'life interest', that is, a usufruct in his farm during her lifetime, and that his children shall receive the ownership of the farm. In this way he makes provision for his wife to enjoy the farm's yield during her lifetime, and for his children to enjoy the full, unlimited right of ownership after her death.

2.2.4.1.3 Mortgage and pledge

Mortgage and pledge are limited real rights over property of which another has ownership. Mortgage and pledge both constitute ways in which debts can be secured. The object of mortgage is immovable property and a mortgage is acquired by registration against the title deed. A pledge has, as its object, movable property and is acquired through agreement and delivery of the property. (For a discussion of security, see chapter 23.)

2.2.4.2 The law of succession

When a person dies, he or she leaves behind what is known as a deceased estate, which consists of all his or her assets and liabilities. This estate is administered by one or more executors under letters of executorship granted by the Master. It is the duty of the executor to pay all the debts of the deceased, realising the assets of

the estate if necessary. After payment of all debts, the remaining balance must be distributed amongst the heirs or beneficiaries.

The estate of a deceased vests in the executor who consequently becomes the legal owner of the assets, but he or she has only bare dominium or naked ownership and not beneficial ownership, that is to say, no benefit accrues to the executor from this ownership. Conversely, the debts of the deceased are binding on the estate and not on the executor personally. Only the executor can sue and be sued in regard to estate

matters. Since the executor is the legal representative of the deceased, legal proceedings are brought or defended by the executor in this capacity.

As was stated above, the balance remaining after payment of the debts of the estate is distributed amongst the heirs or beneficiaries. Who these heirs or beneficiaries are depends on whether or not the deceased left a valid will. In the case of there being a valid will, the estate passes according to the rules of testate succession. If there is no valid will, the rules of intestate succession will apply. (For a discussion of the law applying to the administration of deceased estates, see chapter 29.)

2.2.4.3 The law of intellectual property

From ancient times there have always been things external to a person which are of value to him or her, but which are of an incorporeal, immaterial nature, for example, inventions and works of art. Since, in spite of their incorporeal and immaterial nature, these products of the human spirit may be of great economic value to their discoverer or creator, it very soon became necessary for the law to protect the bond between the creator and his or her creation. In other words, the law gave the creator of a new idea in the scientific, literary or artistic sphere a right to his or her creation. In time, protection was extended, for example, to copyright, patents and trade marks. Today all products of the human intellect which are incorporeal and have economic value are regarded as incorporeal things in respect of which rights can exist.

The most important rights in this respect are copyright, patents, trade marks, goodwill and models, that is, rights which relate to the products of a person's mind. In South Africa, the law relating to intellectual property is governed largely by legislation, for example by the Patents Act 57 of 1978, the Copyright Act 98 of 1978, the Trade Marks Act 194 of 1993 and the Designs Act 195 of 1993. The law of intellectual property is discussed in chapter 18.

2.2.4.4 The law of obligations

When a personal right comes into existence between legal subjects, the bond or legal relationship between the legal subjects is referred to as an obligation. Personal rights may come about through contract, delict, or through various other causes of which the most important example is unjustified enrichment. The legal object in relation to a contract is the performance which must be delivered. In the case of a delict, it is the payment of compensation, and in the case of unjustified

enrichment, the payment of an amount equal to an amount by which one person has been enriched to the detriment of another. The following serve as examples:

(a) If two parties conclude a contract, an obligation arises in terms of which one party has the right to demand that the other keep his or her promise (the other party thus has to render performance). Generally, both contracting parties are simultaneously obligee and obligor. For example, if Joan buys Steve's horse for R100, Joan has the right to claim the horse from Steve (Steve's performance is thus the delivery of the horse to Joan), but at the same time Joan is obliged to pay Steve the R100; likewise, Steve is entitled to claim the R100 from Joan (Joan's performance is the payment of the R100), and at the same time Steve is bound to deliver the horse to Joan.

(b) If, by committing a delict, Lindiwe causes damage to Vasi (for example, Lindiwe negligently drives her car into Vasi's fence), an obligation also arises between Lindiwe and Vasi. In terms of this obligation, Lindiwe is obliged to pay Vasi damages (this is the performance owing) and Vasi has the right to claim damages.

(c) The last major source of obligation is unjustified enrichment. If Thobeka pays Themba R500, believing erroneously that she owes the money to Themba, Themba is unjustly enriched at Thobeka's expense. In terms of the obligation which arises, Thobeka is entitled to claim the R500 from Themba who is obliged to repay it.

The general principles of the law of contract are discussed in greater detail in Section B, whereas in the following more attention is given to the law of delict and unjustified enrichment.

2.2.4.4.1 Introduction to the law of delict

This is probably one of the most interesting and all-pervading branches of the law. It is well known that everyone is to some degree or another exposed to the possibility of suffering damage or loss. The factors causing damage may be contained in natural disasters (such as lightning, hail, floodwaters or drought) or in human actions (such as negligent driving or defamatory statements). Compensation for damage suffered by a person can be recovered from another person only if there are legally recognised grounds for recovery. If, for example, a person has insured himself or herself against damage, the law will compel the insurer to make good such damage or loss. If, however, any damage is caused by the delict of another, that other person will be compelled by law to make good such damage or loss. The law of delict lays down what is required for an act causing damage to qualify as a delict and what remedies are available to the party suffering the damage.

In order to determine the scope and bounds of a person's right of ownership to land it must be determined what the legal norms allow a person to do with his or her land and what is forbidden to be done with such land. The law allows, for instance, a person to cultivate vegetables on his or her land, but not certain kinds of weeds; to build a house on it, but, in terms of a municipal regulation (a rule of the law),

not less than two meters from the boundary; to make a fire on it, but not in such a way that the smoke is continually blowing into a neighbour's windows. At the same time, a neighbour's right to his or her land is similarly limited by legal norms which prescribe what may and may not be done with the land. If this were not so, there would be a continual clashing of interests. The law demarcates interests in the form of subjective rights and in this way ensures peaceful co-existence. Each of these rights has a fixed, limited content in accordance with the rules of the law.

The content of a subjective right consists in the powers of the holder of the right. For instance, the owner of property has the power to enjoy, use and alienate the property. The owner can walk on his or her land, lay out a garden or build a house, sell or let it.

The content and scope of the owner's powers, and, therefore, the bounds of his or her right, vary in accordance with the provisions of the law which demarcate the owner's interests and those of other persons.

Therefore, in a system of subjective rights regulated by objective law, the interests of the legal subjects are juridically demarcated. If one person's right is not respected by another, the retributive character of the legal order takes effect: the legal order comes to the aid of the prejudiced party with the 'power of the sword'. This is done in two ways: the prejudiced party is granted an order ('interdict') which forbids the other party to proceed with his or her course of action, or the wrongdoer is ordered to compensate the prejudiced party for the damage he or she has caused.

2.2.4.4.2 Definition of a delict

The mere fact that a person has caused another to suffer damage is insufficient to find delictual liability. Further requirements must be satisfied before delictual liability can follow. The different elements which constitute a delict appear from the following definition of this legal concept.

A delict is any unlawful culpable act whereby a person (the wrongdoer) causes the other party (the person prejudiced) damage or an injury to personality, and whereby the prejudiced person is granted a right to damages or compensation, depending on the circumstances.

From this definition the following elements of a delict may be isolated: (a) an act, (b) unlawfulness, (c) fault, (d) causation, and (e) damage or injury to personality (harm). To be held liable for the harm which he or she has caused another, the wrongdoer's action must comply with all these requirements or elements.

(a) An act

An act is any voluntary human conduct, but it need not be a wilful act. In the first instance this means that only a human being (not animals, for example) can act in the eyes of the law. Secondly, it means that any human conduct (either a commission or an omission) which at the time of the relevant activity was capable of being exercised under control of the will is, legally speaking, an act. Bearing this in mind, a gatekeeper who, while daydreaming, forgets to close the gate before an oncoming train, definitely acts, since his or her omission was capable of being

controlled by will. On the other hand, the activities of a sleepwalker, or of a person who faints behind the steering-wheel of a moving vehicle, are not determined by will and are, thus, not acts.

(b) Unlawfulness

Not all acts (including omissions) that are harmful to others are delicts. Before an act can be deemed to constitute a delict, it must also (in addition to meeting the other requirements) be unlawful. An act is unlawful when it infringes the rights of another, for example, when somebody is defamed or assaulted. An act is also unlawful if the wrongdoer owed the person prejudiced a duty to take care and this duty is breached, for example in the case of a policeman or -woman who fails to prevent a criminal act against another.

Grounds of justification are special circumstances which convert an otherwise unlawful act into a lawful act: an act which at first glance infringes the right of another proves, on closer scrutiny, to be lawful when the defendant can rely on some particular circumstance which justifies his or her act. If, for instance, a person sinks a borehole on his or her property and, as a result of this, a neighbour's water supply dries up, it would seem that the neighbour's right of ownership has been infringed. However, since such a person has exercised his or her own right, the act is not unlawful.

The grounds of justification usually mentioned are by no means fixed in number, but merely represent the most pertinent circumstances generally found to give rise to the question whether the infringement alleged by the plaintiff can be justified by the defendant's claim that the act was not unlawful because he or she in fact had the right to perform the act. The following grounds of justification are usually distinguished -

(i) Necessity

Necessity exists when, through external forces, a person is placed in such a position that the person's (or another's) legitimate interests can only be protected through a reasonable infringement of the rights of another. For example, if Gert damages Koos's house (for example, by breaking a window) to enable Mary to escape because the house is on fire, Koos's right of ownership is not infringed, since a state of necessity justifies the performance of the act which harms Koos's interests. The municipality which refuses to deliver meat to the public at the abattoir does not act unlawfully if the consumption of the meat constitutes a danger to public health. If a ship can be saved in a storm only by casting the cargo overboard, the owner of the cargo has no action for damages against the crew responsible for such an act. The purpose of an act of necessity is to protect the interests of the perpetrator or of a third party in a dangerous situation.

(ii) Self-defence

Self-defence exists when a person, in a reasonable way, defends him- or herself against an actual, or imminent, unlawful attack by another, to defend his or her

own or another's legally acknowledged right. It differs from necessity in that it is a defence against an unlawful threat or attack; from this it follows that it must be an act directed against a human act for only a human can act unlawfully. For example, if Peter attacks John with a knife, and John in turn wounds Peter fatally, then John may rely on the defence of self-defence. There are, however, several requirements that must be met in order to succeed with self-defence as a valid defence.

(iii) Consent

Where a person legally capable of expressing his or her will gives consent to injury or harm, the causing of such harm will be lawful. Consent takes two forms: consent to injury, and consent to or acceptance of the risk of injury. In the case of consent to injury,

the injured party consents to specific harm. For example, Mpo consents that Chris, a surgeon, may remove his appendix. In the case of consent to the risk of injury, the injured person consents to the risk of harm caused by the other's conduct. For example, Mpo consents to the risk that the operation performed on him, by Chris, may have certain side effects. A participant in sport consents to the risk involved in such a sport; a boxer therefore accepts the risk that a blow from his opponent may paralyse him.

Consent may be given either expressly or tacitly. However, not every factual consent to injury is valid since the consent must not be contrary to good morals (permission given to someone to chop off a person's arm, for example, conflicts with good morals). Consent which is not given freely is also invalid (for instance, Ruth threatens to discharge her employee Sophy from her service if Sophy does not consent to Ruth's giving Sophy a hiding). Furthermore, consent given without the consenting party's being aware of the nature and seriousness of possible consequences is also invalid. (For example, if Ida agrees to undergo X-ray treatment without knowing that unsuccessful treatment may possibly lead to the amputation of the limbs treated, her consent is invalid and her doctor is liable for damages.)

(iv) Statutory authority

A person does not act unlawfully if he or she performs an act (which would otherwise have been unlawful) while exercising a statutory authority. Two requirements apply: firstly, the statute must authorise the infringement of the particular right concerned, and secondly, the conduct must not exceed the bounds of authority conferred by the statute. For example, a municipality will not be liable for burning a fire belt over another's property where such burning takes place in terms of a statute. However, should the fire get out of control due to the negligence of the municipality's employees, and the fire destroys another's house, the municipality will be liable.

(v) Provocation

Provocation exists when a person is provoked or incited by another's words or actions to cause harm to the other. As a general rule, provocation is not a complete defence when verbal provocation has been followed by physical assault. However,

defamatory or insulting allegations made during an argument in retaliation to provocative verbal conduct may be justified and, if provocation takes the form of a physical assault, it may, in fact, constitute a complete defence against an action on the basis of the subsequent retaliatory physical assault. Two requirements must be met. Firstly, the provocative conduct itself must be of such a nature that a reaction thereto is reasonable and therefore excusable. Whether this is the case is judged objectively in view of all the surrounding circumstances. Secondly, the conduct of the provoked person must constitute an immediate and reasonable retaliation against the body of the other person. The action of revenge therefore must not only follow the provocation directly, but must be objectively reasonable as well. Here, 'reasonable' means that the physical assault by the second person is not out of proportion in its nature and degree to the assault by the first aggressor. Examples of the above principles are the following: Paulina insults Wanda and Wanda returns the insult; also, Lethabo assaults Sipho, whereupon Sipho assaults Lethabo. Wanda and Sipho can rely on the defence of provocation. However, should Wanda have slapped Paulina, or Sipho have waited for two weeks and only then assaulted Lethabo, they could not have claimed that they had been provoked.

(c) Fault

An unlawful act does not necessarily entail liability for the wrongdoer: the wrongdoer must also be at fault. A wrongdoer is at fault if he or she has acted intentionally or negligently.

A legal requirement for intent or negligence is that the wrongdoer must have reached a sufficient level of mental development to be able to comprehend the nature and consequences of his or her action. One cannot blame someone who does not have sufficient mental capacity to know any better. This basic principle of the law regarding delicts is contained in the requirement that the wrongdoer must have the capacity to have a blameworthy state of mind. The law lays down, for example, that insane persons and children under the age of seven are not capable of having a blameworthy state of mind, because their mental capacity is too undeveloped. These persons can therefore never be at fault and can consequently never be liable. Whether all children over the age of seven years always have sufficient mental capacity is uncertain, and therefore the law provides that boys under the age of 14 years and girls under the age of 12 years shall be presumed to be incapable of having a blameworthy state of mind. This means in practice that the plaintiff always has to prove that such a child was indeed capable of having a blameworthy state of mind.

Once it has been established that the wrongdoer was capable of having a blameworthy state of mind, the question is asked whether he or she acted intentionally or negligently. A person acts with intent if a person's will is directed towards bringing about a particular result and a person is at the same time aware of the unlawfulness of the actions (actual intention). If a person's will is directed towards bringing about a certain event, but it is foreseen that there is a possibility that another event may come about and, regardless of this foreseeable possibility,

the person proceeds to act, he or she has legal intention in relation to the other event (also known as *dolus eventualis*). If David shoots a horse under the erroneous impression that it belongs to him, legally speaking, he does not act with intent, because by reason of his mistake, he believes that he is acting lawfully.

In the absence of intention a person's conduct may still be reprehensible and consequently he or she may still be at fault. This would be the case where a person's behaviour does not comply with the standard of care that the law requires. In such a case there is negligence.

The criterion the law uses today to establish whether a person has acted negligently is the criterion of the ordinary or reasonable man or woman. A wrongdoer is therefore negligent if the reasonable person, had he or she found him- or herself in precisely the same position as the wrongdoer, would have foreseen harm to another with such a degree of probability that, in the light of the circumstances, he or she would either have refrained from the act or would have carried out the act in another way, or would have taken further precautions before acting.

If a wrongdoer has unlawfully and negligently caused damage, but the injured person has also been negligent (this is referred to as 'contributory negligence'), the damage is divided in proportion to the respective degrees of negligence shown by the parties (Apportionment of Damages Act 34 of 1956). If, for example, Mandla runs into Nkaya with his car, and both were fifty per cent negligent, Nkaya will be able to recover only fifty per cent of his damages from Mandla. If Nkaya's total damages amount to R1 000 he therefore receives only R500.

(d) Causation

A wrongdoer can be held liable only for consequences he or she has legally caused. Causation comprises two elements, namely, factual causation and legal causation. The former is present if a factual causal link exists between the act and the damage. But a single act can give rise to an unlimited number of harmful events and the next step is to determine which acts should in law give rise to liability for the damage in question. The latter type of causation is known as 'legal causation'.

Factual causation is determined by applying the *conditio sine qua non* test. In terms of this test the act of a wrongdoer will have caused the damage if such an act is an indispensable condition for the damage to arise. Legal causation is established where there is a sufficiently close relationship between the wrongdoer's conduct and its consequence that such consequence may be imputed to the wrongdoer in view of policy considerations based on reasonableness, fairness and justice.

(e) Damage or impairment of personality

To incur delictual liability a person must have caused another either damage or impairment of his or her personality.

By damage, patrimonial damage is meant. A person suffers damage if, as a result of another's act, his or her estate becomes smaller than it otherwise would

have been: for example, a person's car is damaged in an accident and is worth less as a result. Thus, to determine whether a person has suffered damage as a result of a delict, the present condition of his or her estate must be compared with what it otherwise would have been. If the present condition of the estate is less favourable, a person has suffered patrimonial damage. The person's estate must then be restored to the position it was in before the delict occurred. As regards the calculation of the amount of the damages, the following should be noted. First, a person may not raise as a defence that the other's damage has, entirely or in part, been extinguished by a third party, for example by a payment in terms of a medical scheme or insurance policy. These facts are regarded as falling outside the dispute and are thus not considered in calculating the amount of damages. Secondly, a person has a duty not to allow his or her damage to accumulate — in other words, damage resulting from his or her own fault cannot be recovered.

Impairment of personality, on the other hand, results when someone's personality is wrongfully infringed, that is to say, when one or more of his or her rights of personality (such as the right to reputation and the right to privacy) is infringed. Impairment of personality does not amount to patrimonial damage and it is, by the nature of things, very difficult to assess precisely the extent of the harm suffered in cases of this kind. For this reason the court grants compensation calculated according to what is fair and just after consideration of all the facts of the particular case.

2.2.4.4.3 Remedies

What remedies does the law grant to a person suffering damage or non-patrimonial prejudice? In the first place, a person whose rights are threatened may protect them by means of an interdict. If someone's conduct threatens another's rights — for example, such a person excavates his or her land, which threatens to cause a neighbour's land to collapse — the neighbour can apply to the court for an order (interdict) which compels the other person to discontinue his or her activities. If, for example, a person has good grounds for believing that a defamatory report about him or her is going to be published in a newspaper, publication can be prevented by means of an interdict.

If a person has already caused another harm by his or her unlawful and culpable conduct, a claim for compensation exists. Several possible actions are at a person's disposal. The action that should be used depends on the nature of harm suffered. If a person's estate has been damaged he or she has suffered patrimonial damage (economic loss, or loss which can be assessed in terms of money), and a claim for compensation, based on the *actio legis Aquiliae*, is available. If a person has not suffered patrimonial damage but an injury to his or her personality, a claim based on the *actio iniuriarum*, or the action for pain and suffering, may be used.

The *actio legis Aquiliae* is thus aimed at recovering patrimonial damage, such as the monetary loss a person suffers if a wrongdoer damages his or her motor car by a delict; the *actio iniuriarum* at recovering sentimental damages *(solacium)*, such as damage to a person's good name by a defamatory assertion that he or

she is a thief; and the action for pain and suffering at recovering compensation, for example for emotional shock. To assert that a person is a thief can, of course, also lead to patrimonial damage (a person's customers no longer support his or her shop). In such a case a person should institute both actions: the *actio legis Aquiliae* for the recovery of the damage suffered by his or her estate and the *actio iniuriarum* for the recovery of sentimental damages.

2.2.4.4.4 Introduction to the law of unjustified enrichment

It is patently inequitable for one person to be enriched to the detriment of another. It is therefore a principle of South African law that nobody should be enriched at the expense

of another. In this context to be unjustly enriched means that there is no valid legal ground for the person who has obtained the benefit to have done so and that it was done at the expense of the other. If a minor child, Henry, who is not competent to enter into a contract without the assistance of his parent or guardian, buys a bicycle from a dealer, Walter, and then refuses to pay for it because he is not contractually liable, he will be enriched at the expense of Walter to the amount of the value of the bicycle. The law now gives Walter the right to claim the bicycle or its value from Henry. Thus, there is an obligation between Walter and Henry, which obligation did not arise contractually (a minor is not contractually liable in respect of transactions entered into without the assistance of his or her guardian), or in delict (the elements of delict have not been complied with). It is important to note that the claim is limited to the amount of the actual enrichment. Should the bicycle in the above example have been damaged, Walter could therefore claim only the amount with which Henry had actually been enriched (that is, the decreased value of the bicycle or the damaged bicycle itself) from him.

2.2.4.4.5 The origin of the claim for enrichment

In Roman law the transferor of property which had been given to another person without legal title could reclaim the property from the other person by means of a legal process called the *condictio indebiti*. In due course, various other legal actions *(condictiones)* were acknowledged in Roman law to provide for certain types of enrichment. These actions were accepted and adopted in Roman-Dutch law, on which South African law is based. Thus, it came to be accepted in South African law that, in certain specific instances, actions could be instituted successfully against persons who had been unjustly enriched. No general enrichment action, however, is recognised in South African law. Should a claimant, therefore, wish to institute an action on the ground of unjustified enrichment, he or she will have to make use of one of the existing acknowledged enrichment actions.

2.2.4.4.6 The obligation imposed upon the enriched person

The obligation imposed upon the enriched person takes one of two forms, namely (a) restitution or (b) payment of a sum of money (compensation).

(a) Restitution

A person who has delivered or transferred money or property which is not due to another person may recover that money or property from the other person. Such delivery or transfer may arise in the following circumstances:

(i) Payment or delivery in error

A person who has paid a sum of money, or delivered property, to another person in the mistaken belief that it was due is entitled to recover the property or money from such other person, provided that -
(a) payment or delivery was made under a mistake
(b) the mistake was reasonable
(c) payment or delivery was not made on condition that it would not be recoverable
(d) payment or delivery was not made by way of a compromise.

The action which is instituted in this instance is known as the *condictio indebiti*.

(ii) Payment or delivery under a contract which is invalid owing to illegality

A party to an illegal contract who has delivered property or money to another party may recover what has been delivered, provided such a person is not equally guilty with the person from whom such property or money is being claimed. If a person is equally guilty with that other person, the *par delictum* rule will prevent recovery (the *par delictum* rule is discussed under Section B below).

(b) Compensation

An obligation to compensate the person at the expense of whom one has been unjustly enriched can arise in the following circumstances:

(i) Partial performance

If one party to a contract has performed only a portion of an obligation which is indivisible (for example, Anna has concluded a contract with Bob the builder to build a house for a fixed amount and the building is abandoned at roof height, whereafter Anna cancels the contract because of breach of contract by Bob), the possibility of enrichment liability arises, because the already-delivered portion of Bob's performance cannot be returned as a result of its nature. Bob will, therefore, be entitled to claim the amount by which Anna's estate has been enlarged as a result of the presence of the construction on her ground, or the expenses incurred by Bob, whichever is the lesser amount.

(ii) Improvements to property

If a person effects improvements to property with the intention of doing so for his or her own benefit and he or she has no right or title to the property, the improvements become the property of the true owner. The person who has effected the improvements is then entitled to claim the amount by which the value of the

property has been increased from the true owner. This amount represents the amount to which the true owner has been unjustly enriched at the expense of the person who effected the improvements. Thus, if a person mistakenly believes that he or she is the owner of ground and erects a house on it, the value of the house may be claimed from the true owner. The measure of compensation claimable in such an instance depends on the nature of the particular improvement to the property, but may not exceed the actual expenses incurred in connection with it. The amount recoverable is thus the lesser of either the defendant's enrichment or the claimant's impoverishment. Should the true owner not wish to accept the improvement, it must be removed by the person who effected it, provided that the removal will not damage the property.

(iii) Negotiorum gestio

Negotiorum gestio is related to enrichment. It arises when one person voluntarily, and without the permission or knowledge of another person, manages the affairs of the last-mentioned (for example, if Lala has Brenda's property stored after a tornado has blown away the roof of Brenda's house in her absence). If the person whose affairs have been managed accepts the *negotiorum gestio*, he or she is obliged to compensate the person who managed them for all necessary expenses incurred.

Further reading

WJ Hosten, AB Edwards, F Bosman & J Church *Introduction to South African Law and Legal Theory* 2 ed (1998) Section B

Section B: General Principles of the Law of Contract

Chapter 3 Law of Contract: Introduction

3.1 The contract as a source of obligations
3.2 Requirements for the formation of a valid contract
3.3 Freedom to contract
3.4 Contracting electronically

3.1 The contract as a source of obligations

In this chapter the formation of a valid contract is explained and a distinction is drawn between a contract and other agreements which do not give rise to obligations. A contract can be described as an agreement concluded by two or more persons with the serious intention of creating legally enforceable obligations.

3.1.1 Obligation

An obligation is the legal relationship that exists between parties to an agreement when the parties acquire personal rights against each other that entitle them to performance and/or oblige them to perform in terms of that agreement. Performance may entail an obligation to do, or not to do, something. Personal rights may come about through various events, for instance, through delict or contract. Thus, the conclusion of a contract is an event giving rise to obligations.

3.1.2 A special type of agreement

Although a contract is an agreement between two or more parties, not all agreements are contracts, and not all agreements, create obligations. For example, social appointments (such as an arrangement between friends to meet at a restaurant on a specified date and time) are agreements but they are not contracts as they do not create legally enforceable obligations. At most, they create only moral duties.

The difference between a contract and another agreement lies in the intention of the parties and in the different consequences that are attached to their agreement.

3.1.3 Two or more parties

A person cannot contract with himself or herself unless he or she acts in a different capacity on each side of the contract.

3.2 Requirements for the formation of a valid contract

The law prescribes certain requirements that must be met for a contract to be valid and legally enforceable. The requirements are as follows:

(a) There must be consensus between the parties. The parties must agree on the objectives of the contract. This is also referred to as 'true agreement' or 'the meeting of minds'. This means that each party to the contract must have the serious intention to create rights and duties to which each of them will be legally bound; that the parties must have a corresponding intention, and that the parties must make their intention known to one another.

(b) Each party to the contract must have capacity to act, which means that he or she must be legally capable of performing the particular act which gives rise to the formation of the contract.

(c) The agreement must be legally possible. This implies that the agreement, as well as the rights and duties that are created, must be permitted by the law: in other words, it must be lawful or legal.

(d) The agreement must be physically possible: it must be objectively possible to receive the rights and to perform the duties arising from the contract, and the performance must be certain or ascertainable.

(e) If formalities are prescribed for the formation of the contract, either by the parties themselves or by the law, they must be observed.

A valid contract will arise only if all these requirements have been satisfied. There may still be an agreement should any of these requirements not be met, but this agreement will not constitute a contract. Each of these requirements will be discussed separately in chapters 4-7 below.

3.3 Freedom to contract

Freedom to contract is considered to be one of the cornerstones of the modern law of contract and one is generally free to choose with whom and on what grounds one wants to contract. However, this freedom may be limited in certain circumstances. For example, a person may not conclude contracts which are unlawful or illegal (see chapter 6).

The following statutes are important with regard to freedom to contract:

(a) The Constitution of the Republic of South Africa, 1996.

The Constitution is the supreme law of the Republic. Chapter 2 of the Constitution contains the Bill of Rights, defining constitutional rights. The Constitution recognises and protects individual freedom, equality and economic activity. Some constitutional principles and values, such as those relating to freedom to contract, public policy, reasonableness and equality, are also part of the law of contract.

(b) The Promotion of Equality and Prevention of Unfair Discrimination Act 4 of 2000.

This Act gives effect to the letter and spirit of the Constitution by prohibiting unfair discrimination on grounds of race, gender and disability, and by prohibiting hate speech, harassment and the dissemination and publication of information that unfairly discriminates. In terms of this Act the equality courts (every high court and magistrate's court is an equality court for the area of its jurisdiction) are afforded a wide variety of powers and functions and may inter alia make an order 'to make specific opportunities and privileges unfairly denied, available to the complainant in question'. This may mean that a person may be forced to conclude a contract with another. For instance, where Vanja refuses to conclude a property rental agreement with Edgar based on his race only, or the local golf club refuses Alvira's application for membership based on the fact that she is female, Vanja and the golf club may

be forced by the equality courts to conclude the rental or membership agreements. An order of an equality court made in terms of the Act has, where appropriate, the effect of an order of the court in a civil action.

Other contractual issues affected by the Constitution will be dealt with below, where relevant.

3.4 Contracting electronically

Trade that is conducted by using electronic means, such as the internet or e-mail, is referred to as electronic commerce transactions (commonly called 'e-commerce'). The internet is a global system of interconnected computer networks. The World Wide Web (www), which was developed in the early 1990s, led to the rapid commercialisation of the internet. It is accessed by using a browser such as *Netscape Communicator* or *Internet Explorer*. A network exists as soon as two or more computers are connected in order to share resources.

Simple retail purchases are the most common form of trading over the internet, while banking and insurance transactions are also increasingly performed online. While the internet allows for speedier transacting, it operates in a paperless, faceless world with its own unique problems and strengths. This, consequently, requires an analysis of whether the law pertaining to agreements effected in the usual manner is still relevant when transacting electronically.

In South Africa, the Electronic Communications and Transactions Act 25 of 2002 (ECT Act) applies to all electronic transactions (commercial and non-commercial) and data messages (data generated, sent, received or stored by electronic means), unless specifically excluded from the operation of the Act (for example, wills and alienation of land (Schedule 1 of the Act): see paragraph 7.3.3 below). The ECT Act aims to facilitate electronic transactions and to promote legal certainty for such transactions. In this regard, section 22 of the ECT Act, for instance, provides that an agreement is not without legal force and effect merely because it was concluded partly or wholly by means of data messages.

Problematic issues presented by e-commerce will be dealt with below.

Further reading

RH Christie *The Law of Contract in South Africa 6* ed (2011)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles 4* ed (2012)

Chapter 4
Consensus

4.1 The concept of consensus
4.2 Offer and acceptance
4.3 The moment and place of formation of a contract
4.4 Consensus and defects in will

4.1 The concept of consensus

4.1.1 Consensus as the basis for contractual commitment

Consensus or true agreement is the basis for every contract. Apart from the other requirements that must be satisfied before a contract will be legally valid and enforceable, a contract will only come into existence if the parties reach consensus on the rights and duties created by their agreement. In order to decide whether a contract exists, one looks first for consensus between the parties, which implies a subjective inquiry. However, as consensus can mostly be revealed only by external manifestations (for example, the physical document which contains the contract), the inquiry as to whether consensus has been reached is generally *also* objective in nature. There must be some form of proof that consensus exists between the parties. Consensus can be reached only if —

(a) every party has the serious intention to be contractually bound
(b) the parties have a common intention — in other words they mus have in mind the same commitment, and
(c) every party makes his or her intention known to every other party by means of a declaration of intention.

These requirements will be discussed separately.

4.1.2 The intention to be contractually bound

Every party to a contract must have the serious intention to be contractually bound. Thus, each of the parties must have the serious intention of creating particular rights and duties which will legally bind them.

Where the parties merely have the intention to reach an understanding, or to make an arrangement based on good faith, their arrangement will only give rise to a 'gentleman's agreement' and not to a binding contract. For instance, if friends make an arrangement to meet at a restaurant to enjoy a meal together, there is normally no intention on their part to be legally bound to each other. At most, they are morally obliged to turn up at the arranged venue and time. If one of the friends

cannot meet the others as arranged he or she can normally not be held legally liable for failing to show up as agreed. The situation is completely different if two people agree that the one will sell his or her car to the other for a specified sum of money. In this instance, the parties intend to create a legal obligation which entitles them to performance and/or obliges them to perform.

A statement made jokingly or merely to highlight the good qualities of the object of an agreement (also referred to as 'puffing') is generally not made with the intention of creating legally enforceable obligations.

4.1.3 Common intention

The parties must also agree on the contractual obligations or commitments they wish to create. They must therefore have a common intention to contract with each other and must intend to create the same legal relationship.

If Andrew gives Ben money by way of a deposit, and Ben accepts it by way of a loan, no corresponding intention to create the same legal relationship exists, and consequently no contract is formed.

4.1.4 Making the intention known

Consensus can exist only if the parties are aware of one another's intention. In other words, all the parties must be aware of their true agreement. The mere existence of two independent but corresponding intentions cannot create a contract. For instance, if Andrew decides to sell his watch to Ben for R50 and Ben, completely unaware of Andrew's intention, decides to offer Andrew R50 for the watch, consensus will not exist until Andrew and Ben become aware of one another's intention.

There are many ways in which a contracting party's intention can be made known. It can be done in writing, orally or by means of conduct. The most common method used to determine whether consensus has been reached is to look for an offer and the acceptance of it.

4.2 Offer and acceptance

4.2.1 The concepts of offer and acceptance

The reaching of consensus requires that every party must declare his or her intention to create enforceable rights and duties. The usual way in which parties make their intentions known to one another is through offer and acceptance.

An offer is a declaration made by a person (the offeror) in which he or she indicates an intention to be contractually bound by the mere acceptance of the offer, and in which the person sets out the rights and duties he or she wishes to create. The offeror invites another party or other parties (offeree/s) to consent to the creation of (an) obligation(s) between the offeror(s) and the offeree(s).

An acceptance is a declaration by the offeree (the person to whom the offer was made) through which it is indicated that he or she agrees to the terms of the offer exactly as put in the offer.

4.2.2 Requirements for the offer and acceptance

An offer and an acceptance will give rise to the formation of a valid contract only if the following requirements are met:

(a) The offer must be made with the intention that the offeror will be legally bound by the mere acceptance thereof by the offeree.

This express or implied intention of the offeror to be bound by the offeree's acceptance distinguishes a true offer from any other proposal. Thus an 'offer' made in jest (jokingly) cannot be accepted as it is not made with the intention of being legally binding upon the mere acceptance thereof. For instance, when somebody calls out on a very hot day that 'I will trade my bike for a glass of icy cold water', he or she would be surprised if somebody claims the bicycle upon being given a glass of water. If the offeror's intention is not expressly articulated, it must be deduced from his or her declaration and the surrounding circumstances. The acceptance must also be made with the intention of being legally bound to the offer exactly as it is. Acceptance of an offer is the unconditional acceptance of all the terms in the offer. Upon acceptance of the offer, the parties are committed to the terms exactly as set out in the offer, without any addition to, or omission, of any terms and without any qualifications or reservations.

(b) The offer must be complete.

It must contain all the terms by which the offeror is willing to abide, as well as all the terms to which he or she wants to bind the offeree. This requirement flows naturally from the previous requirement, as an incomplete offer cannot be accepted 'exactly as set out in the offer'.

(c) The offer, as well as the acceptance, must be clear and certain.

Thus the intended obligations must be stated unequivocally and unconditionally so that the rights and duties intended by the offeror are determined or ascertainable. No contract can arise if the offer is vague or ambiguous, since one of the requirements for a contract is that the performance must be certain or ascertainable. A statement made in a vague way, such as 'Don't worry — you will be paid', will generally not amount to an offer. The acceptance, too, must be clear and certain so that there is no doubt about the fact of acceptance. Even if the offer or acceptance is made tacitly by conduct, the contents of the declaration of intention must be clear.

(d) Normally an offer and an acceptance may be made either expressly (in writing or orally) or tacitly by means of conduct (for example by a nod of the head, a movement of the hand or the handing over of money).

In only a few situations does the law prescribe that the offer and acceptance must be made in a specific manner. For example, an offer and acceptance for the purchase or exchange or donation of land must be in writing. Furthermore, if an offeror's offer stipulates that the offer may be accepted in a specified manner only, for example in writing, compliance with such requirement is imperative. If the acceptance does not comply with this, the acceptance will not result in the formation of a contract.

(e) The offer must be addressed either to a particular person or persons, or in general to an unknown person or persons or to the general public.

If the offer has been addressed to a particular person or persons, it can be accepted only by that person or those persons. Thus, if Annie makes an offer to Guy to buy Guy's farm, the offer can be accepted by Guy only, or by someone authorised to act on his behalf. If an offer is addressed to an unknown person or persons or to the general public, the offer must be addressed in such a way that it

is nevertheless ascertainable to whom the offer was addressed. Such an offer may be accepted by anyone falling within the group to which the offer was addressed. An example of such an offer is the promise of a reward or a prize. In this instance the person who promises the reward or prize makes a public offer that he or she will give a reward or prize to any member of the public, or to any member of a particular group, who performs a specific task in a specific manner. For example, a bank makes an offer that it will pay a reward to any member of the public who supplies information on a bank robbery. The person who provides the information on the robbery, and does so with the intention of accepting the offer, has, by this act, accepted the offer. On the basis of the person's acceptance, consensus is reached and a contract arises, qualifying him or her for the reward. An offer on the internet is usually made to the public in general, while an e-mail offer is directed at a specific person, namely, the holder of the e-mail address.

(f) The offer and acceptance must be communicated.

An offer is only completed once it has been communicated to the offeree and an acceptance is completed when it has been communicated to the offeror (see paragraph 4.3 below).

4.2.3 The falling away of the offer

4.2.3.1 General

The offer on its own, and without an acceptance, cannot give rise to a contractual obligation. Once an offer has been made, it does not remain open for acceptance indefinitely, but lapses:

(a) If the offer stipulates that it is valid only for a certain period of time, the offer falls away if it has not been accepted within that period. If no time limit is set in the offer itself, it expires if it has not been accepted within a reasonable time.

(b) If, before the offer has been accepted, the offeror informs the offeree that he revokes the offer, the offer is extinguished.

(c) If the offeree rejects the offer, the offer falls away and cannot be revived.

(d) If the offeree does not accept the offer exactly as it was made, but makes a counter-offer, the offeree, by implication, rejects the offer and the offer is extinguished as the counter-offer is a new offer. In respect of the new (counter-) offer, the original offeree becomes the offeror, and the original

offeror becomes the new offeree. For instance, where Willie offers to sell a farm to Hilde for R500 000 and Hilde counter-offers R400 000, Hilde is, by implication, rejecting Willie's offer. If Willie does not accept Hilde's counter-offer, Hilde cannot fall back on Willie's original offer, as this would no longer be open for acceptance.

(e) If either the offeror or the offeree dies before the offer is accepted, the offer falls away. No rights or duties are transferred to the deceased's estate unless the offer expressly or impliedly permits acceptance by or to the executor of the deceased's estate. The offer falls away as an offeror normally intends to contract with his or her chosen offeree only.

When the offer has been extinguished, it can no longer be accepted by the offeree. If the offeree purports to accept the offer which has fallen away or which has been revoked, he or she is actually making a counter-offer which the original offeror can accept or reject. The situation is then similar to (d) above.

4.2.3.2 The continued existence of the offer: The option

The offeror can ensure the continued existence of the offer by means of an option. Options can be given in respect of different kinds of contracts, for example, contracts of sale and contracts of lease. The option-giver makes an offer to conclude a particular contract (this is the substantive offer) and, in addition, makes a further offer to keep the first offer open for a specified period (the second offer being the option). If the offeree accepts the second offer (thus, if he or she accepts the option), the option contract comes into being. The offeror is bound to keep open the substantive offer for the agreed period. What this means is that, for the duration of the option, the offeror (option-giver) may neither revoke the substantive offer nor conclude a contract with another person concerning the same subject. When the holder of the option has exercised his or her option, the contract comes into being in accordance with the terms contained in the substantive offer.

For example, Nomsa offers her horse for sale to Jacques and also undertakes to keep that offer open for two weeks. The option arises only when Jacques accepts the second offer. When the option does come into being, Jacques has two weeks in which to decide whether or not he wishes to accept the substantive offer. Moreover, Nomsa may neither offer the horse to someone else nor accept another's offer in respect of the horse until this period has lapsed or until Jacques has rejected the substantive offer. The option is exercised if Jacques accepts the substantive offer within this period and communicates his acceptance to Nomsa. If Jacques exercises his option, the substantive contract comes into being.

4.2.4 Special rules with regard to offer and acceptance

Various types of statements should be distinguished from true offers. The following are examples of statements that are not offers:

4.2.4.1 An invitation to make an offer

A request or invitation to make an offer or to do business is not a true offer. In this regard confusion sometimes arises in respect of the advertising of goods in newspapers, periodicals, catalogues, and so forth, and in respect of the display of price-marked goods in a window shop or on the shop floor. The general rule is that an advertisement or display in itself does not constitute an offer but is rather an invitation to do business. When a member of the public reacts to this invitation, he or she makes the dealer an offer to buy the advertised or displayed item. If the advertiser or displayer accepts the offer, consensus is reached and a contract of sale arises.

When trade is conducted via the internet, the question arises whether a website advertising a company's products constitutes an offer. This would depend upon the

wording of the website, as a true offer must clearly be made with the intent to form a binding contract upon the acceptance thereof. Normally an advertisement on a website would not be regarded as an offer to contract, but rather as an invitation to do business. The client who reacts to this invitation by the advertising company on the website is deemed to make an offer to buy, and only upon acceptance of his or her offer by the advertiser does a contract come into existence. This is the preferred position from an internet trader's point of view, as unwanted offers (whether because of oversubscription or a mistake in the pricing) can then merely be rejected without further legal consequences.

4.2.4.2 Statements of intent

In the business world one often encounters so-called 'statements of intent'. This refers to a document in which a party indicates his or her intention to contract, as opposed to offering to actually do so. The distinction is a fine one and turns on an offeror's intention to be bound, without further thought on the matter, on his or her part in the case of a true offer. By contrast, the 'statement of intent' merely forms the basis on which further negotiations regarding the terms of the contract are based.

4.2.4.3 Calling for tenders

Where a tender is called for and the person calling for the tender (the advertiser) does not bind himself or herself to accepting the highest or lowest tender, the call would normally be no more than a request to submit offers, which the advertiser may accept or reject at will.

4.2.4.4 Auctions

At an auction certain rules relating to the sale are made known beforehand by advertising them or by reading the rules to those present at the auction. Every person who makes a bid at the auction does so subject to the conditions of the auction. Thus a contract exists between the auctioneer and each bona fide bidder to conduct the auction according to the advertised conditions of sale. These conditions form the basis of the distinction between auctions held subject to reservation and auctions not subject to reservation. If the auction rules state, for example, that the

goods will be sold only if a predetermined price is fetched or exceeded, the auction is held subject to reservation. Auctions are usually held subject to reservation and, if the auctioneer does not mention anything, it is presumed that the auction is held subject to reservation. In this case the auctioneer extends an invitation to those present to make an offer. The person bidding makes an offer and is the offeror. The auctioneer can accept or reject any bid regardless of whether it is the highest bid. Only when the auctioneer accepts an offer is consensus reached and a contract arises. Conversely, an auction is not subject to reservation if the conditions of auction expressly provide that the goods will be sold without reserve. In such an event it is the auctioneer who makes an offer. The auctioneer's offer is to sell to the highest bidder, and it is this offer which is accepted by the bidder who makes the highest bid. The agreement of sale will be concluded subject to a condition that, if a higher bid is not made within a reasonable time, the sale shall then be effective.

4.3 The moment and place of formation of a contract

A contract arises at the moment when and, at the place, where consensus is reached. Consensus is reached when each of the parties to the agreement becomes aware that the other party is (or the other parties are) in agreement with him or her. This will take place where and when the offeror becomes aware of the offeree's acceptance of the offer. The exact moment of consensus is important in order to decide whether the offer can still be revoked; whether the offer has expired as a result of the passage of time, and when the contractual duties become enforceable — for example, the moment from which payment of interest must be calculated. The place of formation is important in determining, for example, the court which has jurisdiction to hear a claim in connection with the contract.

4.3.1 Where the offeror and the offeree are in each other's presence

If the offeror and the offeree are in each other's presence when the offer and acceptance are made, it is usually easy to determine the time and place of formation of the contract, since the offeror learns of the acceptance of the offer at the same time and place the acceptance is made known. The contract comes into being at the time when the acceptance is communicated and at the place where the parties happen to be at that moment. This is referred to as the information or ascertainment theory, according to which the contract comes into being when and where the offeror learns of the acceptance of his or her offer.

4.3.2 Where the parties are not in each other's presence

If the offeror and the offeree are not in each other's presence when the offer is accepted, the acceptance is not communicated directly to the offeror, but via another medium.

Where contracts are concluded over the telephone, the parties are considered to be in each other's presence as the offeror learns of the acceptance of the offer at

the same time it is made. Although the offeror and offeree may not be in the same place, the ascertainment theory applies and a contract comes into being at the moment when, and at the place where, the offeror becomes aware of the offeree's acceptance of the offer. If Nabilah from Cape Town accepts Bill's telephonic offer from New York, Bill becomes aware of Nabilah's acceptance in New York and the contract thus arises in New York.

The situation is different when a contract is concluded by post. Assume that Nabilah, who is in Cape Town, makes an offer by letter to Gert who is in Johannesburg, and that Gert accepts by letter. When and where is the contract concluded? As there is no instant communication, different rules apply. In these cases the dispatch theory (also referred to as the 'expedition' theory) applies and the contract comes into being at the place where,

and at the time when, the letter of acceptance is posted, unless the parties stipulate otherwise. The dispatch theory is primarily aimed at protecting the offeree.

Can Gert, the addressee, undo his letter of acceptance by requesting Nabilah, the offeror, by means of a speedier method of communication (such as an sms, email or fax), to ignore the letter of acceptance? If the dispatch theory is applied consistently, the answer will be no. However, since the dispatch theory is primarily directed at protecting the offeree, it is proposed that it should be allowed. To do so will result in a truer reflection of the parties' consensus and will also reflect the practicalities of the situation (for example, where the offerror receives the withdrawal notice he may act upon it, and the offeror cannot thereafter change his mind and attempt to enforce the slower letter of acceptance). Gert could thus undo his acceptance by a speedier means of communication before it (the earlier communication) comes to Nabilah's knowledge.

4.3.3 Electronic agreements

In considering which rule to apply to contracts made, for example, by fax, sms, email or via the internet, the type of machine used to transmit the acceptance is not important when trying to determine the place and time of formation in terms of the common-law principles set out above. It should rather be considered whether the circumstances of the case indicate an instantaneous method of communication and, if that is the case, whether a conversational situation similar to a telephone call existed allowing uncertainties to be cleared up immediately. Where the communication medium allows for this type of instantaneous and 'conversational' communication, the parties are in a position analogous to being in each other's presence, and the ascertainment theory should then prevail. In all other instances the choice of theories should be influenced by the intention of the parties, sound business practice and, perhaps, also by a judgment of where the risk should lie.

In the case of contracts concluded over the internet, the choice of a suitable theory is further complicated by the fact that different services are offered on the internet, for instance electronic data interchange and e-mail. Only the e-mail procedure will be briefly discussed here. As soon as an e-mail has been sent, it travels to the sender's server. The server acts as a central point for the collection

and dispatch of messages from a number of computers. The server sends the message into the internet. The message is reassembled by the recipient's server and placed in the recipient's mailbox, where it remains until it is retrieved by the recipient, whether it is minutes, days or months later. Communication is thus usually non-instantaneous, but where the e-mail is sent via an internal company network to a recipient who is logged on at the moment of its being mailed, it may well take place instantaneously. This is also the case in respect of so-called 'chat rooms' where parties are in real time communication.

It is clear from the above that the application of the common-law rules in an e-commerce environment may differ from situation to situation, depending on the facts. The Electronic Communications and Transactions Act 25 of 2002 addressed some uncertainties in this regard. It regulates contracts concluded by electronic means where the parties failed to, or chose not to, regulate contract formation specifically. The Act provides that, in the absence of a different agreement between the parties, an agreement concluded electronically is concluded at the time when, and the place where, the acceptance of the offer is received by the offeror. This is called the 'reception theory' and it takes precedence over the common-law principles. As the 'receipt' of an electronic message plays a crucial role in this theory, this concept has been statutorily defined. A data message is deemed to have been received by the addressee when the complete data message enters an information system (computer or network) designated or used by the addressee and is capable of being received and processed by the addressee. The message becomes *legally effective* upon such receipt as defined, without the need for acknowledgement. (However, an acknowledgement of receipt of a message may be given by any communication or conduct by the addressee indicating that the message has been received.) The Act also provides that a message is deemed to be received at the usual place of business of the receiver, or if there is no place of business, at the usual place of residence. This means that the receipt of a message on a website at a remote server will not be the place of formation of the contract, which is linked to the physical place of business or residence of the receiver.

When contracts are concluded using a combination of traditional and electronic methods of communication, it is advisable that the parties should expressly indicate the time and place of formation to eliminate uncertainty in this regard.

4.4 Consensus and defects in will

In paragraph 4.1.1 of this chapter it was indicated that consensus is the basis for every contract. It then follows that any circumstance which affects consensus will also affect the existence of the contract. If consensus is absent for any reason (for instance in the case of a material mistake) no valid agreement arises, and the proposed contract is void. Conversely, if there is consensus, but it has been obtained in an improper manner (for instance in cases of misrepresentation, undue influence and duress) a valid contract arises, but it will be voidable at the instance of the prejudiced (innocent) party. The distinction between void and voidable contracts hinges on whether or not consensus existed between the contracting parties.

4.4.1 Absence of consensus — mistake

Mistake exists when one or more of the parties to a proposed contract misunderstand a material fact or legal rule relating to the proposed contract. If such a misunderstanding exists, there is no consensus and consequently no contract will arise. However, it may lead to inequitable results where the parties rely on their own material misunderstanding to escape liability. In order to lessen the undesirable results of a strict application of the consensus theory, it is accepted that, despite the lack of consensus, the parties will be held to their declarations of intention unless the circumstances are such that the mistake is reasonable. If the mistake is unreasonable, it is not excused by the law and the party

who has made the mistake will be held to his or her declaration of intention rather than to his or her true intention. This rule is thus an exception to the principle that consensus is the basis for every contract and is discussed in more detail below.

The harshness of a strict application of the consensus rule is also softened by the fact that only mistakes with regard to a material fact, legal rule or principle will lead to the absence of consensus.

4.4.1.1 Requirements to be met before mistake will render a contract void

A contract will be void on the ground of a mistake if:
(a) the mistake relates to a fact, or a legal rule or principle
(b) that fact or rule or principle is material, and
(c) the mistake (whether of fact or of law) is also reasonable.

A contracting party who wishes to rely on a mistake to render a contract void would have to prove all of the above requirements.

4.4.1.1.1 The mistake must relate to a fact, legal rule or principle

In order to have an effect on consensus, a mistake must be one of fact or law. It is unnecessary to elaborate further on mistake of fact. An example of a mistake in law is where Tessa pays Elton R2 000 in the mistaken belief that she owes him the money.

A mistake in law or fact will only invalidate a contract if it is considered to be excusable in the circumstances.

4.4.1.1.2 The mistake must concern a material fact, legal rule or principle

A mistake must be material. A mistake is material and excludes consensus in the following instances:
(a) A misunderstanding in respect of the identity of the person with whom the agreement is reached. For example, if Andrew dials the wrong telephone number and offers a job to Bennie who answers the telephone, while Andrew is under the impression that he is talking to and offering the position to Lennie,

Andrew will labour under a mistake with regard to the identity of the offeree and no consensus will exist as the identity of the offeree is material to the conclusion of the contract. However, where it is immaterial to Ronit whether she purchases a car from a specific sales person or not, and she consequently purchases a car from Douglas, thinking it is Carol, her mistake will not be material and will not affect consensus. Also remember that a mistake in respect of the other person's attributes, such as his or her full names or character, will usually not eliminate consensus, as opposed to a mistake relating to the identity of the other contracting party.

(b) A mistake concerning the content of the intended contract. This may be an error relating to the time when performance must be rendered, or the place and method of delivery, or the performance itself. Mistake in respect of the performance to be rendered occurs, for example, where Shoni is under the impression that she is making an offer to buy Elna's house in Cape Town but Elna is under the impression that the offer is being made to buy her house in Durban. In such a case there will be a material mistake with regard to the thing which is the subject of the agreement, the performance to be rendered, and there can be no consensus. By contrast, a mistake about the attributes of the object of performance is not a material mistake and does not affect consensus. Consequently, if Shoni and Elna are in agreement that the offer and acceptance are made in respect of the purchase of a specific house in Cape Town, but there is a misunderstanding with regard to one of the attributes of the house (for example the zoned purpose of the erf, or the existence or absence of a servitude over the erf, or the number of bathrooms in the house) which has not been elevated to a supposition (see chapter 8), that mistake has no bearing on the formation of consensus and does not render the contract void.

(c) A mistake in respect of an interpretation the law attaches to the offer and acceptance. In such an instance one or both parties have a particular perception of the content of the contract (that is to say, of the rights and duties created by the agreement), whereas the law attaches a different interpretation to it. For example, there can be a mistake about the nature of the contract. Mike offers to pay Tshepo a sum of money to live in a unit in an old-age home, thinking that he acquires ownership of the property, whereas the law's interpretation of the contract is such that Mike acquires only occupation for the remainder of his life.

Mistake may sometimes be caused by a misrepresentation by the other contracting party. Misrepresentation will normally not void an agreement and merely gives rise to the voidability of the contract at the option of the deceived party (see paragraph 4.4.2.1 below). However, where the misrepresentation leads to a material mistake, it results in the absence of consensus and no contract will arise.

4.4.1.1.3 The mistake in fact or law must be reasonable

If the mistake is not a justifiable (excusable) error, the contract, as it appears from the parties' declarations of intention, will be enforced despite the fact that this may differ from a party's real intention.

Mistake will be reasonable if the reasonable person in the same situation would make the same mistake if he or she were to judge the particular circumstances. The test is therefore objective.

The following is an example of an unreasonable mistake. Jo, who suffers from a hearing problem, is under the impression that Steffi is offering her R1 million for her old bicycle. Steffi is in fact offering only R100. Although no consensus exists with regard to the purchase price, Jo's error cannot be excused since a reasonable person would not simply assume that he or she would obtain such a high price for an old bicycle. Jo is

bound by her declaration of intention when accepting the offer and a valid contract is concluded.

It stands to reason that a reasonable person is expected to have no fault, and, consequently, it is required that the party who wishes to rely on mistake must have no fault in respect of the mistake. A person cannot rely on mistake to deny the contract if he or she were negligent or careless, or paid insufficient attention to the matter, for instance by not bothering to read the contract before signing. A person can rely on misrepresentation if the other party has created the (unreasonable) mistake.

4.4.2 Improperly obtained consensus

It sometimes happens that the assent of one party is obtained in an improper way. Several possibilities exist. First, if one of the parties makes an incorrect representation of the true state of affairs to the other party, thereby inducing the other party to conclude the contract, the other party's assent is obtained in an improper manner.

Secondly, a party who concludes a contract under duress or improper influence does not exercise his or her free will and it is therefore not the party's independent will which is expressed in the declaration of intention.

The contract can be contested in all of these circumstances, based on the fact that the consensus was obtained in a manner which the law does not permit.

4.4.2.1 Misrepresentation

A misrepresentation can be defined as an untrue statement or representation concerning an existing fact or state of affairs which is made by one party to the contract with the aim, and result, of inducing the other party into concluding the contract. The misrepresentation may relate to the qualities or characteristics of the subject of the contract.

A contract will be voidable as a result of misrepresentation if the following requirements are satisfied:

(a) There must be a misrepresentation, that is, an untrue statement concerning an existing fact or condition. A misrepresentation of the law will generally not entitle the misrepresented party to a remedy. It is considered to be similar to a statement of opinion, which, if given honestly, will not result in a misrepresentation. Misrepresentation can be made by an express statement or by conduct (eg gestures and actions). Misrepresentation may also be inferred from circumstances that prevailed at the time the contract was concluded, and can even be tacitly made. It must be clear from the representation that is made that a particular message was conveyed. Concealment of the facts (for instance by keeping silent about something) can also constitute misrepresentation, but only if a duty to disclose certain relevant facts exists, for instance when applying for an insurance policy. An applicant's failure to disclose all relevant facts concerning the insurable risk would constitute a misrepresentation.

Giving an honest opinion or estimate (such as a statement about the future profitability of a business), even if the opinion turns out to be mistaken, does not constitute a misrepresentation. The other person will not have any remedy against the person who gives an opinion, unless in delict where it can be proven that the opinion was given negligently. Thus a dishonest opinion as to a future event may be sufficient to found an action for fraudulent misrepresentation in so far as it falsely reflects the state of mind of the party making the representation. In such a case, the party who wants to rely on the opinion of the person he or she is bargaining with must protect him- or herself by having the opinion made a term of the contract. The same applies to statements of commendation or puffing (see also paragraph 4.1.2 above). The representation must be false or untrue. Correct or accurate statements can never give rise to a misrepresentation. The representation should concern a state of affairs that exists or has existed: in other words, it should relate to facts of the past or present.

(b) The misrepresentation must be made by one contracting party to another contracting party or by someone acting in the service of a contracting party, or on his or her authority, or in collusion with him or her. If such a contracting party is induced to conclude a contract by the false representation made by an outsider, the outsider's statement is not a misrepresentation but a misstatement, which has no effect on the consensus of the contracting parties. Rescission is an obvious remedy where parties to the contract are involved. However, where it is an outsider who makes the misrepresentation, rescission would affect an innocent contracting party and not the person who made the misrepresentation.

(c) The misrepresentation must be unlawful. Normally an act (or omission in an instance mentioned in (a) above) would be unlawful if it is contrary to the norm or standard of a specific community's idea of acceptable conduct. It is not considered to be unlawful merely because it is false; the representation must also be material. The representation is normally material if it concerns facts which would probably induce somebody to conclude a contract. In other words, the importance of the misrepresented fact is weighed against the

contract as a whole to ensure that the misrepresentation of an unimportant fact does not sink the whole contract.

(d) The misrepresentation must have induced the contract as it stands. This is also referred to as the requirement of causality, because there has to be a causal link between the misrepresentation and the contract. This means that, but for the misrepresentation, the deceived party would either not have concluded the contract at all or would not have concluded it on the same terms. By implication, this requires that the misrepresentation should have been made during the negotiations preceding the conclusion of the contract. A false representation of facts after the

conclusion of a contract cannot induce a contracting party to conclude a contract, as it has already been concluded. It stands to reason that a person who knew that the statement was false cannot allege that he or she was induced by the misrepresentation to conclude the contract. However, the person to whom a representation is made is under no obligation to ascertain whether the representation is true or not. The person may rely on the misrepresentation without making further enquiries even where the ascertainment of the truth would have been a simple thing to do.

(e) The misrepresentation can be made intentionally, negligently, or innocently. The degree of fault that can be attributed to the misleader determines the availability of a claim for damages (see paragraph 4.4.2.1.1 below).

4.4.2.1.1 The effect of misrepresentation

Misrepresentation does not exclude consensus between the parties and the contract is therefore not void. This means that a valid contract arises. Misrepresentation causes the contract to be voidable since it is regarded as improper to obtain consensus in this manner.

The contract is voidable at the instance (choice) of the deceived party. He or she may elect to uphold or to rescind the contract. If the innocent party elects to uphold the contract, he or she may claim whatever remedy may be appropriate for the breach of contract (see chapter 11). Where the innocent party elects to rescind the contract, the obligations are terminated, resulting in consequences similar to those discussed under cancellation of contract in chapter 11.

The innocent party who elects to continue with the contract may claim specific performance or damages. The party who made the misrepresentation cannot rely on his or her misrepresentation and force the innocent party to rescind the contract or argue that the innocent party ought to have rescinded the contract. The election lies solely with the innocent party. Rescission must consist of words or actions which will give one party a clear message that the other party intends to rescind the contract. The date of termination can be of great importance because even though the contract is rescinded *ab initio* (from the start) it continues in operation until terminated and either one or both parties may have acquired liabilities under the contract in the interim period.

Whether or not the further remedy of a claim for damages is available to the deceived party depends on the degree of fault associated with a specific type

of misrepresentation. Three forms of misrepresentation can be distinguished, namely, intentional misrepresentation, negligent misrepresentation, and innocent misrepresentation.

(a) Intentional misrepresentation

Intentional misrepresentation occurs if a false statement of a material fact is made with the intention of inducing a contract, and if that statement is made either in the awareness that it is false, or recklessly (carelessly), without regard to the truth or falseness of the statement. Intentional misrepresentation is distinguished from other kinds of misrepresentation by the fact that the party misleading the other either knows that the other party is being misled by his or her false representation of the situation, or that he or she is reckless with regard to the truth of the situation or facts being presented.

The party who was induced by intentional misrepresentation to conclude a contract may claim damages from the guilty party irrespective of his or her choice of upholding or rescinding the contract. The basis for damages is the delictual conduct of the guilty party, and the deceived party must be placed in the position he or she would have been in if the misrepresentation had not been made. A claim for damages for intentional misrepresentation is, therefore, a claim in delict and not in contract.

(b) Negligent misrepresentation

This kind of misrepresentation can be defined as a false statement of a material fact which is made negligently and with the aim of inducing a contract. Negligence will be assumed if a person makes a statement he or she believes to be true, without taking the steps a reasonable person would have taken in the circumstances to satisfy him- or herself that the statement were true. Here, too, the misrepresentor is at fault and, therefore, the party who has been misled will base his or her claim for damages on delictual principles. The party who has been misled may claim damages irrespective of whether he or she has decided to uphold or to rescind the contract.

(c) Innocent misrepresentation

If a false statement is made with the intention of inducing a contract, but the party who makes the statement is neither fraudulent nor negligent, the statement is referred to as an 'innocent misrepresentation'. Assume that Fikile, who has been assured erroneously by an acknowledged art expert that his painting is a true Picasso, and sells it as such to Willem. Fikile has taken every reasonable step that could have been expected of him to verify who the artist was, and, consequently, his misstatement of the origin of the painting is neither fraudulent nor negligent. Since Fikile, the misrepresentor, has no fault, there is no room for the application of delictual principles. Accordingly, Willem, the deceived party, has no claim for damages. Willem nevertheless retains his choice of upholding or rescinding the contract.

4.4.2.2 Duress

Duress is an unlawful threat of harm or injury, made by a party to the contract or by someone acting on his or her behalf; that causes the other party to conclude a contract. It is not necessary for the threat to be in the form of expressed words or actions. Duress can be implied, tacit, or by conduct and may also be by subtle forms of intimidation.

If a person is induced to conclude a contract by duress, such a person concludes the contract rather than undergo the threatened action. The threatened person's will is directed at the particular agreement, consensus is reached and a contract in fact arises, except, for example, where a person physically forces the hand of the innocent party to sign a written contract, in which case the contract will be void *ab initio*. However, since

the consent is obtained improperly, the contract is voidable. The threatened party has the choice of either upholding or rescinding the contract (see the discussion on the effects of misrepresentation). Irrespective of whether the threatened party decides to uphold or rescind the agreement, damages may be claimed from the guilty party, calculated according to the former's negative interest, that is, he or she must be placed in the position they would have been in had the duress not occurred.

The following requirements must be satisfied before a contract will be voidable based on duress:

(a) There must be actual physical violence or a reasonable fear of violence or damage. The test is objective. The fear must be the kind that would overwhelm the resistance of a reasonable person in the same position. A reasonable fear of violence or damage would exist if a threat is directed at the life or limb or freedom of the threatened person or his or her immediate family, or at the unlawful damage of his or her property. It has been proposed that the increase in incidence of taking hostages during the execution of a crime should lead to a review of the requirement that the threat must be directed against the 'threatened person or his or her immediate family'. It may be required that the rule be brought into operation where the threat is exerted over strangers.

    A threat of economic damage or ruin may constitute duress and allow the avoidance of a contract in certain instances. However, such cases are likely to be rare for it is not unlawful in general to cause economic harm or ruin to another in a competitive economy. In commercial bargaining, the exercise of free will is always hampered to some degree by the expectation of gain or the fear of loss. 'Hard bargaining' is not the equivalent of duress and is also not unlawful, even where there is an imbalance of power. Thus, even though a threat of economic harm may, in certain circumstances, constitute duress, that will not necessarily be unlawful.

(b) The threat must be of an imminent or inevitable evil. The question will be whether the person could not have averted the threat other than by agreeing to the contract. The time that passes from when the threat is made to when the contract is concluded can play an important role in determining whether the threat was imminent or not.

(c) The threat of harm or violence must be unlawful (or *contra bonos mores*). If a contracting party uses a threat to obtain a more beneficial performance than one he or she would reasonably be entitled to, this would apparently comply with the requirement of unlawfulness.
(d) The duress must be exercised by one contracting party against the other contracting party.
(e) The threat must cause the threatened person to conclude the contract.

Therefore, it must be the threatened person's fear of the impending harm that persuades him or her to conclude the contract or to conclude it on particular terms. A person who, despite the threat, concludes the contract for some other reason cannot complain of duress.

4.4.2.3 Undue influence

Undue influence is any improper or unfair conduct by one of the contracting parties by means of which the other contracting party is persuaded to conclude a contract with the former, contrary to the latter's independent will. The influence must weaken the other party's power of resistance and make his or her will pliable.

Undue influence is not always easily distinguishable from intentional misrepresentation or from duress. A court will be more readily disposed to find that undue influence has been exercised where there is a special relationship between the parties. Such a special relationship is one which exists, for example, between doctor and patient, attorney and client, and guardian and minor. If such a special relationship exists, it is relatively easy for the 'stronger' party to abuse the situation. This may take place, for example, through the abuse of the other party's ignorance or lack of experience, physical frailty, intellectual weakness or mental dependence on the 'stronger' party. By taking advantage of the special relationship, the other's will is made pliable so that he or she is influenced to conclude a contract that would otherwise not have been concluded.

If a party is persuaded through undue influence to conclude a contract, his or her will is directed at the contents of the contract and a contract does indeed come into existence. However, the party's assent to the contract has been obtained improperly so that his or her independent will was not exercised. Consequently, the victim may elect to uphold or rescind the contract and/or claim damages based on his or her negative interest, that is, to be placed in the position he or she would have been in had the influence not been exerted (see the discussion on the effect of misrepresentation above; see also chapter 11 paragraph 11.4.1). The elements of undue influence are the following:
(a) The party who has allegedly exercised the undue influence must have acquired an influence over the victim.
(b) That party must have used his or her influence to weaken the victim's ability to resist, so that the victim's will became susceptible.

(c) The influence must have been used unscrupulously to persuade the victim to consent to a transaction the victim would not have entered into of his or her normal free will and which was to the victim's disadvantage.

An example of undue influence is if Kgomotso, an elderly farmer who is ailing and weak, is induced by Mvusi, his doctor, to donate a farm to Mvusi.

Further reading

RH Christie *The Law of Contract in South Africa 6* ed (2011)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles 4* ed (2012)

Chapter 5
Capacity to Perform Juristic Acts

5.1 Introduction
5.2 Age
5.3 Marriage
5.4 Mental deficiency
5.5 Influence of alcohol or drugs
5.6 Prodigals
5.7 Insolvency

5.1 Introduction

In the previous chapter it was emphasised that consensus is the basis for a contract. A further requirement for the validity of a contract is that the parties must have capacity to perform juristic acts.

Capacity to act (capacity to perform juristic acts) must be distinguished from legal capacity (competence to have rights and duties) and civil or criminal liability (competence to incur civil or criminal liability for wrongdoing). According to South African law, every legal subject, irrespective of whether he or she is a natural person (a human being) or a juristic person (such as a company), legally has the capacity to be the bearer of rights and duties. This capacity is termed legal capacity, and the bearer of the rights and duties is referred to as a legal subject. However, not every person who has legal capacity has capacity to act.

The term 'capacity to act' refers to the capacity to perform juristic acts, to participate in legal dealings and to conclude valid contracts. Only natural persons are potentially capable of having capacity to act. Juristic persons can never be capable of performing juristic acts. Consequently, a contract on behalf of the juristic person must be concluded by a natural person. For example, a company, which is a legal person and can therefore be the bearer of rights and duties, cannot itself perform juristic acts because it is not capable of acting. A natural person must, therefore, perform juristic acts on behalf of the company. This special relationship falls outside the scope of this chapter.

However, not all natural persons have capacity to act. In certain circumstances a person can be incapable of performing juristic acts, or his or her capacity can be limited. The existence of, or the limit on, a specific person's contractual capacity is determined by the law's view of that person's ability to form and declare a will

and that person's ability to judge the rights and duties that will flow from his or her acts.

An individual who has capacity to act may lose the capacity completely or his or her capacity may be limited, owing to various factors. These factors are discussed below.

5.2 Age

Every person's ability to form and declare a will, as well as the ability to appreciate the consequences of a contract, is determined by his or her level of intellectual and emotional development, which in turn is mostly determined by his or her age. A distinction has

traditionally been drawn between three major age bands to determine a person's capacity to act, namely:

(a) nought to seven years
(b) seven to 21 years (the traditional age of majority), and
(c) 21 years and older.

The Children's Act 38 of 2005 states the age of majority is 18 years. The age of majority in South Africa has thus been lowered from 21 years to 18 years. This amendment was necessary to bring the age of majority into line with the Constitution and with international instruments which define a child as a person under the age of 18 years. The lowering of the age of majority has affected the above-mentioned traditional distinctions and changed the last two age bands to: seven to 18 years (see (b) above) and 18 years and older (see (c) above).

These three age bands and the consequences of contracts concluded by persons in each of these bands will be discussed below.

5.2.1 Majority

In terms of the Children's Act a person or child becomes a major when he or she reaches the age of 18 years. Unless a person's independent ability is in some way flawed as a result of some other factor (such as mental deficiency), a person will have full capacity to act when he or she reaches the age of majority.

Previously, when the age of majority was still 21 years, a person who had reached the age of 18 years could apply to the High Court for an order to be declared a major. If such an application was granted, the minor acquired full capacity to act.

It is not clear in terms of the Children's Act whether a person under the age of 18 years may apply to a court to be declared a major. But the Children's Act provides that every child (or anyone acting in the interest of the child) may bring, and be assisted in bringing, a matter to a court, provided that the matter falls within the jurisdiction of that court. It has been argued, however, that this does not necessarily remove the common-law restriction on a child's capacity to litigate.

A minor obtains full capacity to act upon marriage unless the minor's capacity is also flawed for some reason other than his or her age. A minor retains the acquired

capacity to act even if the marriage is dissolved before he or she reaches the age of majority.

5.2.2 Minority

A 'minor' or 'child' is any natural person who has not yet reached the age of majority (18 years). Minors have either no capacity to act at all or they have limited capacity, depending on their age. A distinction is drawn between minors or children who have not yet reached the age of seven and those who are between seven and 18 years old. Minority does not revive after it has been terminated.

5.2.2.1 The minor or child under the age of seven years

In terms of our law a minor under the age of seven has an insufficient level of development to enable him or her to form a sound judgment of contractual obligations. Such a minor has no capacity to act and can therefore not conclude any contract whatsoever. The minor under the age of seven years is not even capable of concluding a contract in terms of which he or she acquires rights without incurring any concomitant obligations and may, for example, not even accept an offer of a donation.

5.2.2.2 The minor or child over the age of seven years

Although a minor who is older than seven years has an independent intellect and can therefore exercise an independent will, it is assumed that he or she does not possess mature and sound judgment. In order to supplement this defective judgment, a minor needs assistance from someone who has full capacity to act. The minor over the age of seven, therefore, has limited capacity to act because he or she may normally perform juristic acts only with the assistance of a guardian.

The Children's Act provides that a parent or guardian of a child must assist or represent the child in administrative, contractual and other legal matters. Moreover, this Act provides that a parent or guardian of a child must administer and safeguard the child's property and property interests. Parents generally have equal rights of guardianship over their children born in marriage. In general, the spouses may exercise these rights independently of each other. However, if more than one person has guardianship of a child or minor, the consent of all the persons that have such guardianship is necessary in respect of a child's marriage, application for a passport, departure from the Republic and alienation or encumbrance of any immovable property of the child, unless a competent court orders otherwise. The guardian's assistance may take the form of assenting and being present at the conclusion of a contract, or of its prior authorisation or subsequent ratification. The effect of the guardian's assistance, or the contracting on behalf of the minor, is that the contract becomes enforceable both by and against the minor. The guardian generally acquires no personal liabilities or rights under the contract. If a contract concluded on behalf of the minor is to the minor's detriment, he or she may, within one year after reaching majority, apply to the High Court for the cancellation of the contract and restitution of everything that has been performed in terms thereof.

The minor would have to prove that the contract was to his or her detriment at the time it was concluded.

A minor or child with limited capacity to act may, however, conclude contracts without assistance if they are exclusively to his or her benefit, namely, contracts in terms of which rights but no duties are acquired. A minor may, for example, accept a donation and may conclude an agreement which releases him or her from a debt but does not impose a duty on him or her to render counter-performance.

There are also several statutory exceptions to the general rule that a minor is contractually liable only if he or she concludes the contract with the required assistance.

Persons who have not yet reached the age of majority will have capacity to act in the following instances: a female minor, irrespective of age, may consent to the termination of pregnancy with or without the consent of her parents (a medical practitioner or registered midwife or registered nurse must advise such minor to consult with her parents, guardian, family members or friends before the pregnancy is terminated; however, the termination of pregnancy shall not be denied because the minor chooses not to consult them — Choice on Termination of Pregnancy Act 92 of 1996); a minor of 17 years and older may obtain a learner's driver's licence (National Road Traffic Act 93 of 1996); a minor over the age of seven years is allowed to withdraw monies deposited in his or her account (Post Office Act 44 of 1958); a minor of 16 years and older may make a valid will (Wills Act 7 of 1953). A minor over the age of 16 may, without assistance, make deposits with and withdrawals from a bank, and cede or burden the investment (Mutual Banks Act 124 of 1993 and Banks Act 94 of 1990).

A child *below* the minimum age set by the common law for a valid marriage, namely 15 years for girls and 18 years for boys, may, in terms of the Children's Act, *not* be given out to marriage or an engagement by their parents or guardians as part of social, religious or cultural practices. Moreover, a child *above* this minimum age may *not* be given out to marriage or an engagement as part of social, religious or cultural practices without the child's consent. Children under these minimum ages may, in exceptional circumstances, get married but only when the Minister of Home Affairs has given consent to such a marriage.

If a parent dies, the surviving parent will be the minor child's guardian. If both parents die, the court will appoint another person with the capacity to act as guardian. If the child is born out of wedlock, the mother will normally be the guardian. However, if a minor wants to get married, or to apply for a passport if he or she is younger than 18 years, or if any immovable property or right to immovable property belonging to the minor needs to be sold or encumbered, the consent of both parents must be obtained. The Children's Act confirms the previous position under the Guardianship Act 192 of 1993 but, in addition, provides for parental rights of unmarried fathers under certain circumstances. If the parents should divorce, the court granting a divorce order will normally also provide for the guardianship of the minor children born from the marriage. The court may make any order it considers to be in the 'best interests of the child', the standard

for all matters concerning a child in terms of the Children's Act. It may for instance grant exclusive guardianship to one parent, if that is in the best interest of the child.

The Children's Act, furthermore, provides that any person having an interest in the care, well-being and development of a child may apply to the High Court for guardianship of such a child.

The Children's Act makes more detailed provision for children of 12 years and above to consent to their own medical treatment or operations on them. This is the case where a child is over 12 years old and has sufficient maturity and mental capacity to understand the benefits, risks, social and other implications of such medical treatment. The same applies to an operation on a child but, in this instance, the child must be assisted by his or her parent or guardian. The parent or guardian of a child may, however, consent to the medical treatment of, and an operation on, a child if he or she is under the age of 12 years, or over the age of 12 years, but is of insufficient maturity to understand the benefits and risks of such treatment or operation.

The Children's Act provides for HIV tests on children. A child may be tested for HIV only when it is in the best interests of the child and consent has been given. Consent may be given by the child him- or herself if the child is 12 years old or older, or under the age of 12 years and is of sufficient maturity to understand the benefits, risks and social implications of such a test. The parent must give permission for an HIV test on a child if the child is under the age of 12 years and is not of sufficient maturity to understand the consequences of such a test. A care-giver (that is, any person other than a parent or guardian who factually cares for a child, such as a foster parent or a person at the head of a child and youth care centre or a shelter where the child has been placed) may also consent to an HIV test to be done on a child. It is required that a child must be properly counselled before and after an HIV test. The same applies to parents and caregivers who have knowledge of the test.

In terms of the Children's Act, a child also has the right to have access to information on health promotion and the prevention and treatment of ill-health and disease, sexuality and reproduction, and to information regarding his or her own health status and its causes and treatment. The Act further provides that children over the age of 12 years shall have access to contraceptives in certain circumstances.

5.2.2.3 Special situations

The following special situations must be noted:

(a) Contracts for which the guardian's assistance is insufficient

In specific situations the guardian's assistance is insufficient and the consent of the High Court, or some specified person, must also be obtained. For example, the guardian(s) as well as a Master of the High Court must consent to the alienation or mortgaging of immovable property belonging to the minor if the value of the property is less than R100 000. If the value is more than R100 000 the guardian(s)

as well as a judge or judges of the High Court must consent to the alienation or mortgaging (in other words, the court as such must consent and not just the Master of the Court).

Note that the above-mentioned additional consent is only required where property is alienated, and not where property is acquired.

(b) Tacit emancipation

An emancipated minor has the capacity to conclude certain contracts without the assistance of his or her guardian. The guardian's consent may be given expressly or tacitly. Tacit emancipation occurs where the guardian allows the minor to lead an

economically independent existence. The consent must, however, appear from some act which shows the guardian's consent. Mere inattentiveness or indifference does not amount to consent.

The test for determining whether the minor has been emancipated is whether the minor is economically independent and whether the guardian allows him or her a measure of contractual freedom. Emancipation may be indicated by a separate living place and an own business, but these factors are not always conclusive evidence.

It is a question of fact whether a particular minor has full capacity to act as a consequence of his or her emancipation, or whether the capacity to act is restricted to the conclusion of contracts related to the business the minor conducts or the occupation he or she practises with the consent of the guardian. The facts of each case will determine the degree of legal independence a particular minor enjoys (the extent of his or her emancipation). It must be borne in mind that while emancipation can provide capacity to act, it is not a means of terminating minority. For example, an emancipated minor still needs the guardian's permission when he or she wants to get married. A minor also requires the consent of the guardian (and the High Court or the Master) if he or she wishes to alienate or burden fixed property.

(c) Contracts which the minor or child concludes without the necessary assistance in spite of a limited capacity to act

If the minor, in spite of his or her limited capacity, concludes a contract without the necessary assistance of the guardian, the contract is not necessarily void and without effect.

A contract is binding on the minor if the guardian ratifies (confirms) it before the minor reaches the age of majority, and also if the minor him- or herself ratifies it subsequent to acquiring the capacity to act (irrespective of the manner in which the capacity to act was obtained). Such ratification causes the minor to be bound as if he or she had had full capacity to act at the time of concluding the contract.

If a minor concludes a contract without the necessary assistance or ratification of the guardian, it is not enforceable against the minor, not even after the minor has obtained majority. Nonetheless, it is always at least partially effective. The minor does not incur liabilities towards the other contracting party, but the other party incurs liabilities towards the minor. This principle can be explained by means of

an example. Suppose a minor, without the consent of the guardian, sells his or her bicycle to a major for R400. The minor is entitled to claim payment of the money but is not obliged to deliver the bicycle.

If the major has not yet performed in terms of the contract and the minor wants to claim payment of the money, the minor may initiate proceedings against the major only with the assistance of the guardian. Once the guardian's assistance has been obtained, the contract is, by implication, ratified. The effect is that the minor's promised performance in terms thereof becomes enforceable. If the minor then institutes action against the major for payment of the money without the minor having delivered the bicycle or having tendered delivery, the major may raise the defence that he or she need not pay until the minor's obligations have been fulfilled or the minor has offered to fulfil them. Essentially, the minor is able to enforce his or her rights only by rendering or tendering the promised performance.

The position of the major who has already performed in terms of a contract with the minor is less favourable. The major may well find that the minor either refuses to render performance of the obligations in terms of the contract, or reclaims the performance if he or she has already performed. In neither case will the major have any contractual remedy at his or her disposal. The major's only redress is to institute a claim against the minor based on unjustified enrichment. The minor, however, is liable towards the major only in so far as the unjustified enrichment has continued to exist up to the moment of the minor's being sued. This means that, in the above example, the minor is liable for the return of only so much of the money as remains in his or her possession when the action is instituted. There are three possibilities in this regard:

(i) If the minor recklessly squandered the full amount, he or she cannot be sued on the grounds of unjustified enrichment because there is nothing left and the minor is therefore no longer enriched.
(ii) If the minor bought a luxury item such as a radio, he or she is obliged to surrender the radio or its value.
(iii) If the minor used the money to provide necessities or essentials for which the guardian normally would have to pay (such as food and clothing), the minor or guardian will be liable to repay that part of the money which brought about a saving of the expenditure. The guardian would otherwise have been enriched, since he or she is responsible for providing the necessities to the minor.

(d) Fraudulent misrepresentation of majority

If a minor, by any form of conduct, poses as a major in a fraudulent manner and thereby induces a third party to contract with him or her, the minor should be held liable on the contract as though he or she were, in fact, a major and had the capacity to act. Although this is not an uncontested viewpoint, it seems like a fair practice as the fraudulent minor would also be liable in delict. This rule would form an exception to the general rule that a minor is not bound by a contract which was concluded without the necessary assistance.

5.3 Marriage

Marriages concluded according to South African law are regulated by the Matrimonial Property Act 88 of 1984. Marriage has certain patrimonial consequences which relate to the chosen marital regime. Marital regime refers to marriages in and out of community of property. These patrimonial consequences used to have a big impact on the spouses' capacity to act and used to be the most important factor to consider when determining such capacity. Although certain consequences remain a consideration, the abolition of the husband's marital power renders it unnecessary to consider this former restriction on a married woman's contractual capacity with regard to contracts concluded after 1 December 1993.

In order to determine whether a specific spouse has capacity to act in a given situation, a distinction must be drawn between —

(a) agreements concluded prior to 1 December 1993 where the husband still had marital power
(b) certain agreements concluded by a spouse married in community of property, and
(c) agreements concluded by a spouse married out of community of property.

5.3.1 Agreements concluded prior to 1 December 1993 in cases where the husband had marital power

In common law and in terms of the Matrimonial Affairs Act 37 of 1953 (the relevant sections of this Act were subsequently repealed) a married woman could be subject to the marital power of her husband. Under the old regime it was possible to exclude the marital power in the case of marriages out of community of property, in which event the wife had full capacity to act.

The effect of marital power was that a married woman who was subject to that power had limited capacity to act. If the husband possessed the marital power, he had the capacity to control and administer the joint estate or his wife's separate estate. He was liable, therefore, for compliance with the obligations of the joint estate. The wife herself was debtor and creditor in respect of her separate estate, but she needed her husband's assistance to institute or defend an action in this regard. Without her husband's consent, the married woman who was subject to her husband's marital power could not conclude contracts which imposed liabilities or duties on the common estate, or jointly and severally on her or her husband's separate estates.

In 1984 marital power was abolished in respect of marriages concluded on or after 1 November 1984. Parties who were married under the old regime were able to take the necessary steps, within a certain prescribed period, to make the new regime applicable to their marriage. They were consequently also able to abolish the marital power in respect of their marriage. If the necessary steps were not taken, the marital power would still have applied to marriages in community of property under the old regime, as well as to marriages out of community of property where the marital power was not specifically excluded.

However, a further amendment abolished the last vestiges of marital power with effect from 1 December 1993. Now, notwithstanding when and how (in or out of community of property) a couple is married, marital power has been completely abolished.

Although marital power has been abolished in respect of all marriages, the 1993 Act has no effect on any legal consequences which attached to any act or omission or fact existing before its promulgation. This implies that where consent was required before 1 December 1993, but not obtained, the agreement would still be voidable at the husband's option. If the husband chooses not to ratify, the third party's claim would have to be based mainly on unjustified enrichment as the agreement would remain invalid.

These problems will fade away in time as transactions concluded before 1 December 1993 recede into history.

5.3.2 Agreements concluded by a spouse married in community of property

According to South African law, spouses are married in community of property unless they agree to the contrary. The most important patrimonial consequences of a marriage in community of property are the following:

(a) The separate assets and liabilities of the husband and wife are consolidated (joined) so that there is only one common (joint) estate. Each spouse is the owner of one half of the joint estate, which is divided only when the marriage is dissolved by divorce or by the death of one of the parties. However, in exceptional cases it is possible for a spouse to retain specific separate property: for example where an asset is bequeathed in terms of a will to a spouse with the express condition that it is to be excluded from the joint estate.

(b) The joint estate acquires the profits and bears the losses which arise during the marriage. For example, if Anne purchases clothes on account, the joint estate will be liable and not only Anne in her personal capacity. Rights and duties flowing from contracts that are binding on the joint estate become the common rights and duties of the spouses. The joint estate thus results in community of profit and loss. In other words, any contractual rights or duties are shared equally by the spouses.

In principle, after the abolition of the husband's marital power as discussed above, each spouse has full capacity to act with regard to the joint estate. Thus each spouse is, in principle, free to manage the joint estate, dispose of assets and incur debts without the consent of the other spouse.

Where a debt is recoverable from a joint estate, the spouse who incurred the debt or both spouses jointly may be sued. Where a debt has been incurred for necessities for the joint household, the spouses may be sued jointly or separately. Note, though, that the Act refers specifically to household necessities for the joint household. Where the spouses have separated, the common law addresses the problem by determining which spouse's misconduct led to the separation. If it was

the wife's, her capacity to bind the joint estate for necessities ceases. If it was the husband's, the wife's capacity to bind the joint estate continues. If the separation was by mutual consent, an adequate allowance by the husband deprives the wife of the capacity to bind the joint estate over and above the amount of the allowance.

The general rule that each spouse has full capacity to bind the joint estate is qualified with regard to certain assets of the joint estate and certain transactions which involve the joint estate. In these instances each spouse has to obtain the other spouse's consent to the qualified transaction unless the intended transaction is carried out by a spouse in the ordinary course of his or her profession or trade, in which case the requirement will be waived in certain circumstances.

Written consent is required if immovable property and investments (financial or otherwise but excluding securities listed on the stock exchange) are alienated or otherwise burdened as stipulated in the Act; where a spouse binds him- or herself as surety; acts as purchaser in certain property transactions; wishes to withdraw money held in the name of the other spouse in a bank or similar institution; institutes certain legal proceedings against him or her; or defends proceedings instituted against him or her. For certain of the above-mentioned transactions, the written consent must also be attested by two competent witnesses.

In other instances the required consent can be obtained verbally or tacitly, for example, where movable assets of the common household are alienated or otherwise burdened, or where an asset is donated to the prejudice of the other spouse's interest in the joint estate.

Consent can be given by way of ratification, except where a spouse binds him- or herself as surety or alienates or otherwise burdens the immovable property forming part of the joint estate, or where consent is required for the registration of a deed in a Deeds Registry.

When a spouse concludes a transaction with another person in contravention of the above provisions, and that other person does not know and cannot reasonably know this, the particular transaction is deemed to have been concluded with the required consent.

If the spouse whose consent is required withholds it unreasonably, or if, in any other case, there is good reason to dispense with consent, the High Court may, on application, permit the transaction without the required consent.

The court may also, on application by a spouse, indefinitely suspend any powers which the other spouse may exercise in terms of the Act. The court will do so only if it is convinced that it would be necessary for the protection of the applicant spouse's share of the common estate to do so.

5.3.3 Agreements concluded by a spouse married out of community of property

Parties to a marriage may agree in an antenuptial contract that their marriage will be out of community of property. Such an antenuptial contract must be concluded prior to the marriage. It will only be binding on outsiders if it is also notarially executed and registered in a Deeds Office within a specified time after such notarial

execution. Normally the parties to an antenuptial contract stipulate that their intended marriage will be out of community of property and without community of profit and loss. Each spouse then retains his or her separate estate and each one has full capacity to act only in respect of his or her own estate. Each spouse will, in principle, be liable only for the debts incurred by that spouse in respect of his or her own estate, except in the case of household necessities.

The Matrimonial Property Act 88 of 1984 provides that spouses married out of community of property (irrespective of whether or not the spouses were married before or after the 1984 Act came into operation) are obliged to make pro rata contributions, in accordance with each one's financial means, in respect of necessities for the common household. The position may be illustrated as follows. Suppose the wife earns R500 per month and the husband R1 000. The wife's pro rata contribution to household necessities is one-third (R500 as a proportion of the total income of R1 500) and the husband's pro rata contribution is two-thirds. Spouses married out of community of property are jointly and severally liable to third parties for all debts incurred by either spouse for necessities for the common household.

Every marriage out of community of property concluded after 1 December 1984 is subject to the accrual system unless expressly excluded by the antenuptial contract. This system does not affect a spouse's capacity to act, and will thus not be discussed, but it is an important aspect of marriages out of community of property. Accrual refers to the amount by which the net value of a spouse's estate at the dissolution of the marriage, either by divorce or by the death of one of the spouses, exceeds the net value of his or her estate at the commencement of the marriage.

5.4 Mental deficiency

If a person's mental condition is such that he or she is not able to understand or appreciate the nature or consequences of his or her conduct at a level which is sufficient to enable him or her to manage a particular affair and make rational decisions, it stands to reason that such a person cannot form the necessary will to conclude a contract. Such a person is completely contractually incapable. If a person who is mentally deficient purports to conclude a contract, the contract is void and without consequence, so no rights or duties are created by it. This also applies to agreements in terms of which the mentally deficient person acquires rights without incurring obligations.

There is a presumption that every person is normal. When a court, on application by an interested party, has certified a person as mentally deficient (in terms of the Mental Health Care Act 17 of 2002), a curator is appointed to administer such a person's estate and to manage his or her affairs. Neither the certification as mentally deficient nor the appointment of a curator has any effect on the mentally deficient person's capacity to act. The test is solely a factual one and the question is whether the person was normal or mentally deficient at the moment of concluding the contract. If a mentally deficient person concludes an agreement after having

been declared mentally deficient, he or she can nevertheless be held liable if the contract was concluded during a moment of normality.

The certification as mentally deficient or the appointment of a curator does have an influence, however, on the burden of proof, since it creates a presumption that the person no longer has the capacity to act. Therefore, before certification or appointment there is a presumption of normality and of capacity to act, and thereafter there is a presumption of contractual incapacity. The person who avers the opposite must prove it.

5.5 Influence of alcohol or drugs

A person who is in such a state of intoxication caused by alcohol or drugs that he or she does not appreciate the nature and consequences of his or her actions, or who is unable to control the actions, is incapable of forming a will. Legally, therefore, such a person is incapable of performing juristic acts. Any agreement concluded while a person is in such a condition will be void and unenforceable. However, if a person is indeed able to form a will in spite of the influence of alcohol or drugs, he or she will have the capacity to act despite the fact that his or her judgment may be affected to some extent.

It is therefore a question of fact whether, at the moment of concluding an agreement, a person has the capacity to act. Since there is a presumption that every person has capacity to act, a party who alleges incapacity either in him- or herself or another due to alcohol or drugs must prove it.

5.6 Prodigals

If, as a result of a person's propensity to squander his or her own money in an irresponsible and extravagant manner, a person is incapable of managing his or her own affairs competently, the High Court may, on application by an interested party, declare such a person a prodigal. A curator will then be appointed to manage the prodigal's affairs on his or her behalf.

However, mere prodigal tendencies have no effect on a person's capacity to act. Only when the court declares the person a prodigal and appoints a curator will that person be forbidden to perform juristic acts without the consent of the curator. In this way a prodigal's capacity to act is limited. Only agreements which are solely to the prodigal's advantage, and which do not render him or her liable for the discharge of obligations, may be concluded without the assistance of the curator. A prodigal's position is similar to that of the minor with limited capacity to act. Because a prodigal has the ability to reach consensus, his or her unassisted contracts are voidable and not void and can therefore be ratified by the curator.

The limitation on a prodigal's capacity to act is terminated when the order is set aside by the court.

5.7 Insolvency

A person's capacity to act is not influenced merely by insolvency. However, if a person's estate is sequestrated (see chapter 28), a person's capacity to act will be influenced by certain provisions of the Insolvency Act 24 of 1936.

The sequestration of a person's estate causes the insolvent estate to vest in the Master and then in the trustee as soon as one is appointed. It is the trustee's duty to liquidate the estate for distribution amongst creditors. After sequestration the insolvent loses the capacity to act with regard to the assets of the insolvent estate. Any agreement attempting to dispose of such assets would be invalid. This limitation has no effect on assets which are excluded from the insolvent's estate.

The insolvent may also not conclude agreements which may probably have a detrimental effect on the insolvent estate, without the permission of the trustee. In these instances the insolvent's capacity to act is limited. The contract would not automatically be void, as it can be ratified by the trustee, but it is voidable at the option of the trustee.

With regard to the other spheres of the insolvent's life, his or her capacity to contract will generally not be influenced by the sequestration. The insolvent's capacity to act will only be influenced to the extent provided for in the Insolvency Act. The insolvent may, for instance, accept any position as employee without the permission of the trustee. The insolvent may, however, not be employed by or do business as a general dealer or manufacturer, or have an interest in such a business without the consent of the trustee.

Further reading

RH Christie *The Law of Contract in South Africa* 6 ed (2011)

Chapter 6
The Agreement must be Possible

6.1 Introduction
6.2 Legal possibility
6.3 Possibility and certainty of performance

6.1 Introduction

The requirement that the agreement must be possible comprises two elements, namely, legal and physical possibility of execution.

6.2 Legal possibility

Legal possibility requires that the agreement, as well as the rights and duties that are created, must be permitted by the law (be lawful and legal) to constitute a contract. A contract will be unlawful or illegal when its conclusion, or the reason or object of its existence, or rights and duties agreed upon, is/are forbidden by common or statutory law. There are in existence many statutory and common-law principles rendering a contract illegal, but we discuss only some examples and their consequences hereunder.

6.2.1 Contracts contrary to the common law

An agreement can be contrary to the common law because it is legally impossible to execute, or because it is against good morals, or against public policy (or interest). The principles underlying these concepts overlap to a large extent. The determination of common-law legality often requires the weighing and balancing of a variety of interests.

The Constitution is generally a reliable indicator of good moral values and public policy, and courts have to promote the spirit, purport and objects of the Constitution when interpreting any law, including the common law. The Supreme Court of Appeal has held that the meaning of 'public policy' now derives from the Constitution's founding values of human dignity, the achievement of equality, the advancement of human rights and freedoms, and non-racialism and non-sexism. Public policy must be determined with reference to the Constitution and, where a contractual term violates the Constitution, the contract is contrary to public policy and is therefore unenforceable.

6.2.1.1 Contracts which cannot be legally executed

In general it can be said that a contract cannot be legally executed if the rights and duties in terms of the contract cannot be performed in accordance with general legal principles. For instance, it is impossible to buy and to sell something which is not capable of being privately owned (for example, the sea or the moon).

6.2.1.2 Agreements that are contrary to good morals

An agreement will be contrary to the good morals of the community if the contract itself, its purpose or the rights and duties agreed upon are contrary to the community's perception of what is proper and decent. For example, contracts which are aimed at providing illicit sexual services and contracts which impair the stability of a marriage are contrary to the South African community's perceptions of what is proper and decent. If Kylie and Dudu conclude an agreement to run a brothel in partnership, and they both

know that such conduct is contrary to good morals, their agreement is illegal as its purpose is contrary to good morals and thus contrary to the common law.

The convictions of the community with regard to good moral values differ from one community to another, and also change within any particular community with the passage of time.

6.2.1.3 Agreements that are contrary to public policy

A contract will be contrary to public policy if the contract itself, its effect or the purpose of its conclusion is harmful to the interests of the public at large. A contract is generally not contrary to public policy merely because its terms offend an individual's sense of propriety and fairness — it should be unconscionable, immoral or illegal. A contractual term which is not per se contrary to public policy will not be enforced if its enforcement would be contrary to public policy. Also, the courts will not give effect to the implementation of a contractual provision if it will be unreasonable or unfair to do so. Note again that the Supreme Court of Appeal has stipulated that when deciding whether to invalidate a contract on the ground of 'public policy', the courts have to take into account the founding values of the Constitution, namely, those of human dignity, the achievement of equality, the advancement of human rights and freedoms, and non-racialism and non-sexism. Harm should be substantially incontestable. Although the concept of 'public interest' generally refers to the interest of society as a whole, it must be remembered that a society's interest may, in certain circumstances, be served by upholding the interest of a section of the society, or even individual interests. If it is also kept in mind that public policy generally favours utmost freedom of contract, it becomes evident that the determination of public policy is often problematic.

A number of contracts will now be discussed as examples of existing indicators of public policy, but it must be borne in mind that public policy also adapts to changing convictions with the passage of time.

(a) Agreements involving the administration of justice

Any agreement which misuses or thwarts the administration of justice is contrary to public policy. For example, an agreement which deprives a contracting party of any and all opportunity to properly defend him- or herself against future wrongs committed against him or her is void. Another example of this is an agreement by which someone undertakes not to report another person's crime to the police. This may also fall under (b) below and is an instance of the overlapping mentioned above. It is also contrary to public policy to bribe public officials.

(b) Agreements involving crimes and delicts

Since every person is expected to behave lawfully, an agreement to commit a crime is contrary to public policy and therefore legally unenforceable. This also applies in respect of an undertaking by a person to commit a delict, for example to defraud a creditor or an insurance company.

(c) Agreements affecting the safety of the state

An agreement between a person and a subject of an enemy state, which is at war with the former's own country, is contrary to public policy and therefore not permissible if the agreement is to the advantage of the enemy state. Therefore, an agreement to provide military supplies to the enemy state is unlawful and invalid.

(d) Agreements restraining a person's freedom to participate in legal transactions

An agreement which restrains the freedom of a person to take part in legal transactions is contrary to the public interest if the agreement is such a serious infringement of the person's freedom of action that public policy cannot countenance it. In Roman times, such agreements were considered void. These days, however, the general view is that they are merely voidable.

According to this principle a person is not permitted to undertake that he or she will refuse to accept an inheritance upon the future death of the testator. Nor may a person be deprived of the freedom of testation by an agreement stipulating that his or her possessions will be bequeathed in a certain manner. Such agreements in respect of legacies must be distinguished from valid donations between the living.

Antenuptial contracts are exceptions to the rule. Here parties (who are to be married) may agree to the appointment of the other spouse as heir, thereby actually providing for the maintenance of the survivor.

(e) Agreements restraining a person's freedom to participate in trade

An example of an agreement interfering with a person's freedom to take part in commerce is a contract in restraint of trade. Two kinds of contracts in restraint of trade commonly occur.

First, it often happens that the purchaser of a business enterprise or of a professional practice insists on including in the contract of sale an undertaking by

the seller that, for a specified period and/or within a specified geographical area, the seller will not practise his or her profession or carry on a business in competition with the purchaser. This kind of contract in restraint of trade would be found, for example, where a hairdresser Zaza sells her salon to Vusi. Vusi realises that Zaza's personality, or her outstanding competence as a hairdresser, is the reason for the clients' support of the salon. Vusi also realises that these clients will continue to support Zaza if she operates a salon in the same city, and that he will possibly end up without clients despite the large sum of money he has paid for the salon and goodwill. Vusi insists on a clause in the contract of sale which forbids Zaza from working in a salon in the same city for the

following two years. It is clear that Zaza's freedom to take part in commerce is restricted by the agreement, because she is deprived of her free choice regarding the time and/or the place at which she may carry on business and/or practise her trade.

The second kind of contract in restraint of trade commonly relates to the protection of trade secrets and commercial contracts. For example, an employer who trains an employee may convey knowledge to him or her of certain secrets of their business. In their contract they agree that, subsequent to the employee leaving the employer's service, the employee will not render the same kind of labour or service within a specified period and/or within a specified geographical area. Clearly, the employee's freedom to compete in the employment market is restrained by such an agreement.

Such contracts bring two principles of public policy into conflict. On the one hand, it is in the public interest that everyone should be able to participate freely in commerce. On the other hand, it is also in the public interest that contracts must be executed. Where these two interests are brought into conflict, they are set off against each other. Contractual commitment is then regarded as the stronger of the two interests, and takes precedence. Although the Constitution entrenches a person's freedom to choose his or her trade, occupation or profession, it does not affect the common-law balance between the two interests. Though an entrenched constitutional right can only be limited in accordance with the statutory limitation clause (that is, if the limitation is reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom, taking into account a number of factors), it has been held that a successful application of the common-law principles developed by the courts will generally result in the required compliance. In other words, if the limitation on a person's freedom to trade is lawful in terms of proven common-law principles, it will not transgress the provisions of the Constitution, and the agreement will be upheld.

One of the factors which the courts often take into consideration when determining whether the agreement is contrary to public policy is whether the restraint is reasonable to both parties. The reasonableness of the restraint may hinge on the nature of the restraint (what activity it prevents), the geographical size of the area which is covered by the restraint and the length of time of its operation. For example, a restraint by means of which a professional person may not practise his or her profession (nature) in South Africa (area) for a period of ten years (time) will probably be regarded as unreasonable since it unreasonably limits that person's

ability to take part in professional commercial life. The parties' own view as to what is reasonable is not decisive. The court will consider the circumstances that prevail at the time when it is asked to enforce the clause in restraint of trade. The court's determination can even be influenced by factors which were not present to the minds of the parties when they entered into the agreement. Thus the content of the agreement cannot itself be the only determining factor of what is reasonable. Whether a restraint of trade is reasonable or not will be determined with reference to the circumstances of the case at the time the determination is made.

Where a clause does not protect a legally recognisable interest of the employer (that is, an interest belonging to the employer which is worthy of protection), but seeks merely to minimise or exclude competition, it would be against public policy and unreasonable. The court will not allow general or specialised skills and knowledge which belong to an employee (as part of his or her general stock of skills and knowledge) to be excluded from the labour market by way of a restraint of trade clause.

To summarise, it can be said that contracts in restraint of trade are, in principle, valid and enforceable. The law thus permits the restraint of a person's freedom of trade if parties freely conclude an agreement to this effect. The court will refuse to enforce the contract only if the circumstances of the case show that enforcement would be contrary to public policy, based on the principles enunciated above.

(f) Gambling contracts

The essential feature of a gambling contract is that one party undertakes to render performance to another if some uncertain future event, which is dependent on chance or luck, occurs; for example, if a particular dog wins a dog race. Games of skill which are not dependent upon chance or luck are normally contrasted with gambling: for instance, where a prize is awarded to the most competent player. However, where parties have no genuine interest in determining who is the best player, but merely play a game of skill with the specific object of trying to make money by staking an amount on the outcome of the game (thus a specific intention to gamble), the contract will be a gambling contract.

Betting, gaming, gambling and wagering are often used as interchangeable terms. Although certain gambling contracts were initially prohibited by legislation as they were considered too undesirable, it was found over time that legal disapproval would not stop people from gambling. The legislature consequently reflected a move away from prohibition of gambling toward its regulation with the Lotteries Act 57 of 1997 and the National Gambling Act 7 of 2004. These Acts provide that gambling or lottery debts incurred in the course of lawful, regulated or licensed gambling or lottery activities are valid and enforceable in a court of law.

Gambling or gaming debts resulting from unlawful, unregulated agreements remain subject to the common law. At common law a gambling contract is mostly valid. A party to such a contract may perform in terms of the contract and validly pay his or her debt. However, since such contracts are contrary to public policy, the law will not assist in their enforcement as they are generally regarded as encouraging

prodigality and wastefulness with detrimental and undesirable consequences for individuals and society. Consequently, such a gambling contract is not enforceable in a court. However, a gambling contract leads to a natural obligation between the contracting parties, implying that even though the law will not enforce the obligation arising from such a contract, it will still recognise its existence.

6.2.2 Contracts contrary to statutory law

Various contracts are contrary to statutory law because they are forbidden by an Act of Parliament, a provincial law, or by a municipal regulation — usually because they are

considered harmful to society. An agreement which is illegal or unlawful at common law is often also regulated by legislation to extend the original prohibition or to add criminal sanctions. The courts will hold an agreement to be void if to allow it would defeat the purposes of the legislation.

A contract contravenes a statutory law only if it contemplates a contravention of a prohibition, that is, if the contractual terms as such contravene a prohibition. There is no contravention of a prohibition if the agreement is merely concluded. The following example explains the situation. The law forbids the unauthorised trading in liquor without a licence for longer than one month. If a contract of sale is concluded between the owner of a licensed liquor store who wishes to sell his store to a purchaser who, at that stage, does not have a licence, but who has applied for one, the agreement as such is completely valid. If the purchaser does not obtain the licence in time and contravenes the prohibition, it will not affect the validity of the agreement as such.

Two examples of statutory prohibitions which could affect the validity of a contract are the sale of weapons and ammunition or of unpolished diamonds. A sale of these commodities by and to someone who does not hold the prescribed licence is prohibited.

A contract infringing any of the constitutional rights entrenched in the Bill of Rights (contained in Chapter 2 of the Constitution) may be illegal and unenforceable if it does not satisfy the requirements of the limitation clause, that is, that the limitation should be reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom, taking into account a number of factors.

6.2.3 Consequences of illegality

An unlawful or illegal 'contract' is, with a few exceptions, void under the common law. None of the parties acquire any enforceable rights and duties from the contract. Examples of these are agreements thwarting the administration of justice, agreements involving crimes and delicts and agreements affecting the safety of the state.

However, certain illegal agreements are not invalidated by their illegality but are merely unenforceable.

The effect of statutory illegality has to be determined with reference to the wording of the statute. Statutory illegality will void a proposed contract if the legislature makes its intention plain by enacting that an agreement in contravention of a prohibition will be null and void. However, such express provisions are not always present and, consequently, it is sometimes difficult to determine the effect of the contravention on an agreement. One school of thought advocates that what the law prohibits or penalises it also voids. The preferred approach, however, is to determine the intention of the legislature in all instances, as it is possible that the legislature considered the penalty a sufficient sanction without the need to void the contract. For instance, where a contract is reached in contravention of the anti-avoidance provisions of the Income Tax Act 58 of 1962, it does not render the contract void: it merely renders the taxpayer liable to prosecution and penalties.

Where an agreement is void owing to illegality, no party may institute an action against the other to claim a promised performance on the grounds of the unlawful agreement. This rule is expressed in the maxim known as *ex turpi causa non oritur actio* (no action arises from a shameful cause). This rule is never relaxed. Even if one of the parties has already rendered performance (such as payment of the purchase price), the court will not recognise that contract. The unlawfulness of the contract has a further consequence, namely, that a party who has suffered a loss as a result of the contract is not able to rely on the contract to claim damages. For example, Joe sells unpolished diamonds to Piet in contravention of a statutory prohibition. Piet pays in cash and Joe subsequently refuses to deliver the diamonds to him. Piet can claim neither the diamonds nor damages from Joe.

The question arises whether a person who has performed may reclaim his or her own performance on the ground of unjustified enrichment. This possible relief is usually not allowed either, as a result of the existence of a legal rule known as the *par delictum* rule. This rule is contained in the maxim *in pari delicto potior est conditio possidentis* (when there is equal guilt the possessor is in the stronger position). In the above example, Joe is in possession of the money agreed upon and, since he and Piet are equally guilty, Joe is in the stronger position. Therefore, Piet cannot reclaim the purchase price from him.

The *par delictum* rule applies to actions which are based on unjustified enrichment. Contrary to the application of the *ex turpi causa* rule, the courts have indicated that they are prepared to relax the *par delictum* rule where particular circumstances show that the public interest requires such relaxation.

The unlawfulness of a contract may also affect transactions connected to the contract. For example, Kylie and Dudu conclude an agreement in terms of which they agree to run a facility for providing illicit sexual services in partnership. They borrow money in terms of a separate agreement from Don for the construction of a building for this facility. It has already been stated above (see paragraph 6.2.1.2) that the agreement between Kylie and Dudu will be unenforceable as its purpose is contrary to good morals and thus contrary to the common law. But what about the loan agreement between Kylie, Dudu and Don?

The answer will depend on two principles. First, indirect enforcement of an unenforceable contract is never permitted. In the stated example the loan

agreement is not an indirect attempt to enforce the unenforceable partnership agreement between Kylie and Dudu. It is a separate but connected transaction. The second relevant principle is that a connected contract which helps or encourages the performance of the unlawful contract may also be condemned, depending on whether, in the court's view, the connected contract is causally connected to the unlawful contract or whether the connection is too remote to have any bearing upon the unlawful act. It has also been held

that a tainted act may not be 'unenforced' at the instance of the wrongdoers (Kylie and Dudu in the example), but it may be voidable at the instance of the innocent party (Don in the example).

6.3 Possibility and certainty of performance

A further requirement for the creation of a contract is that the performance of rights and duties flowing from the agreement must be objectively possible at the time of the conclusion of the contract. Furthermore, as it would be impossible to perform something which has not been determined and is not determinable, it is also required that the performance should be certain or ascertainable.

6.3.1 Objective possibility to perform

Performance will be impossible if, at the moment of concluding the contract, it is objectively (absolutely) impossible to render the performance (for example, the cow which Thandi sells to Paul has already died). No valid contract arises.

It is only objective impossibility of performance which causes the contract to be void. Objective or absolute impossibility implies that it must be totally impossible for anybody to perform in terms of the contract. If it is just impossible for a specific debtor or creditor to perform, but not necessarily for other people, the impossibility is merely subjective. If the performance is just inconvenient or difficult, the performance is also not objectively impossible, for instance, where the cow which Thandi sells to Paul in fact belongs to Charl, or where a purchaser is unable to obtain a loan from the bank to pay the purchase price. In both these examples performance is not absolutely impossible. In these instances the validity of the contract will not be affected unless an agreement to the contrary was reached. If the parties fail to perform, it will amount merely to breach of contract.

Impossibility of performance at the conclusion of the contract must be distinguished from performance which is possible at the moment of conclusion but which subsequently becomes impossible, and also from performance which is rendered impossible by the debtor after concluding the contract. These two aspects are discussed in chapters 10 and 12 below.

6.3.2 Divisibility of performance

Also of importance when determining whether a performance is possible is the divisibility or indivisibility of the performance. If an indivisible performance is objectively impossible, no valid contract arises. If only part of a divisible

performance is objectively impossible, a valid contract will arise in respect of the separable part which can still be performed.

Whether a performance is divisible or indivisible depends on the nature of the performance and the intention of the parties. The performance will be indivisible in character if it can be rendered in only one manner, namely, in its entirety (for example, where a person undertakes to deliver a house or a vehicle). On the other hand, a performance is divisible in character if it is physically possible to render the performance in separate units (for example, two horses) and if it is the parties' intention that the performance should be regarded as divisible. If a contract is divisible in the physical sense, there is still only one contract, although performance is divisible.

Divisibility is a legal concept. The law cannot convert a physically indivisible performance into a divisible one. The law can do the opposite, however, namely regard a physically divisible performance as indivisible. This will be the case, for example, where parties determine the price of a set of encyclopedias. Although it is possible to handle the books individually, the law will normally treat the set as indivisible with the result that the books must be delivered as a set. Whether the law will regard a particular performance as divisible or indivisible will depend on the subject matter of the contract and the intention of the parties. Determining the purchase price as an inclusive amount will normally be an indication that the performances of the purchaser and the seller are indivisible. Where the duty to pay is stated as an amount per unit, the law will normally regard it as an indication of divisibility. For example, where Thandi purchases two horses from Paul at R750 and stipulates that she will pay R500 for the one horse and R250 for the other, the parties' performances will normally be regarded as divisible, unless it was their intention to buy and sell the horses as a team. Where goods are sold as individual items, each with a fixed price, the transaction will, as a rule, be held to be composed of several contracts. The fact that two contracts are made at the same time and recorded in one document does not mean they should be reduced to one contract.

It has been held that to determine the intention of the parties, one should ask whether the contracting parties would have concluded separate contracts in respect of each part of the performance.

6.3.3 Determined and ascertainable performance

It is impossible to perform under an agreement where the nature of the performance is unclear and ambiguous: for instance, when the performance is not determined or ascertainable.

Whether or not a performance is determined, ascertainable or uncertain may depend on a contracting party's right, under the contract, to choose or identify a specific performance. The contracting party's right to choose or identify a specific performance is a contractual obligation based upon the exercise of a choice or formula. Because the manner in which the choice or identification is to be exercised may differ from contract to contract, the law has identified various types of obligations which are based on a right of choice. The law distinguishes

between a facultative obligation, which results in a determined performance, and alternative and generic obligations, where the exercise of the selection results in an ascertainable performance. This is discussed below.

6.3.3.1 The determined performance

Performance will be determined if the parties expressly mention the performance in their agreement. For example, the parties explicitly agree that Karel will buy the stallion, Blackie, from Vanja against payment of R15 000. The identity of the horse and the

purchase price are specified — both performances are determined. An example of a determined performance is also found in the facultative obligation.

In the case of some simple obligations the debtor is authorised to perform a different specified performance if he or she so chooses. This type of obligation is known as a facultative obligation. The obligation may, for instance, obligate the debtor, an art dealer, to deliver a painting, 'The Potato Eaters', but may allow the dealer, if he or she so chooses, to deliver another painting to the same value. In the facultative obligation the performance is determined from the beginning and the creditor is not entitled to claim a different performance — the creditor may only claim 'The Potato Eaters' from the art dealer. Performance remains determined and only the debtor may exercise another choice. If performance becomes impossible without any fault on the debtor's part, the debtor will be relieved of the obligation.

6.3.3.2 The ascertainable performance

The performance will be ascertainable if, at the time of concluding the contract, the parties agree on a criterion or a formula to identify the performance or if they agree that a specified person will determine the performance. The performance will be ascertainable, for example, if the parties agree that Kgomotso will buy the first heifer to be born on Vusi's farm, at a price to be determined by an outsider, Zola. The parties have thus laid down a criterion to determine the subject-matter of the contract and a method of determining the price.

Obligations are also ascertainable where the identification of the performance depends upon the exercise of a choice or the application of a formula. Alternative and generic obligations are further examples of such instances.

(a) The alternative obligation (performance of choice)

The alternative obligation exists where a party may select the performance which is due from two or more different alternatives, for example either of two horses, or one horse from a specified three. The objects from which the selection may be made, and the quantity that must be set aside, must be established at the time of concluding the contract.

Unless otherwise agreed upon, the debtor has the right of selection. When he or she has exercised his or her choice, the performance is no longer determinable, but is indeed determined. The choice is irreversible and the debtor is bound to deliver the chosen performance. Contrary to the position with a facultative obligation, where impossibility of performing the stipulated performance relieves the debtor

of his or her obligations, the impossibility of performing one of many alternatives will not relieve the debtor from his or her obligation, as he or she will have to choose between the remaining options, which would then be the only options.

(b) The generic obligation

In the generic obligation the performance is determined by describing a kind *(genus)* of commodity in terms of number (for example, 100 bags of mealies) or mass (for example, 100 tons of mealies) or measure (for example, a quantity of extra-large mealie kernels).

The generic obligation thus involves the selection of the performance from a specific *genus*. For a valid determination of the performance the contract must contain an indication of the following:

(i) The kind of commodity from which the selection must be made
(ii) The method of selection; be it according to number, mass or measure, and
(iii) The party who must make the selection. If there is no agreement about the person who may select, the right of selection resides in the debtor.

By separation of the performance, the generic obligation is converted into a simple obligation. The performance is no longer ascertainable, but indeed determined. The individualised object or objects must then be delivered.

Subject to the assumption that things of a particular kind do exist, a party to a generic obligation can never rely on impossibility of performance, since the kind cannot be extinguished.

Further reading

RH CHRISTIE *The Law of Contract in South Africa 6* ed (2011)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles 4* ed (2012)

Chapter 7
Formalities

7.1 Introduction
7.2 The general rule: No formalities required
7.3 Contracts where formalities are required

7.1 Introduction

The final factor that we take into consideration when determining whether a valid contract has come into existence is whether compliance with any formalities is prescribed for the formation of that particular type of contract. Formalities are those requirements relating to the outward, visible form in which the agreement must be cast to create a valid contract. These requirements may be stipulated either by the law or by the contracting parties themselves. Usually, compliance with formalities consists of reducing the contract to writing, with or without the signatures of the parties.

If the law requires that certain formalities must be observed, these requirements must be satisfied to create a valid and enforceable contract. Likewise, the formalities required by one or both contracting parties must also be complied with. However, if there is no express provision that certain formalities must be complied with, a contract will arise when parties who have the capacity to act reach consensus on obligations that are physically and legally possible.

7.2 The general rule: no formalities required

The general rule is that no formalities are required for the formation of contracts. In most cases an informal contract is binding and contracts are validly concluded without the observation of any formalities. For example, most contracts of sale arise orally or through conduct. If a person removes an item from a supermarket shelf and, without a word, offers a bank note at the point of payment, and the shop assistant accepts the money and allows the person to take the item, a contract of sale with the person arises tacitly through conduct.

Normally, parties are free to choose the way in which they wish to create a contract, and they may, at will, conclude the contract in writing, orally or tacitly. Thus, when parties wish to conclude a contract of lease of movable assets (a type of contract for which formalities are not required by law) they are free to decide whether the contract should be concluded in writing, orally or tacitly. When Anna offers to rent Bob's car, she may make the offer by having a formal letter drawn

up by an attorney, or by writing an informal note herself, or by making the offer orally. Bob may accept the offer in any of these ways, or by a mere nod of the head, or by handing over the keys to the car.

It is also possible for certain aspects of the contract to be in writing while other matters are agreed on orally or tacitly.

7.3 Contracts where formalities are required

7.3.1 Formalities required by law

It has been stated above that the prescription of formalities is the exception to the rule, and that at common law no formalities are required. However, the legislature has laid down certain requirements that must be satisfied when concluding certain types of contracts. These requirements are aimed mainly at preventing fraud and at reducing uncertainties and evidential problems. The most common requirement is that certain contracts have to be reduced to writing and should be signed in order to render them valid. For instance:

(a) Contracts for the alienation of land

According to the Alienation of Land Act 68 of 1981, no contract for the alienation of land is valid unless it is contained in a contract of alienation signed by the parties to the contract or by their agents acting on their written instructions. However, any alienation of land in contravention of the Act will be deemed to be valid if both parties have performed fully and the land has been transferred to the new owner. The Act also provides for special enrichment rules in case of invalidity due to non-compliance with the Act.

(b) Contracts of suretyship

The General Law Amendment Act 50 of 1956 provides that a contract of surety is valid only if it is in writing and signed by, or on behalf of, the surety.

(c) Contracts of donation in terms of which performance is due in the future

In terms of the General Law Amendment Act 50 of 1956, a contract of donation under which performance is due in the future is valid only if the terms thereof are contained in a written document that is signed either by the donor or by someone acting on his or her written authority. Such authority must be granted in the presence of two witnesses. A donation that has been completed by delivery and transfer falls outside this provision.

(d) Consumer contracts

In terms of the Consumer Protection Act 68 of 2008 (see chapter 30), a written record of each transaction which falls within the ambit of the Act must be given to the consumer. The written record must contain certain minimum information, such as the supplier's full name or registered business name, as well as its VAT

registration number. The Act provides specifically that a franchise agreement must be in writing and signed by, or on behalf of, the franchisee and that it must comply with the Act's requirements on plain and understandable language. The Act further provides that the Minister may prescribe certain further categories of contracts which have to be in writing. The mere fact that a consumer contract has not been signed by the consumer does not make it invalid. Where the Act compels the supplier to provide the consumer with a copy of the contract, free access to an electronic copy of the contract will suffice.

In other instances, although a written and signed contract is required by legislation, non-compliance will not automatically lead to invalidity of the contract. The National Credit Act 34 of 2005 does not specifically prescribe writing as a requirement for the validity of a credit agreement. However, from the provisions of the Act, it is clear that a credit agreement has to be in writing and signed by the parties. Section 93 of the Act provides that a document that records a credit agreement must be in the prescribed form, and if there is no applicable form for the type of agreement in question (see further chapter 16 for a discussion of the different types of credit agreement), it may be in any form that is determined by the credit provider. Section 93 further provides that the credit provider must, irrespective of the form of the agreement, provide the consumer with a copy of the agreement in a paper form, or in a printable electronic form. Although non-compliance with the requirement that the agreement be in writing will constitute a criminal offence by the credit provider, it will not lead to the invalidity of the credit agreement.

Other formalities may be required. For instance, the Deeds Registries Act 47 of 1937 requires an antenuptial contract to be registered in the manner and within the time mentioned in the Act. Unless registered, the antenuptial contract is of no force and effect against any person who is not a party to it. In other words, the antenuptial contract will be valid between spouses but not against third parties.

7.3.2 Formalities required by the parties

Apart from the instances where the legislature requires compliance with certain formalities to create a valid contract, it sometimes happens that the contracting parties themselves prescribe formalities. If the offeror sets the requirement that acceptance of the offer must be in writing, acceptance of the offer will result in a valid contract only if the acceptance is in writing.

Parties sometimes negotiate the contents of their contract orally and agree that the final agreement will be in writing. If an oral agreement precedes the written agreement, it must be determined from the contract whether the parties intended reduction to writing to be a requirement for validity or mere proof of their oral contract. If writing is a requirement for the validity of the contract, the 'contract' remains invalid until it is put in writing. Conversely, if the parties merely intended the written agreement to ease the proof of the oral agreement's terms, the oral contract becomes binding immediately upon conclusion, even though nothing has been put in writing.

7.3.3 Writing and signing of electronic transactions

As noted above, the most commonly prescribed formalities are those requiring the writing and signing of certain agreements. As more agreements are being concluded electronically, the Electronic Communications and Transactions Act 25 of 2002 (the ECT Act) provides that data messages (electronic messages) are recognised as writing if the document or information is accessible for future use, except in respect of transactions concluded under the following Acts:

- An agreement for alienation of immovable property as provided for in the Alienation of Land Act 68 of 1981
-

An agreement for the long-term lease of immovable property in excess of 20 years as provided for in the Alienation of Land Act 68 of 1981

- The execution, retention and presentation of a will or codicil as defined in the Wills Act 7 of 1953
- The execution of a bill of exchange as defined in the Bills of Exchange Act 34 of 1964
- The Stamp Duties Act 77 of 1968 (now repealed).

As it is impossible to attach a traditional handwritten signature to an electronic document, the ECT Act also provides that an electronic signature can legally fulfil the same function in certain circumstances. An electronic signature can be anything from the typing of a name at the end of a document, a scanned handwritten signature or the use of complex identification technology, as long as it is intended to be a signature.

Where a signature is required by law, only the use of an *advanced electronic signature* will comply, according to the ECT Act. This is defined as a signature which results from an accredited process allowing the recipient (as well as a third party certification authority) to verify the source of the communication (that is, the identity of the 'signatory') and that the communication has not been altered. Where a signature is not required by law, other methods may be used. The parties to an electronic transaction may either stipulate a specific type of electronic signature, or use an appropriate and reliable method which identifies the person and indicates his or her approval of the information communicated.

Further reading

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AJ Kerr *The Principles of the Law of Contract* 6 ed (2002)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles* 4 ed (2012)

Chapter 8
Terms of the Contract

8.1 Introduction: The term
8.2 *Essentialia, naturalia* and *incidentalia*
8.3 The condition
8.4 The time clause
8.5 The supposition
8.6 The warranty
8.7 The modus
8.8 The cancellation clause
8.9 The penalty clause
8.10 The forfeiture clause
8.11 The Rouwgeld clause (Rouwkoop clause)
8.12 The entrenchment clause

8.1 Introduction: the term

'Term' is a general word which covers all the specific provisions to be discussed in this chapter.

A term in a contract is a provision which imposes, on a contracting party, one or more contractual obligations to act in a specific manner or to refrain from performing a specific act, or which qualifies the contractual obligations. It thus defines the contractual obligations to which the parties bind themselves and which they can enforce against each another, or it stipulates the time when or the circumstances in which the obligations either become enforceable or are terminated.

Terms, which are statements made seriously and deliberately with the intention that they should be enforceable in law, must be distinguished from statements in respect of the contract made with no intention that it should have legal consequences. Sales talk or puffing, for example, is merely the excessive praise of performance and does not constitute a term of the contract. The following example will attempt to illustrate the distinction. Mmatau purchases a motor vehicle from Fast Cars Garage which is represented by a salesperson, Mia. The following statements are made during the oral agreement:

(a) Mmatau undertakes to purchase a red 1.3 litre Ford motor vehicle from Fast Cars Garage for R140 000: this is a contractual term as it imposes an

obligation on Mmatau to pay a certain amount, and on Fast Car Garage to deliver a specific vehicle.

(b) Mia informs Mmatau that the vehicle will be delivered the next Wednesday: this is a contractual term as it qualifies Fast Cars Garage's obligation.

(c) Mia informs Mmatau that the specific model is the cutest and most economical one of the range: this is not a term but mere sales talk. Other examples of sales talk are where a salesperson claims that the house he or she wishes to sell is the most beautiful in the neighbourhood, or that a specific play will certainly have the audience hysterical with laughter.

There are different ways of incorporating terms into a contract, namely, expressly, tacitly or by implication.

(a) Express terms

The contracting parties may incorporate terms into their contract by means of articulated declarations of intent. A term is articulated if it is expressed in so many words, whether in writing or orally.

The parties usually agree expressly on the in- or exclusion of a term to their contract. The Consumer Protection Act 68 of 2008 contains a number of further provisions regarding terms of a contract, including that a consumer contract may not contain unfair, unjust or unreasonable terms and conditions. The Act further provides that if a consumer contract contains a term or condition which may affect the consumer's rights, or which could not reasonably be expected in that type of contract, the supplier must draw the consumer's attention to such term or condition. (See chapter 30.)

(b) Tacit terms

A tacit term is a term which has not been expressed in words but is based on the parties' true intention, or their intention as imputed by the law. It will, for instance, be based on the parties' true but unexpressed intention where it had, in fact, been considered during negotiations but had seemed so self-evident as not to necessitate an express provision. An imputed tacit term is only read into a contract if both parties overlooked or failed to anticipate the event in question — it is based on their assumed intent in respect of a given situation they had not bargained for.

A tacit term is inferred by the court from the express terms and surrounding circumstances, which can include the recognition of terms customarily included or observed in a specific trade and which were known to both parties (terms arising from trade usages).

A tacit term is read into a contract only if it is reasonable and if it is necessary in a business sense for the proper functioning of the contract. The test to determine whether a tacit term forms part of the contract is to determine what the parties would have answered if, at the time of concluding the contract, someone were to have asked them what the position in respect of a specific situation or problem would be. If both parties were to answer that the position is as expounded in the alleged tacit term, the court would read the tacit term into the contract.

(c) Implied terms

An implied term is also a term which has not been expressed in words. It can be incorporated into the contract by operation of law. For example, the Consumer Protection Act provides that contracts which are regulated by the Act contain an implied warranty on repaired goods. Thus, under a consumer contract, the supplier warrants every new or reconditioned part installed during any repair or maintenance work, as well as the labour required to install it, for a period of three months, or for such longer period as the supplier may specify in writing. The period of three months is calculated from the date of installation.

When a contract has been classified as a particular type of contract, the law imputes certain consequences to the contract. For example, if the contract is typified as a contract of sale, a guarantee against latent defects is included in the contract by operation of law (see chapter 13). The guarantee against latent defects, therefore, forms part of every contract of sale unless the parties specifically alter or exclude it. Terms which are thus implied by law are usually referred to as the *naturalia* of that particular type of contract.

Terms can also be implied by trade usage if it is so universal and well-known that a party's knowledge and intention to be bound by it can be presumed. The trade usage would have to be long-established, reasonable, uniformly observed and certain. Trade usage is a hybrid type of term as it can either be inferred by the courts as a tacit term where the trade usage is known to both parties, or be recognised as an implied term in certain circumstances if one party cannot prove that the other party knew of the trade usage.

8.2 *Essentialia*, *naturalia* and *incidentalia*

Terms are classified as *essentialia*, *naturalia* or *incidentalia* for the purpose of providing a guideline for the analysis of different types of contracts.

8.2.1 *Essentialia*

Essentialia are those terms which are essential for the classification of a contract as belonging to a particular class or category of contract. For example, two *essentialia* of a contract of sale are that the seller binds him- or herself to deliver something to the buyer, and the buyer binds him- or herself to pay a sum of money in exchange for the asset. If the buyer is bound not to pay a price but to deliver some object in exchange for the asset, there is no contract of sale because an *essentialia* of sale is lacking; there may, however, be a contract of exchange. The *essentialia* of a contract therefore serve to identify a particular contract as belonging to a particular class or category of contract. Such identification is important as the category of the contract determines the *naturalia* of a particular contract. For example, if the essential elements of a contract of sale are present, certain results or *naturalia* would follow naturally by operation of law.

8.2.2 *Naturalia*

Naturalia are terms which the law attaches to every contract of a particular class. *Naturalia* help to determine the rights and duties of contracting parties and the effects and consequences of their contracts. The *naturalia* of many contracts known to South African law are based largely on ideas originating in Roman law, but have been adapted by our courts, legislation and trade usage. The operation of *naturalia* may generally be excluded by agreement between the parties. For example, a guarantee against latent defects is implied by law into all contracts of sale unless it is specifically excluded by the parties. In some instances the law prohibits or limits the right of parties to exclude the warranty against latent defects. For example, in terms of the Consumer Protection Act, the parties may only exclude the warranty against latent defects if certain requirements have been complied with.

8.2.3 *Incidentalia*

Once parties have agreed upon the *essentialia* of a particular type of contract, such a contract has been concluded in bare outline. Further details must usually be provided. *Naturalia* may fulfil this function, but if contracting parties have special requirements, additional terms may be inserted. These additional terms are referred to as *incidentalia*. Examples are the allowance of a certain time for paying the money due or for the paying thereof in instalments.

8.3 The condition

In common parlance the word 'condition' is often used to refer to what, in reality, is the all-inclusive concept 'term'. However, a condition is a particular kind of term and does not include all the terms generally found in contracts. A condition can be described as a contractual term which renders the operation (the coming into effect or the termination of the contractual obligations) and consequences of the contract dependent on the occurrence, or non-occurrence, of a specified uncertain future event.

The event must be specified: in other words, there must be no doubt which event will render the obligations operative or terminate them.

The event must also be uncertain: in other words, it must be uncertain whether the event will indeed occur. If Monica makes an offer to buy Tasneems's house 'if the sun rises tomorrow', she does not refer to an uncertain event because the rising of the sun is an event which, according to general human experience and expectation, will certainly take place. The reference to the sun's rising cannot, therefore, constitute a condition. If, however, Monica agrees to buy the house 'if the building society grants a loan within one month', she does refer to an uncertain event because it is uncertain whether or not the building society will grant the loan. In this case, then, Monica attaches a condition to her offer. The purchase is subject to a condition and the contract becomes operative only if the condition is fulfilled.

Since only future events can be uncertain, it stands to reason that a condition must refer to a future event. For example, Monica's offer to purchase will be

subject to a condition where she agrees to buy Tasneem's farm if oil is found on the farm as a result of the drilling which is currently being undertaken. It is uncertain whether oil will be found on the farm. Conversely, if Monica agrees to buy the farm subject to there being an oil well on the farm, she does not make the offer subject to a condition (even if she uses the words 'on condition' instead of 'subject to') because the existence of an oil well on the farm is not an uncertain future event. It can be determined objectively whether or not an oil well is in existence at the time of concluding the contract. The offer is therefore subject to an existing state of affairs: in other words, it contains a supposition. The supposition is discussed in greater detail below.

It is of practical importance to distinguish between conditions and other terms of contract as, for instance, the passing of risk in a contract of sale depends upon the contract being unconditional (see chapter 13).

Conditions can be classified into various categories (for example, positive and negative, voluntary, incidental and mixed, and so forth). In this discussion only the classification of conditions as suspensive or resolutive will be addressed.

8.3.1 The suspensive condition

A suspensive condition is a contractual term which suspends the operation of the contractual obligations in terms of the contract until the condition has been fulfilled.

Upon conclusion of an agreement containing a suspensive condition, a valid contract arises and a binding contractual relationship exists from which the parties cannot resile (withdraw). Although there is an existing binding contractual relationship, the operation of the contractual rights and duties are suspended until the condition has been fulfilled. Although conditional, the rights and duties exist. They can be ceded, are transferable upon death and are acknowledged in the event of insolvency. A creditor can also protect his or her conditional right by means of an interdict. The contractual rights and duties come into operation and become enforceable only when the condition is fulfilled. The condition will be fulfilled when the uncertain future event in fact takes place. If this specified uncertain future event does not take place, the condition is not fulfilled and the contractual obligations do not become operative but are terminated.

An example of a suspensive condition is the following: Makoshini makes an offer to lease Fred's car subject to the condition that she obtains a promotion and an increase in her salary within a certain period of time. If Fred accepts the offer, a contractual relationship between Makoshini and Fred comes into existence and they are bound to keep to the provisions of the contract. However, the contract does not come into operation. Its operation is suspended until the condition is fulfilled. Only when the condition is fulfilled (which will be the case if Makoshini obtains the promotion and increase within the specified period) may Fred claim payment of the rental money and may Makoshini claim delivery of the car. If the condition is not fulfilled (for example, because Makoshini is not promoted), the contractual relationship is dissolved and neither of the parties has an obligation

towards the other. The contract is terminated, and does not come into operation because the condition was not fulfilled.

8.3.2 The resolutive condition

A resolutive condition is a contractual term which renders the continued existence of the contract dependent on the occurrence (or non-occurrence) of a specified uncertain future event. If an agreement contains a resolutive condition, a binding contract comes into existence immediately upon the conclusion of the contract, and the contractual rights and duties become operative and are immediately enforceable. If the condition is fulfilled (namely, when the specified uncertain future event takes place), the contract is dissolved

and the contractual rights and duties cease to exist. Stated differently, the contract comes into operation when concluded and is undone by the fulfilment of the condition.

For example, Alan lets his farm to Bill. The parties agree that their contract will be dissolved if Allan marries. The contractual obligations become operative when the contract is concluded, but when Alan marries, the fulfilment of the condition causes the contract to be dissolved and terminated.

If parties have already performed prior to the fulfilment of the condition, and the contract is therefore dissolved after performance has been rendered, each party usually has to return whatever he or she has received in terms of the contract. For example, Mirry donates a vehicle to her cousin, Taryn, subject to the condition that Taryn must return the vehicle if she fails her examinations. The consequences of the contract become operative immediately the contract is concluded, and Mirry is obliged to deliver the vehicle to Taryn. If, at the end of the year, Taryn fails her examinations, the condition is fulfilled and the contract is terminated. The contractual relationship is ended and Taryn must return the vehicle.

However, complete restitution of performance subsequent to the fulfilment of the resolutive condition is not required in all types of contracts. Where a contract creates continuous obligations, in other words, regular performances by the party or parties over a period of time and not a single performance, complete restitution does not occur upon fulfilment of the resolutive condition. For example, Shantaal lets her house to Bongiwe subject to the contract being dissolved if Bongiwe is transferred to another city. When Bongiwe's employer in fact transfers her, the contract is dissolved and the obligations which would have been due in the future are terminated. However, Shantaal need not repay the rental which Bongiwe has paid in respect of the completed period during which Bongiwe occupied the house. In these circumstances the contractual obligations already complied with are not undone, and the rental already paid cannot be reclaimed.

8.4 The time clause

The time clause must be distinguished from the condition. Unlike a condition, where a contract comes into operation or is dissolved upon the occurrence or non-occurrence of a specified uncertain future event, the time clause is brought into

operation by the reaching of a certain and determined or ascertainable time which has been agreed upon.

The time clause determines a specific time when (for example, 1 January 2017) or the period within which (for example, six months after conclusion of the contract) the contract will either become operative or be dissolved. The moment must be specified so that there is no doubt about the exact moment which will result in the fulfillment of the time clause. The moment is one which, according to ordinary human experience, is certain to take place. No uncertainty can exist about whether the moment will take place. Exactly when it will take place may be either certain or ascertainable. The moment will be certain if it is specified in the contract, for example, Christmas Day 2017. It will be ascertainable if it can be determined with reference to a moment or an event mentioned in the contract, for example, the moment of the insurance policy holder's death. Time clauses can be either suspensive or resolutive.

8.4.1 The suspensive time clause

The contract is subject to a suspensive time clause if the duty to perform is postponed until a determined or ascertainable moment has arrived. The consequence of a suspensive time clause is that the contract comes into being when it is concluded, and the parties are bound to the obligations; but the rendering of their performances in terms of the contract is postponed until the moment has arrived or the period has lapsed. The contractual obligations come into operation and are enforceable only when the specified moment arrives or when the specified period ends. The enforceability of the rights and duties are, therefore, postponed until the determined or ascertainable moment has arrived.

For example, Molapho undertakes that he will buy Elna a new vehicle after Lyle's death. It is certain that Lyle will die, although it is uncertain when he will die. The moment for performance is therefore determinable. When the contract is concluded, a contractual relationship between Molapho and Elna arises and both of them are bound by the contract. However, the performance is enforceable only after Lyle's death.

8.4.2 The resolutive time clause

The contract is subject to a resolutive time clause if the parties agree that the obligations flowing from the contract will have effect only until the arrival of a certain moment or until the expiry of a certain period of time. In this case the contract comes into being when it is concluded and the obligations are immediately operative so that performance is immediately enforceable. When the moment arrives, however, the obligations are extinguished.

For example, Bongiwe rents Shantaal's house for a period of two years. When this period of two years expires, the resolutive moment has arrived and the obligations are extinguished. Bongiwe's obligation to pay the rental, as well as Shantaal's obligation to make the house available to Bongiwe, is terminated.

8.5 The supposition

A contractual term which renders the existence of the contract dependent on an event which has taken place in the past, or on a state of affairs which existed or exists at the time of concluding the contract, is known as a supposition. Contracting parties will include a supposition when they are uncertain whether a specific situation exists or existed, and they only wish to contract if it, in fact, exists or existed. If a contract rests on a supposition, contractual obligations come into being only if what is supposed indeed exists or existed.

Since suppositions are sometimes couched in words referring to 'conditions' (for example, '… conditional upon …'), such 'conditions' must always be examined carefully to determine whether they are suppositions in law or true conditions. An example of a supposition is the following: Manoj is the owner of a plot in a coastal town. Frans wants to purchase the plot only if it has a sea view. Manoj does not know whether this is the case and is not willing to give a guarantee in this regard. They agree that Frans will purchase the plot provided it has a sea view. If the sea is indeed visible from the plot, obligations are created from the beginning. Conversely, the contract creates no obligations if the plot does not offer a sea view. This is not a condition as it does not relate to the happening of an uncertain future event. It is a supposition as the contract depends on an existing state of affairs.

By providing that the operation of the contract is subject to a supposition, a party's motive for concluding the contract may become a term of the contract. This can be explained by the following example. Anthony wants to buy a stallion from Pete because he is under the impression that his own stallion, Blackie, has contracted a terminal disease and has died. If he simply buys the stallion without subjecting the operation of the contract to the supposition that Blackie has died, a contract arises between Anthony and Pete upon conclusion of their agreement, and the parties are bound irrespective of whether Blackie is dead or alive. Blackie's supposed death is Anthony's motive for buying the other stallion, and Blackie's death or health has no effect on the contractual obligations. Anthony's mistaken motive, if Blackie has not, in fact, died, will not relieve him of his liabilities. However, Anthony can make his motive a term of the agreement by expressly subjecting his offer to buy Pete's stallion to the supposition that Blackie has died. If it is then determined that Blackie is alive, no obligations ensue from the agreement. If Blackie is indeed dead at the moment of conclusion of the contract, the contract is enforceable.

8.6 The warranty

A warranty is a contractual term whereby a contracting party accepts absolute responsibility for proper performance relating to the absence of defects in the warrantor's product or service, or to the possibility that the warrantor is able to render the performance, or to the quality or standard of the warrantor's product or service, or to the quantity of the performance, et cetera.

Although the word 'warranty' is sometimes used to express any promise in regard to the debtor's basic performance (for example, to deliver a particular vehicle), we are concerned here with the special usage of this word, namely, as a specific term

in a contract. In law the concept 'warranty' is a qualification of the nature of the obligation promised, in the sense that the debtor assumes an additional obligation when he or she provides a warranty. The additional obligation forms part of the contract as a result of the express inclusion of the warranty. For example, if Koos sells a refrigerator to Bert and guarantees that the exterior paint of the refrigerator will retain its original colour for three years, Koos undertakes an additional obligation. The result of this term is that, if Koos delivers the refrigerator and the exterior paint, in fact, discolours within the period of the warranty, Koos is in breach of contract.

These additional obligations are not always indicated by the word 'warranty'. Sometimes the word 'guarantee' or other words are used. The terms of the contract must be interpreted to determine whether a warranty is intended by the parties.

Apart from warranties that are expressly agreed upon by contracting parties, certain warranties can form part of a contract by operation of law. In terms of our common law, such terms form part of certain contracts unless expressly excluded by the contracting parties. Examples of these are warranties against latent defects, and against eviction in contracts of sale. It is important to distinguish between expressly incorporated warranties and warranties incorporated by operation of law, as the remedies which are available in the case of a breach may differ. The breach of a contractual term constitutes a breach of contract. Consequently, whenever a party does not honour a warranty, he or she will be in breach of contract. The innocent party will be able to make use of the legal remedies available for breach of contract as discussed in chapter 11. Conversely, if the implied common-law warranty against latent defects is breached, the purchaser will, depending upon the degree of the defect, be entitled to the remedies of the *actio redhibitoria* or the *actio quanti minoris* (see chapter 13).

8.7 The modus

A modus is a contractual term which burdens a contracting party's right to the performance made to him or her in terms of the contract. The burden can be to perform towards a third party, or to do something, or to refrain from doing something. The burden will always relate to something that has to happen in the future.

For example, Nelson donates a house to Podile, subject to the modus that she must use part of it as a nursery school. The contract is unconditional and Podile can enforce Nelson's performance immediately, even if she has not yet complied with the modus. Podile can therefore claim delivery of the house immediately, but if she subsequently fails to execute the charge, she is guilty of breach of contract and Nelson can use the ordinary contractual remedies. A further example of a modus is where a father donates his farm to his son subject to a modus that the son must pay a specified sum of money to his sister. The son can claim delivery of the property immediately, even before he has paid the money to his sister. He is, however, contractually bound to pay the money to his sister, and failure to do so will constitute breach of contract.

8.8 The cancellation clause

The cancellation clause entitles a contracting party to cancel the contract summarily if the other party is in breach of contract. If such a term is included in the contract, the party in whose favour the cancellation clause is stipulated can cancel the contract without further ado as soon as the other party breaches the contract. It is unnecessary to send a letter of demand or a notice warning the other party of the intended cancellation of the contract (see chapter 11).

8.9 The penalty clause

8.9.1 General

The law and, more particularly, the common law, attaches certain consequences to breach of contract by affording certain remedies to the innocent party. Depending on the type of breach committed, the innocent party can claim execution of the contract, or cancel the contract, and/or claim damages. Sometimes, however, contracting parties find these common-law remedies insufficient, and they incorporate 'remedies' of their own design into the contract in order to further penalise the party who is in breach, or to deter him or her from breaching the contract by the threat of a further penalty. A penalty clause is an example of this.

The obligation imposed by a penalty clause usually consists of the payment of a sum of money. In most building contracts, for example, the owner and the building contractor agree that the construction work must be completed on or before a certain date. A penalty clause is added to the contract in terms of which the building contractor must pay the owner a certain sum of money for each day the construction operations continue beyond the date of completion agreed upon. If the contractor breaches the contract by failing to complete the construction work in time, the penalty clause becomes operative and he or she must pay the sum of money stipulated. The addition of such a term to the contract is an effort to penalise the contractor for late completion of the work. Essentially, a penalty clause is a calculation of damages in advance. At the same time it serves to deter non-compliance with the obligations agreed upon.

A penalty clause can also consist of an obligation to deliver something, or to render another performance. A clause stipulating that the debtor will remain liable for performing, even if the creditor cancels the contract, also amounts to a penalty clause, as does a forfeiture clause, discussed below. Since such contractual penalty measures can have iniquitous results, the legislature attempted to impose some measure of control over the use of such clauses by enacting the Conventional Penalties Act 15 of 1962. The Act provides that a penalty clause is enforceable, subject to the court's discretion to reduce the extent of the penalty to an amount which it considers reasonable in the circumstances. A penalty will be unreasonable if it is out of proportion to the prejudice the creditor suffered as a result of the debtor's breach of contract. The debtor bears the onus of proving that the penalty is out of proportion to the prejudice suffered by the creditor.

The question of reduction of the penalty will ordinarily have to be brought to the court's attention by the debtor, who bears the onus of proving that the penalty is out of proportion to the prejudice suffered by the creditor, although the court may act on its own initiative.

The penalty creditor derives the following basic benefits from the penalty clause:
(a) The penalty is recoverable merely on the ground of the debtor's breach of contract.
(b) The extent of the penalty is predetermined.

Since the penalty is recoverable merely by reason of the fact that the debtor has committed breach of contract, there is no need for the creditor to prove damages or the extent thereof. The creditor merely has to prove the debtor's breach of contract.

The penalty is intended as a substitute for damages. The Act therefore prohibits the creditor from claiming damages as well as the stipulated penalty. The creditor can claim only one or the other: in other words, either damages or the penalty. The Act does allow parties to stipulate in the contract that the creditor will have a choice between claiming a penalty and claiming damages. If the contract expressly provides for such a choice, the creditor is entitled to hold the debtor liable on either of these two grounds. However, if the contract does not expressly provide for such a choice, the creditor is limited by the Act to enforcing the penalty and the alternative right to damages is lost. The underlying principle is that the creditor, of his or her own free will, negotiated for the remedy of a penalty, and that remedy was chosen as a replacement for the claim for damages the creditor would have had at common law.

8.9.2 The National Credit Act and penalty clauses

In considering the enforceability of penalty clauses, one has to distinguish between at least three types of contract or scenario:
(a) those contracts which are governed by the National Credit Act 34 of 2005 as well as the Conventional Penalties Act
(b) those contracts which are governed by the Conventional Penalties Act only, and
(c) those contracts which are governed neither by the National Credit Act nor by the Conventional Penalties Act.

It is sufficient to mention here that the National Credit Act contains provisions which affect the enforceability of certain penalty clauses. Section 101 of the National Credit Act provides for the different types of cost (including penalty charges in the guise of, inter alia, 'default administration charges') that a consumer may be required to pay under a credit agreement.

Where a contract is governed by both the National Credit Act and the Conventional Penalties Act (scenario (a) above), the possibility exists that the provisions of the National Credit Act, on the one hand, and those of the Conventional Penalties Act, on the other, may be in conflict. Schedule 1 to the National Credit Act (see

s 172(1)) provides that, in the case of conflict between the provisions of these two Acts, the provisions of the National Credit Act will prevail 'to the extent of the conflict'. At this stage it is a vexed question whether bank default charges (for example, the charge levied by a bank when a client draws a cheque while there are insufficient funds in the former's account to honour the cheque) qualify as a penalty charge.

In the case of scenario (b) above, the validity and enforceability of the penalty clause will be determined by the provisions of the Conventional Penalties Act.

In the case of scenario (c) above, the validity and enforceability of the penalty clause will be determined by the common law.

8.10 The forfeiture clause

A party who is entitled to cancel or rescind a contract in certain specified circumstances will normally be entitled to restitution as well. The right to restitution entitles the party who cancels or rescinds the contract to claim the return of everything he or she has already performed in terms of the contract. However, by including a forfeiture clause in their contract, parties agree that one of them, or both, will lose this right to restitution in certain circumstances. In this way a forfeiture clause makes provision for a party who is in breach of contract to lose the right to restitution. The party who is in breach therefore forfeits all performances already rendered in terms of the contract. For instance, a contract of sale can provide for a purchaser who commits breach of contract to forfeit all instalments which have already been paid.

The provisions of the Conventional Penalties Act in respect of penalty clauses apply to forfeiture clauses. For instance, forfeiture clauses are subject to reduction at the discretion of the court in a similar manner as penalty clauses.

8.11 The Rouwgeld clause (Rouwkoop clause)

A *rouwgeld* clause must be clearly distinguished from a penalty clause. Whereas a penalty clause becomes operative only in the event of breach of contract, a *rouwgeld* clause is not connected to a breach of contract. Accordingly, a *rouwgeld* clause is not subject to the provisions of the Conventional Penalties Act.

If a contract contains a term to the effect that a party may withdraw from the contract upon the payment of a certain sum of money, we are dealing with a *rouwgeld* clause. If the clause relates to a contract of sale, it is called a *rouwkoop* clause. The amount payable is known as *rouwgeld* money (or *rouwkoop* money) because it represents the amount to be paid for the right to dissolve the agreement.

A *rouwkoop* clause which commonly forms part of contracts for the sale of land is a provision that the purchaser must pay a deposit when signing the contract and that, if he or she withdraws from the contract, the deposit will be forfeited as *rouwkoop* money. For example, Mpho sells his house to Nonzizwe and the contract contains a *rouwkoop* clause which provides that, should Nonzizwe withdraw from the contract, Mpho may retain, as *rouwkoop* money, the R5 000 deposit Nonzizwe

paid when concluding the contract. As soon as Nonzizwe withdraws from the contract, the *rouwkoop* clause comes into operation and she forfeits the amount of the deposit as *rouwkoop* money. The *rouwkoop* clause entitles Nonzizwe to cancel the contract. No further consequences, adverse to Nonzizwe, flow from her dissolving the contract. Because she acts in terms of the contract her withdrawal does not amount to breach of contract. Mpho can claim neither specific performance nor damages.

8.12 The entrenchment clause

A contractual term which provides that the agreement may be altered only by means of written amendment is known as an entrenchment clause. Such a term has the effect that the contract may not be varied by an oral agreement, even if the parties are in complete agreement in regard to the proposed amendment.

Further reading

RH Christie & GB Bradfield *The Law of Contract in South Africa* 6 ed (2011)

AJ Kerr *The Principles of the Law of Contract* 6 ed (2002)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles* 4 ed (2012)

Chapter 9
Interpretation of the Contract

9.1 Content of the contract
9.2 Principles of interpretation

9.1 Content of the contract

The content of a contract consists of the terms incorporated into that contract by the parties. These terms can be incorporated orally, tacitly or in writing.

Where parties verbally or tacitly agree on the promised performance, the content is evident from their words and conduct.

Where the agreement is in writing, the content of the contract is generally determined from the document. Where the written agreement has been signed, the signatory is usually bound by the ordinary meaning and effect of the words which appear over his or her signature, as the signature signifies assent to the document. This rule is referred to as the *caveat subscriptor* rule. The only defences available to a signatory of a document would be misrepresentation, fraud, illegality, duress, undue influence and mistake.

In the case of unsigned written agreements, other evidence may be necessary to prove that the document is a true reflection of the contractual terms. This situation is often referred to as the 'ticket cases', as unsigned documents are often used by bus services, airlines, theatres, sports stadiums and similar entities. The description may, however, be used to cover all cases where a supplier provides customers with a document containing the terms on which the supplier is prepared to do business and which is not intended to be signed, whether the document is an actual 'ticket' or not. This includes a notice on a website to the effect that the use of the website or the placing of an order will be subject to the standard contract of use of the site or of the sale.

'Click-wrapped' agreements, whereby a customer wishing to make use of the services offered by a website is instructed to 'click' on a certain icon, thereby indicating acceptance of the terms of contract offered by way of a linked page, are specifically provided for in the Electronic Communications and Transactions Act 25 of 2002. The Act provides that the click-wrapped information will be incorporated into the agreement if the reference to it would be noticed by a reasonable person and where it is accessible to the buyer in a form which is readable, retrievable and capable of being stored. These agreements cannot be classified as 'ticket cases' as the customer indicates his awareness of the contractual terms by clicking on the required button or icon on the website.

Unfortunately, uncertainty or conflict regarding the exact content of a contract often arises. This results in a need to interpret the content of the contract in order to determine the true intention of the parties and the obligations they intended. In resolving these conflicts, the interpreter (usually the courts) uses certain principles or techniques which have evolved over time.

9.2 Principles of interpretation

In principle, there is no difference between contracts concluded in writing, orally or by conduct. Apart from specific exceptions where compliance with formalities is required, the

validity of a contract is not affected by the manner of its creation. The same principles of interpretation can usually be applied when interpreting all contracts, irrespective of the manner of conclusion.

The purpose of the interpretation of contracts is essentially the determination of the parties' intention. This is the most important principle of the interpretation of contracts.

Certain rules, guidelines or techniques serve to facilitate the determination of the parties' intention. These rules or techniques of interpretation mostly assume that a written document is in issue, but it should be kept in mind that, unless obviously inappropriate, these rules apply to oral agreements as well. Some of these guidelines are the following:

(a) It is accepted that the parties normally use all words in their ordinary grammatical meaning. Words that carry a technical meaning, or which are used in a specific manner within a particular branch of business or profession, will be interpreted in accordance with that specific usage.

(b) After ascertaining the literal meaning of the words or phrase, the context in which the words are used, the contract as a whole and the surrounding circumstances are taken into account: for instance, by considering the purpose of the contract, previous negotiations between the parties, and subsequent conduct of the parties showing the sense in which they acted on the document. Note that the use of surrounding circumstances is not in contravention of the parol evidence rule (see later) where it is merely referred to as an interpreting aid in determining the meaning of the words used and not in order to prove a contradicting term.

(c) If any uncertainty or ambiguity remains with regard to a word or a phrase, the courts sometimes interpret the clause against the party who was responsible for its drafting.

(d) The law also uses various presumptions. One such presumption is that the parties intend their agreement to be valid and enforceable. The courts will, therefore, attempt to interpret the contract in a manner that will not affect its validity. Another important presumption is that the parties do not intend to deviate from the common law unless, and only to the extent that, this is expressly indicated. Thus, where parties express themselves on a particular matter but omit some detail, the common-law rules will regulate that aspect.

(e) When a contract is reduced to writing, the parol evidence rule is brought into operation (discussed in greater detail below).

A special set of interpretive rules has been formulated to deal with the so-called ticket cases mentioned above. A supplier would be entitled to assume assent where:

(a) the customer reads and understands the document and, by his or her conduct (entering the theatre, boarding the plane), indicates that the terms have been accepted;
(b) it is impossible to prove that the customer read the document, but the supplier took all reasonable steps to ensure that the customer was alerted to the terms and the customer thereafter, by his or her conduct, indicated that the terms were accepted.

If the contract is so obscure that the parties' intention cannot be determined even with the aid of these guiding principles, the contract is void for vagueness.

9.2.1 The parol evidence or integration rule

Where agreements are involved or lengthy, or where there is a likelihood that a difference of opinion might arise with regard to the exact terms of the contract, such terms are often recorded in writing so as to avoid or minimise arguments about the content of the contract. The fact that the agreement is reduced to writing brings the parol evidence rule (also known as the 'extrinsic evidence rule' or the 'integration rule') into operation, irrespective of whether the eventual document is the outcome of extensive negotiation and consultation, or whether it is a standard-form contract which a consumer signed without even having looked at its terms.

In terms of the parol evidence rule, once a contract has been reduced to writing or integrated into a single complete document, the written document is the only record of the agreement, and it is this document which has to be interpreted in order to determine the content of the contract. The document containing the parties' agreement stands as the only evidence of the terms of their contract.

The effect of this rule is that once a contract has been recorded in writing and the written contract purports to reflect the whole contract on a particular subject matter, a contracting party will not be allowed to submit evidence in the form of agreements reached before or simultaneously with the conclusion of the integrated written agreement which contradict, alter or add to the terms of the integrated written agreement.

It is important to note the parameters of the rule carefully. It is clear that the rule will, *inter alia*, not apply in the following instances:

(a) It does not affect evidence of an agreement concluded subsequent to the written contract, even if it varies or contradicts the written contract, and even if it makes additions to, or exclusions from, the written contract. Evidence of such a subsequent contract will indeed be admissible as the parol evidence rule applies only to contracts reached prior to, or simultaneously with, the

integrated written agreement. If the written contract contains an entrenchment clause, such subsequent alterations must obviously be in writing.
(b) It does not prohibit the evidence of, for instance, prior inducing agreements where the terms of the earlier (or simultaneous) document do not contradict, alter, add to or vary the terms of the integrated written agreement.
(c) As the rule only extends to extrinsic evidence, which tends to contradict the terms of the integrated written contract, evidence to prove —
    (i) the nullity or voidability of the contract as a whole is not subject to the rule. For instance, evidence to show that the written contract was subject to a true condition suspending the operation of the contract, which was not expressed in the document, is allowable.

(ii) objectively determinable facts recorded in the document are also not subject to the rule. For example, evidence that the document was signed at a particular time and place is allowed.

Section 55(2)*(e)* of the Consumer Protection Act contains an important exception to the integration rule. The Act empowers the court to ensure fair and just conduct, terms and conditions in a consumer contract. One of the factors which the court must consider is whether, at the time the contract was entered into, there was any negotiation between the supplier and the consumer, and, if so, the extent thereof. This can affect the parol evidence rule, because section 55(2)*(e)* allows the court to take into account evidence outside the written record of the contract in interpreting the terms and conditions of the contract.

9.2.2 Rectification

Sometimes a written document does not reflect the true intention of the parties to the contract because an error slipped in when the agreement was put into writing. For example, the purchase price of a plot, or the plot number, is stated incorrectly as a result of a typing error. As a result of the operation of the parol evidence rule, the parties will not be able to submit extrinsic evidence which is in conflict with the terms of the integrated written contract. To prevent this state of affairs the law recognises that, in appropriate circumstances, a written contract may be improved in order to record the parties' true intention. Thus rectification is permissible if the parties who apply for it can prove —

(a) the parties' true intention, and
(b) that the written document does not accurately reflect it.

Rectification can generally not rectify a failure to comply with a formal statutory requirement. For instance, where the law requires a signature, failure to sign an agreement cannot be rectified. While the courts accept that this interpretation may have anomalous results, its application is seen as a means of upholding the objectives of a specific statute.

An interesting exception in this regard concerns unsigned wills. Section 2(1) of the Wills Act 7 of 1953 provides that a will must be signed by the testator for it to be valid. Section 2(3) of the Law of Succession Amendment Act 43 of 1992

provides relief in those cases where a will was drafted on the instruction of a testator, but had not yet been signed at the time when the testator passed away. Section 2(3) provides that such an unsigned 'will' may be declared valid by a court. Note that section 2(3) does not provide for rectification of the will, but for condonation of the non-compliance with a statutory requirement.

Further reading

RH Christie & GB Bradfield *The Law of Contract in South Africa* 6 ed (2011)

AJ Kerr *The Principles of the Law of Contract* 6 ed (2002)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles* 4 ed (2012)

Chapter 10
Breach of Contract

10.1 Introduction
10.2 Default of the debtor
10.3 Default of the creditor
10.4 Positive malperformance
10.5 Repudiation
10.6 Prevention of performance

10.1 Introduction

The primary purpose when creating contracts is their fulfilment or discharge by due and proper performance. Unfortunately, not all contracts end in this way. Where the intended result is not achieved as a consequence of the fault of one of the parties, that party commits breach of contract.

There are five different forms of breach of contract:

(a) default by the debtor
(b) default by the creditor
(c) positive malperformance
(d) repudiation
(e) prevention of performance.

Before the various forms of breach are discussed, it is necessary to say something about debtors and creditors in the breach of contract situation. As will be discussed later, some of the forms of breach can be committed by both a debtor and a creditor, while others are unique to the obligation of either a debtor or a creditor. The terms 'debtor' and 'creditor' are used in relation to a specific obligation of the contract and not to the contract as a whole. The debtor is the party who has to perform a specific obligation, while the creditor is the party who is entitled to performance of the obligation in question. Where a contract creates obligations for both parties, each will, in turn, be a debtor and a creditor, depending on which obligation is involved. Let us illustrate this by an example. In a contract of sale two of the most important obligations are the obligation of the purchaser to pay the purchase price and the obligation of the seller to deliver property (the *merx*). In respect of the obligation to pay the purchase price, the purchaser is the debtor and the seller is the creditor. But when the delivery of the *merx* is involved, the seller is the debtor

and the purchaser the creditor. If the purchaser is in breach of contract by not paying the purchase price, it is the debtor who is committing breach of contract. Likewise, if the seller delivers a defective *merx*, he or she is breaching the contract as debtor. However, when the seller refuses to accept payment, or if the purchaser destroys the *merx* so that it cannot be delivered to him, the breach of contract in both instances is by the creditor.

10.2 Default of the debtor

A debtor commits breach of contract in the form of default of the debtor, also referred to as *mora debitoris*, if he or she does not perform at the agreed time, and the delay is without legal justification. It is then said that the debtor is in *mora* or in default.

10.2.1 Requirements

There are two requirements that have to be met:

(a) Performance must be delayed. In the case of default of the debtor, the latter is only late with his or her performance. If, in any other way, the debtor's obligations are not honoured, for example, by the rendering of defective performance, the debtor does not commit *mora debitoris*, but possibly another form of breach of contract, for example, positive malperformance. It must also still be possible to perform at a later stage. In some contracts the time at which performance must take place is so closely linked to the content of the obligation that proper performance cannot take place after the specified time. In such a case the debtor's culpable failure to perform at the agreed time will not constitute *mora*, but another form of breach of contract, namely, prevention of performance. For example, Naledi has to do the catering for Fattima's wedding reception on 12 November 2014. On the day of the wedding Naledi does not arrive to cater for the reception because she negligently wrote the wrong date in her diary. Naledi's failure to perform on the day of the wedding is not *mora debitoris*, but prevention of performance. Although Naledi can probably still deliver the food agreed upon at a later stage, this will not amount to proper performance. The wedding reception is over and it is no longer possible to cater for it. Because the time at which performance had to take place was an integral part of Naledi's performance, she has made her own performance impossible by not performing at that time.

(b) It is obvious that the performance must already be claimable, or there can be no question of late performance. If the enforceability of the obligation depends on a suspensive condition or time clause, performance will be claimable only once the condition has been fulfilled or the period has expired. The terms of the contract may either provide for a specific day or time for performance of the respective obligations, or no time may be specified. A day or time for performance could be agreed on by the parties expressly or tacitly. An example

of a tacit agreement on the time of performance is where I call an emergency plumber to fix a serious water leakage. In such a case, the plumber and I have tacitly agreed that performance must take place immediately. Where no date or time for performance of the obligations is fixed in the contract, either expressly or tacitly, there is an implied term that performance is to take place within a reasonable time.

(i) Where a specific date or time for performance has been stipulated and the debtor fails to perform on or before the appointed time, he is automatically in *mora*. This situation is termed *mora ex re*. The specific date for performance that is referred to here must be a day of which it is both certain **that** it will arrive and **when** it will arrive, for example 31 March 2014, or immediately. If a contract specifies that Stephen has to perform on the day when André dies, Stephen will not automatically be in *mora* (*mora ex re*) if he fails to perform on that day, because although it is certain **that** André will die, it is uncertain **when** this will happen. The Supreme Court of Appeal, however, confirmed that a debtor may fall into *mora ex re* even where the contract permits a degree of latitude in regard to the time for performance, for example, where the contract requires performance on 'about 1 December'. It will always be a matter of interpretation how much latitude is intended. So, if a debtor fails to perform on 'about' a specific date, he or she may also be automatically in *mora*.

(ii) Where no exact date for performance has been specified, the creditor can determine a date by demanding that the debtor perform before or on a certain date. Although a demand may be made orally, it is always advisable to put the demand in writing. However, it is required that, when fixing a date, the creditor must allow the debtor a reasonable time within which to perform. The determination of a reasonable time will depend on the circumstances. The debtor falls in *mora* if he or she fails to perform on the determined date. In this case, it is said that the debtor is in *mora ex persona*. A demand is also necessary to place the debtor in *mora* if the time for performance is a day of which it is certain that it will arrive, but uncertain when it will arrive. Stephen, in the above example, will only be in *mora* (*mora ex persona*) if, after André's death a specific date for his performance has been determined by demand and he has failed to perform on that date.

Until recently it was believed that fault of the debtor was a requirement for breach of contract in the form of default of the debtor. However, the Supreme Court of Appeal recently held that fault is not a requirement for default of the debtor. On the other hand, if a legal justification exists for the delay, there will be no breach of contract: for instance, no breach of contract exists where the debtor cannot perform timeously owing to bad fortune or circumstances beyond his or her control, for example, where the debtor has undertaken to deliver goods and the ship carrying the freight is delayed by a storm at sea. However, if the debtor has

warranted performance at a particular time, late performance will constitute breach of contract even if there is legal justification for the debtor's delay. The reason for this is that by giving the guarantee, the debtor assumes the risk of a delay.

10.2.2 The consequences of the debtor's default

Default of the debtor entitles the creditor to the remedies for breach of contract, to be discussed in chapter 11. In addition to this, it also has an effect on the liability of the debtor should performance become impossible while he or she is in *mora*. As a general rule, supervening impossibility of performance extinguishes the obligation, releasing the debtor from the duty to perform. However, if performance becomes impossible after the

debtor has fallen in *mora*, such supervening impossibility of performance does not have the effect of extinguishing the obligation, with the result that the debtor who is in *mora* may not claim to have been relieved of his or her obligation where performance has become impossible.

10.3 Default of the creditor

Default of the creditor, or *mora creditoris*, as it is also referred to, occurs where the creditor causes the debtor's performance to be delayed. *Mora creditoris* is a form of breach of contract which can occur only where discharge of the debtor's obligation involves a bilateral juristic act, that is, where the creditor's co-operation is required for the debtor to be able to render performance. This would be the case, for example, where Saul and Roger contract that Roger will lay carpeting in Saul's house and where Saul, therefore, has to co-operate in allowing Roger's workmen access to the house.

10.3.1 Requirements

The following are the elements of *mora creditoris*:

(a) The performance must be dischargeable. The performance owing to the creditor must be dischargeable in terms of an existing and valid obligation and must be physically and legally capable of being discharged. Performance will not be dischargeable until any related suspensive condition is fulfilled, or until it is time for the performance if, by the relevant time clause, the parties intend that performance should not occur before a particular date.

(b) The debtor must tender performance. The debtor must offer proper performance as specified in the contract and must call upon the creditor to co-operate. If the tendered performance is defective, the creditor may refuse to accept it. The creditor's refusal will, in this case, not constitute breach of contract.

(c) The creditor must fail to give his or her co-operation and thereby delay performance. If an exact date has been set for the creditor's co-operation, the creditor will automatically be in default (*mora ex re*) if he or she does not co-operate on that day. If no specified date for performance or co-operation has been agreed upon, the debtor has to call upon the creditor to co-operate

and fix a date for such co-operation. The creditor will be in *mora ex persona* if he or she does not co-operate on the date determined in the demand. As in the case of *mora debitoris*, the performance should merely be delayed and it must still be possible for the debtor to perform at a later stage. If the time at which performance should take place is an integral part of the performance, the creditor's failure to accept performance at the agreed time will, if the other requirements are present, amount to prevention of performance by the creditor.

10.3.2 The consequences of the creditor's default

When the creditor is in default, the following consequences arise:

(a) The debtor's duty of care is diminished if the creditor is in *mora*; the debtor is responsible only for intentional loss and loss occasioned by gross negligence.

(b) In the case of reciprocal agreements, the debtor remains entitled to the performance due to him or her. The creditor's *mora* may thus not be used by the creditor to escape from his or her obligation to perform. Of course, the debtor also remains liable for his or her performance and will have to perform later. In other words, the obligations of the parties are not terminated as a result of *mora creditoris*.

(c) Should the performance become impossible (other than through intention or gross negligence of the debtor), while the creditor is in *mora*, the debtor is released from the obligation to perform. However, the creditor remains liable for the counter-performance. For example, if a creditor, in terms of a building contract, is in *mora* in respect of taking delivery of the completed building and the building is destroyed by an earthquake, the creditor remains liable for the contract price.

(d) If the debtor is in *mora*, it is removed by the subsequent default of the creditor. Default by one party is always extinguished if the other party subsequently falls in *mora*, since these two forms of breach of contract cannot exist alongside each other in respect of the same obligation. If Thabo has to pay an amount to David on 30 April, but fails to do so, Thabo will be in *mora debitoris*. If Thabo then informs David that he will pay the amount on 2 May and calls on David to receive the payment, David will be in *mora creditoris* if he does not co-operate to receive Thabo's payment on 2 May. From this date Thabo will no longer be in *mora* because he has tendered proper performance. (In this example we assume that David has not cancelled the contract owing to Thabo's *mora*.) However, the fact that the earlier *mora* is extinguished does not mean that any liability for it will also be extinguished. The creditor can, for example, still claim damages if he or she has already suffered loss as a result of the debtor's default. It is possible, of course, that *mora debitoris* and *mora creditoris* may exist simultaneously, but then in respect of different obligations. In fact, it often happens in a reciprocal contract that the party who does not perform timeously at the same time does not co-operate to receive the other party's performance. The first-mentioned party will then be in both

forms of *mora* simultaneously. For example, Imran sells a computer to Jim and they agree that Jim will pay when Imran delivers the computer at Jim's house on a specific day. On the agreed date Jim is not home and Imran cannot deliver the computer. Jim is in *mora creditoris* because as creditor he did not co-operate so that Imran could perform. At the same time Jim also did not meet his obligation as debtor, namely, to pay, and in respect of that he is in *mora debitoris*.

10.4 Positive malperformance

Positive malperformance is that form of breach of contract which occurs when the debtor commits an act which is contrary to the terms of the contract. Performance can be that a

person must do something or must refrain from doing something. For this reason, there are two situations which can be distinguished with regard to positive malperformance:

(a) The debtor tenders defective or improper performance: for example, the house which he or she has undertaken to build is built, but with finishes inferior in quality to those specified in the contract.

(b) The debtor does something he or she may not do in terms of the agreement. For example, the debtor carries on business in competition with his or her former employer in violation of a contractual term (restraint of trade) prohibiting such conduct.

10.5 Repudiation

Repudiation as a form of breach of contract is understood as any behaviour by a party to a contract indicating that he or she may not honour the obligations under the contract. A party can behave in this way with regard to all his or her obligations in terms of the contract: for example, where the existence of the contract, is denied: where the party tries without justification to withdraw from the contract, or where the party gives notice that he or she cannot or will not perform. However, it is also possible for a party to repudiate only some of his or her obligations or a part of the contract, for example, where the party offers inadequate or defective performance as proper performance.

Under these circumstances the innocent party is not expected merely to wait and bear the risk that the other party might really not honour his or her obligations. Repudiation already constitutes breach of contract, entitling the innocent party to the usual remedies for breach of contract. However, the innocent party is not obliged to take steps at this stage. He or she can reject the repudiation and wait until the repudiating party eventually commits another form of breach such as *mora* or positive malperformance. In such a case the earlier repudiation need not be proved.

It can sometimes be very difficult to establish whether certain behaviour constitutes repudiation. The basic question is whether the person alleged to have repudiated his or her obligation has behaved in a way that would lead a reasonable

person to conclude that the repudiating party does not intend to fulfil his or her part of the contract. It is thus not the intention of the repudiating party that is conclusive, but the perception of a reasonable person in the position of the innocent party. The test is an objective one in which the conduct of the repudiating party is assessed against the background information available to the innocent party.

10.6 Prevention of performance

10.6.1 Prevention of performance by the debtor

The debtor commits breach of contract in the form of prevention of performance where he or she culpably renders his or her own performance impossible. In this case, the debtor is not released from the obligation to perform. Because the debtor can no longer perform as agreed, he or she will have to pay damages instead of performing. For example, the debtor has to develop and print a photographic film for the creditor, but negligently exposes it to light before development is completed. The photos can no longer be printed. Although performance has been made impossible, the debtor can be held liable for the loss suffered by the creditor.

10.6.2 Prevention of performance by the creditor

The creditor who culpably renders the debtor's performance impossible commits breach of contract in the form of prevention of performance. For example, the debtor has to service the creditor's motor car, but before this can be done, the creditor negligently causes an accident in which the motor car is destroyed. Prevention of performance by the creditor must be distinguished from default of the creditor, or *mora creditoris*. In the case of prevention of performance by the creditor the debtor's performance is made impossible and, consequently, can never be rendered. In the case of *mora creditoris*, the creditor merely delays the debtor's performance but does not render it impossible, so that it is still capable of being rendered.

Where performance has become impossible through the fault of the creditor, the debtor will be deemed to have discharged his or her obligation. The debtor is still entitled to the creditor's performance, but the debtor must bring into account any expenses which have been saved by reason of the debtor no longer being obliged to perform. In the above example, the debtor need no longer service the creditor's motor car, but will be entitled to payment of the contract amount less any savings, for example, on the oil and spare parts that would have been used.

Further reading

RH Christie & GB Bradfield *The Law of Contract in South Africa* 6 ed (2011)

AJ Kerr *The Principles of the Law of Contract* 6 ed (2002)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles* 4 ed (2012)

Chapter 11
Remedies for Breach of Contract

11.1 Introduction
11.2 Execution of the Contract
11.3 Cancellation of the contract
11.4 Damages

11.1 Introduction

Where one party to a contract commits breach of contract, the rules of the law of contract protect the innocent party's personal rights and grant him or her redress in the form of a legal remedy which can be enforced through an action in a court of law. The legal remedies at the disposal of the innocent party are execution of the contract, cancellation of the contract, and damages. The availability of the respective remedies is determined by the nature and seriousness of the breach of contract which has been committed, and also by the terms of the contract.

Execution of the contract is the primary remedy, while cancellation can be seen as an additional remedy for breach of contract. The remedy of execution of the contract is, in principle, available with respect to all the forms of breach of contract. In general, the remedy of cancellation of the contract is also available with respect to all the forms of breach of contract, but only if the breach is of a serious nature or if the contract contains a cancellation clause.

The remedies of execution of the contract and of cancellation of the contract are mutually exclusive and the innocent party has a choice between the one and the other. Although the innocent party can claim the two remedies in the alternative, enforcement of the one excludes the other.

Where the innocent party suffers damage as a result of the breach of contract of the other party, he or she is also entitled to claim damages as a remedy. This is so, irrespective of whether the innocent party has cancelled the contract or claimed the execution thereof.

11.2 Execution of the contract

The remedy of execution of the contract is the obvious remedy for breach of contract, since it attempts to achieve the same result as was intended originally by the parties, or a result that is as close as possible to that. Execution of the contract can comprise one of three possible orders, namely:

(a) an order for specific performance
(b) an order for reduced performance
(c) a prohibitory interdict.

11.2.1 Orders for specific performance

An order for specific performance is a court order which commands a contracting party to render the performance he or she has undertaken to render. However, such an order will not be made or enforced against a person whose estate has been sequestrated, since it

may prejudice the other creditors. An order for specific performance also cannot be granted where performance is no longer possible, since the law cannot force anybody to do the impossible. In such a case the innocent party can claim damages in lieu of performance.

In all other cases the court has a discretion, and will consider making an order for specific performance. The aim of the exercise of the discretion is to prevent injustice and to make a decision in accordance with legal and public policy. In principle, the public interest requires that debtors meet their obligations even if they find it inconvenient and even if the contract is unreasonable. The court will, in making its decision, take into account all the available evidence and facts in accordance with the above-mentioned aim. Grounds on which the court will refuse an order for specific performance include where such an order would affect the defendant unreasonably harshly, or where the order would comprise an injustice or would be inequitable under all the circumstances: for example, where the cost to the defendant in being compelled to perform is out of all proportion to the corresponding benefit to the plaintiff. It is not a rule of our law that specific performance will be denied in respect of an obligation to render personal services. The situation will be judged according to the same principles as any other performance, namely, whether ordering specific performance would be inequitable to the debtor. The court could order specific performance of one or some of the obligations undertaken by the debtor while refusing to do so in respect of other obligations or terms.

11.2.2 Orders for reduced performance

In certain circumstances the court will order a contract party to render a reduced performance. This can happen if the other contract party has rendered performance, but his or her performance is defective or incomplete. In principle, incomplete performance by one party would entitle the other party to refuse to render his or her counter-performance. The vast majority of contracts in the commercial world create rights and duties for both parties. When there is a connection between the obligations of the respective parties, in the sense that the different obligations are undertaken in exchange for one another, the principle of reciprocity is present. The intention of the parties is the decisive factor in determining reciprocity.

The principle of reciprocity means that the plaintiff can claim the defendant's performance only if he or she has performed or is willing to perform. Subject to the terms of the contract, the party whose performance is being claimed has the

right to withhold it until the party claiming performance renders or tenders (offers) his or her own performance. This means that when the plaintiff who has rendered incomplete or defective performance claims performance from the defendant, the defendant can defend him- or herself and refuse to perform by relying on the fact that the plaintiff has not yet performed in full. This defence is called the *exceptio non adimpleti contractus* (that is, the defence of the incomplete contract).

The *exceptio* — the defence that the plaintiff, that is, the party claiming the performance, has not fulfilled his or her part of the contract — is available only where performance by both parties must occur simultaneously, or where the plaintiff must perform before the defendant. The *exceptio* is not available to the defendant where the plaintiff has cancelled the contract because of the defendant's breach of contract and where the plaintiff is claiming damages instead of performance. It is also not available where the plaintiff does not have to perform, for instance, in the case of a contract of donation.

The effect of the operation of the principle of reciprocity and of the *exceptio non adimpleti contractus* is that, where the plaintiff who seeks to rely on specific performance by the defendant has not rendered his or her own performance or is not willing to perform, or has rendered defective performance, the court will not order specific performance. This situation can be illustrated by the following example: Podile sells a set of ten books to Sifiso at a price of R2 000. When Podile delivers the books to Sifiso, she informs Sifiso that she has lost one of the books. Sifiso refuses to pay the R2 000 and Podile wants to claim specific performance by Sifiso, that is, payment of the R2 000. Sifiso can now raise the *exceptio non adimpleti contractus* as a defence against Podile's claim. He is entitled to withhold payment until Podile delivers the remaining book or offers to do so. The principle of reciprocity and the *exceptio* would, therefore, constitute an absolute bar to the remedy of specific performance for as long as a plaintiff fails to render or tender his or her own performance.

However, where fairness requires it, a court may, at its discretion, refuse to allow a defendant to rely on the *exceptio* and order him or her to render a reduced counter-performance. In this way the contract is enforced despite the fact that the plaintiff (creditor) has rendered or tenders incomplete or defective performance. Because the plaintiff's or creditor's performance was incomplete, the court then orders the defendant or debtor in turn to render only a reduced performance, and not the full performance which he or she had undertaken to render. In the above example, the court could, for example, order Sifiso to pay R1 800 instead of the R2 000 because he has received only nine of the ten books.

The court will grant a plaintiff an order for reduced performance only if he or she has proved the following:

(a) that the defendant is using the defective performance
(b) that the circumstances are such that it would be equitable for the court to exercise its discretion in favour of the granting of such an order
(c) what the reduced contract price should be, that is, the contract price less the amount required to bring the performance up to the required standard.

In our example it will thus depend on the circumstances whether the court will grant an order for reduced performance. If Sifiso specifically wanted to obtain a complete set of books, for example, owing to its collector's value, and is not using the nine books, it is unlikely that the court will grant an order for reduced performance. In these circumstances Sifiso would probably already have cancelled the contract owing to Podile's defective performance. If, however, Sifiso is using the nine books and could easily obtain the outstanding book elsewhere, an order for reduced performance will probably be granted.

11.2.3 Prohibitory interdicts

Should a party do something he or she may not do in terms of the contract, or threaten to act in this manner, the other party may apply for an interdict to end or prevent such conduct. For example, if a party conducts business in contravention of a restraint of trade agreement, the other party can obtain an interdict prohibiting the first-mentioned from continuing to compete.

11.3 Cancellation of the contract

Cancellation is an abnormal remedy for breach of contract, because the consequence is that the parties do not accomplish that which they originally agreed upon. Since it is a general principle of our law that persons should be bound by their contracts, this remedy is not necessarily available in every case of breach of contract. The parties can expressly agree in their contract that one or both of them will be entitled to cancel the contract if the other party commits breach of contract. The cancellation clause will determine under which circumstances the remedy will be available — it could limit cancellation to certain degrees of breach of contract, or it could be cast in wide terms so as to allow cancellation in every instance of breach of contract. Such a cancellation clause is also called a *lex commissoria*.

If a contract does not contain a cancellation clause, the innocent party will be entitled to cancel the contract only if the breach of contract is material, that is, of a serious nature. The availability of cancellation can best be described in relation to each form of breach of contract individually.

11.3.1 Cancellation and default of the debtor

In the event of *mora debitoris* the creditor will have the remedy of cancellation in the following circumstances only:

(a) **Specific date for performance (*mora ex re*) and tacit term that timely performance is essential.** When the time for performance is stipulated and where there is no cancellation clause, the failure to perform by the stipulated date may be such a serious breach of the contract that the creditor will be justified in cancelling the contract. In these cases the time for performance is said to be of the essence to the contract. In effect, a tacit term of the contract, that the creditor is entitled to cancel the contract in the event of the debtor's

failure to perform on or before the stipulated date, is construed. The mere fact that a contract specifies an exact date for performance does not mean that time is of the essence to the contract. Such a tacit term that time is of the essence might possibly be construed where the contract applies to goods that are subject to continuous price fluctuations, or where the contract is a so-called commercial contract.

(b) **Notice of intention to cancel.** If the debtor is in *mora* with a substantial part of his or her obligation, the creditor can acquire a right of cancellation by sending the debtor a notice of the intention to cancel the contract. By giving notice of the intention to cancel the contract, the creditor acquires a right of cancellation as if such a right had originally been included in the contract by means of a cancellation clause. In other words, the creditor will be entitled to cancel the contract in the event of the debtor's default, even if there is indeed no cancellation clause in the contract, provided the creditor gives the debtor notice of the intention to cancel the contract. The creditor's notice of intention to cancel must allow the debtor a reasonable time within which to perform, and must state clearly that the creditor will lay claim to a right of cancellation if the debtor fails to perform by the date stipulated. In cases where no date for performance is stipulated and where the creditor, therefore, first has to demand performance from the debtor in order to place him or her in *mora ex persona*, it is permissible for the creditor to combine the demand with a notice of intention to cancel, thereby not only fixing a date for performance but also acquiring a right of cancellation. Where the debtor is already in *mora ex re*, but time is not of the essence to the contract, the demand is used only to acquire a right of cancellation.

(c) **Cancellation clause.** If the parties have agreed that the creditor can cancel the contract in the event of the debtor's default, the creditor will be able to cancel the contract even if the default is not a material breach of contract.

11.3.2 Cancellation and default of the creditor

The innocent party will be entitled to cancel the contract for *mora creditoris* under the same circumstances as those for *mora debitoris*, namely:

(a) **Specific date for performance (*mora ex re*) and tacit term that timely performance is essential.** In this case it is essential that the creditor co-operates to allow timely performance by the debtor.

(b) **Notice of intention to cancel.** The debtor notifies the creditor that he or she will cancel the contract if the creditor does not co-operate to receive the debtor's performance.

(c) **Cancellation clause.** If the parties have agreed that the debtor can cancel the contract in the event of the creditor's default, the debtor will be able to cancel the contract even if the default is not a material breach of contract.

11.3.3 Cancellation and defective performance (positive malperformance)

The creditor will be entitled to cancellation of the contract following defective performance by the debtor in the following circumstances:

(a) **Material breach of contract.** Where the defect is of such a serious nature that the creditor cannot reasonably be expected to abide by the contract, the creditor may cancel the contract. When a court has to decide whether the creditor is entitled to cancellation, it will balance the competing interests of the two parties, bearing in mind that cancellation is a more radical remedy than specific performance or damages.

(b) **Cancellation clause.** If the parties agreed on a cancellation clause, the creditor will be able to cancel the contract in the agreed circumstances, even if the performance is not materially defective.

11.3.4 Cancellation and repudiation of the contract

Cancellation will be available in the following instances:

(a) **Material repudiation.** As in the case of cancellation for materially defective performance, the repudiation must be repudiation of a materially important obligation before the innocent party will have the option to cancel the contract. It is important to note that the innocent party remains entitled to rather seek an order for execution of the contract even where the guilty party is unwilling to accept the counter-performance tendered by the innocent party.

(b) **Cancellation clause.** If the parties agreed on a cancellation clause, the innocent party will be able to cancel the contract in terms of the cancellation clause, even if the repudiation does not relate to a materially important obligation.

11.3.5 Cancellation and prevention of performance

Prevention of performance by the debtor entitles the creditor to cancellation, since execution of the contract is no longer possible. However, if the creditor has prevented the performance of the debtor, the debtor is regarded as having performed and can either insist on performance by the creditor or claim cancellation.

11.3.6 The act of cancellation

Where a contract party becomes entitled to cancel the contract, he or she must make a choice between cancelling the contract and enforcing it. It is important to note that the innocent party is not compelled to cancel. The innocent party always has the choice of claiming execution of the contract, but if performance has been made impossible, he or she will have to be content with damages in lieu of performance.

The Supreme Court of Appeal has confirmed that a right of cancellation must be exercised within a reasonable time after the innocent party has become aware of the other party's breach of contract. If the innocent party has not cancelled the

contract within a reasonable time, the assumption could be made that this remedy has been waived. However, the right of cancellation does not lapse merely because the innocent party takes unreasonably long to exercise or make known his or her choice. The innocent party still has the opportunity to explain why it took so long and that he or she has not waived the right of cancellation.

Although the act of cancellation usually consists of a notification to this effect, the choice which the creditor has made might also appear from his or her conduct. If the creditor accepts or retains defective performance, or uses it, he or she will be deemed to have elected to enforce the contract. The same goes for where the creditor fails to exercise a choice within a reasonable time or where he or she acts in any way which is irreconcilable with the intention to cancel. The party who obtained a right of cancellation can, without forfeiting the right of cancellation, give the other party the opportunity of rectifying his or her defective performance. However, such a party has to make it clear that the giving of such an opportunity is only conditional and that the right to cancel in case the other party does not perform satisfactorily is reserved.

The innocent party exercises the right of cancellation by notifying the other party of the cancellation. The notice of cancellation can be in any form (oral or written), as long as it is clear and unequivocal. It is sufficient if the innocent party's decision to cancel, or his or her conduct indicating this election, is reported to the guilty party by a third person acting independently. A mere threat to cancel is not yet a cancellation.

From the point of view of proof it is, of course, always advisable that important juristic acts be put in writing. If the contract itself prescribes requirements with regard to the act of cancellation, for example, that it can only be done in writing, such requirements must, of course, be complied with.

11.3.7 The consequences of cancellation

The major consequence of cancellation is the termination of the obligations. If neither of the parties has performed, both of them are relieved of their obligations to perform. The general rule is that if either one or both of the parties have performed, whatever has been performed by the other party must be returned to him or her (restitution). However, a court may, in certain circumstances, dispense with restitution if the court considers it equitable to do so, irrespective of the innocent party's ability to make restitution.

If restitution has become impossible, the party who is cancelling the contract is relieved of the duty to return the performance which has been received, as long as the impossibility is not due to his or her fault. Where restitution has become partially impossible, the party has to return that which is left.

If it is impossible for the guilty party to return the innocent party's performance the innocent party need also not return the guilty party's performance.

Where a contract involving continuing obligations is cancelled, the rights that have accrued prior to cancellation are not affected.

11.4 Damages

It is fair to assume that when parties conclude a contract, they have its fulfil-ment in mind. In general, therefore, the policy of the law is to regard the fulfilment of contractual obligations highly. One of the remedies which the law puts at the disposal of the innocent party, where he or she has suffered loss as a result of the breach of contract of the other party, is damages.

The underlying idea of the remedy of damages is that the innocent party's patrimony should not be allowed to be diminished by the defendant's breach of contract, and that

the innocent party should, by means of the payment of damages, be placed in the position he or she would have been in had the contract indeed been carried out.

Whenever a party to a contract has suffered loss as a consequence of the other party's breach of contract (irrespective of the form of the breach of contract), the innocent party is entitled to damages as a remedy, whether he or she has cancelled the contract or claimed its execution.

11.4.1 Patrimonial loss

The mere fact that one of the parties has committed breach of contract does not mean that the other party has necessarily suffered loss. Before it can be said that the innocent party has suffered loss, it must be clear that patrimonial loss occurred, that is, the breach of contract must have adversely affected the value of the innocent party's patrimony (estate). Compensation, for example, for pain and suffering, cannot be claimed on the basis of contract, even where the impairment of personality was the direct result of breach of contract. Compensation can, however, be claimed on the basis of delict.

The loss a plaintiff has suffered can consist of the amount by which the value of his or her patrimony would have increased through proper performance, or the amount by which his or her patrimony has decreased because proper performance did not take place. The following two financial positions are, therefore, compared with each other:

(a) the financial position the plaintiff would have been in if the contract had been carried out and breach of contract had not occurred
(b) the plaintiff's actual financial position.

The difference (should the first-mentioned exceed the last-mentioned) constitutes the plaintiff's loss. The importance of this remedy lies therein that the defendant must compensate the plaintiff, to the extent that this can be done by the payment of money, for the patrimonial loss suffered by him or her as a result of the breach of contract. The debtor must, by payment of the damages, place the innocent creditor in the same patrimonial position he or she would have been in had proper and timeous performance taken place. For example, if the creditor would have made a profit from the contract, he or she can claim that profit. The innocent party has to be compensated to the amount of his or her positive interest in the performance of the contract. This is in contrast with negative interest which applies when the

injured party has to be placed in the position he or she would have been in had the agreement never been entered into. (Negative interest is claimed where unlawful conduct has taken place, for example, when the conclusion of a contract has been influenced by misrepresentation, duress or undue influence.)

11.4.2 Causal connection between breach of contract and loss

The breach of contract must have caused the loss or, put differently, the loss must have been a consequence of the breach of contract. The innocent party may, therefore, claim damages only for losses which resulted from the breach of contract.

If factors other than the breach of contract, including the negligent conduct of the innocent party, also caused or contributed to the loss, the guilty party will nevertheless be liable as long as the breach was one of the causes of the loss.

A court will not adjust the damages to reflect the degree to which the loss was caused by the breach on the one hand and the other factors on the other hand. The Apportionment of Damages Act 34 of 1956 allows for an apportionment to be made in instances of contributory negligence of the injured party and it also regulates contributions between joint and several wrongdoers. However, this Act applies only in respect of claims based on delict. In claims based on contract, the party who has breached the contract will be liable for the full amount of the loss that was caused by the breach. The following example can illustrate this principle: Thandi negligently writes out a cheque for R10 in a way that makes it easy to change the amount of the cheque. The amount is indeed altered to R1 000 by the party who deposits the cheque. Thandi's bank then acts negligently by paying the cheque without noticing the alteration. Thandi claims R990, the difference between the two amounts, as damages arising from the bank's breach of contract. Because the bank's negligence was one of the causes of the loss, and since the action is based on breach of contract, the bank is liable for the full loss even though Thandi's negligence contributed to the loss.

11.4.3 Foreseeable loss

In some circumstances the defendant will not be liable for the patrimonial loss of the other party, despite the fact that it resulted from the breach of contract by the defendant. The following example can serve as an illustration: Danie sells a watch to Gugu. For some time the watch runs perfectly, but one day it suddenly stops owing to a defect. As a consequence of this, Gugu misses her train and cannot keep a very important business appointment. As a result, she loses a considerable amount of money, and is declared insolvent. Among other things she is unable to pay for the education of her children as a result of this. It would not be fair to hold Danie liable for all these consequences, despite the fact that it may be argued that they were all caused by Danie's breach of contract. For which of the aforementioned consequences should Danie then be held liable?

The defendant's liability is limited to such loss as naturally and generally flows from the kind of breach of contract in question, or alternatively such loss

as was actually foreseen by the parties, or may reasonably be supposed to have been contemplated by them as a probable consequence of breach of contract. To establish what the parties actually contemplated, or may be supposed to have contemplated at the time the contract was concluded, regard may be had to the subject-matter and terms of the contract itself, or the special circumstances known to both parties at the time of conclusion of the contract. The test for determining whether damages flow naturally and generally from the breach is whether, having regard to the subject-matter and terms of the contract, the harm that was suffered can be said to have been reasonably foreseeable as a realistic possibility.

11.4.4 The duty to mitigate damages

The defendant will not be held liable for loss, arising after breach of contract, which the injured party could have limited by exercising reasonable care. For example, Bert undertakes to deliver ten kilograms of frozen chicken at Alfred's premises at 9:00 on 31 March. Bert arrives to deliver the goods at the appointed time, but finds the premises locked and nobody present. It appears that Alfred was negligent in not making arrangements for the receipt of the chicken. Thus Alfred has breached the contract through *mora creditoris*. Bert will be able to recover his loss in attempting another delivery at a later stage (for example, the transport costs). But if he leaves the frozen chicken outside the premises in the sun and it rots, he will not be able to recover the cost of replacing the chicken, because he has not taken reasonable steps to limit his loss. Bert could have taken the chicken back and stored it for later delivery, claiming the extra costs of delivery and storage as damages. The onus will be on Alfred to prove that Bert could have limited his loss by taking reasonable steps.

11.4.5 The proof of loss and the calculation of damages

As has already been shown, the loss to the innocent party who has been the 'victim' of the defendant's breach of contract consists of his or her positive interest, namely, the difference between the value his or her patrimony would have had had the contract been carried out, and the actual value of his or her patrimony at the time of the breach of contract. Translating this principle into practical realities has proved to be an exceedingly difficult task. The following are some of the typical yardsticks used in practice:

(a) Where the contract is a contract of sale in respect of a marketable commodity and the *merx* is not delivered on time, the damage is usually expressed as the difference between the contract price and the market value of the commodity at the time and place performance should have occurred.
(b) In the event of failure to discharge a money debt, interest is awarded as damages, calculated from the due date for payment.
(c) In the case of the defective execution of a piece of work, the amount which it would cost to repair the defect, or the amount which it would cost to have the work done by somebody else, may be awarded as damages.

Proof of the loss suffered is, almost without exception, one of the most critical aspects of the litigation between plaintiff and defendant. In a civil case the onus of proving the loss which he or she has suffered rests on the party who claims damages.

Further reading

RH Christie & GB Bradfield *The Law of Contract in South Africa* 6 ed (2011)

AJ Kerr *The Principles of the Law of Contract* 6 ed (2002)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles* 4 ed (2012)

Chapter 12
Transfer and Termination of Personal Rights

12.1 Introduction
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12.1 Introduction

Although personal rights can be terminated in various ways, they can be transferred in one way only, namely, by way of cession. Cession will now be discussed and, thereafter, the ways in which obligations can be terminated.

12.2 Cession

The rights flowing from a contract are personal rights, that is, rights to claim performance by the other party to the contract. Like any other asset in a person's estate, a personal right is capable of being transferred. The transfer of a right by agreement is known as 'cession'. The person who transfers the right is called the 'cedent', and the person to whom it is transferred, the 'cessionary'. For example, Manelisi owes John R100. John in turn owes Sam R100. John and Sam agree that John will transfer (cede) his claim (personal right) against Manelisi to Sam. John is the **cedent** and Sam the **cessionary**. Cession is thus an agreement between the holder of a right (a creditor, John in our example) and a third party (Sam in our example), to the effect that the third party shall henceforth be the holder of the right. In other words, it is an agreement by which a personal right is transferred to another creditor.

Cession is not a means of terminating an obligation, since the original obligation continues to exist. Neither does it create new obligations. The debtor merely has to perform to a new creditor.

In general, cession of rights may take place freely. However, the parties to the contract may agree that the rights under the contract will not be ceded. The law may also prohibit cession. For instance, the cession of a statutory pension or a right to such a pension is prohibited by legislation. The right to maintenance also cannot be ceded. Closely related to this is the rule that a right cannot be ceded where the claim is so intimately connected with the person of the creditor that the exercise of it by somebody else will encumber the debtor with a materially different obligation. So, for instance, one who has hired the services of a physician, or a portrait painter, will not be able to transfer his or her right to such services to a third party by way of cession.

A debtor's position may not be prejudiced by a cession. It is this consideration that lies at the root of the prohibition against a cession of part of a claim. Generally speaking, a

right can be ceded only in its entirety. Where Manelisi owes John R100, John is not allowed to cede his claim to the amount of R60 to Sam, and to retain the balance or to cede it to Maggie, unless Manelisi consents to such a splitting of the claim. Such a cession could result in Manelisi's having to defend himself against two or more claims, accompanied by higher costs.

Should the debtor have a counter-claim against the cedent which is not yet capable of being set off — for instance, because it is not yet claimable — the debtor will no longer be able to set off his or her counter-claim against the main claim. This consequence is not usually considered to be prejudicial to the debtor's position.

However, if a claim is ceded with the *mala fide* intention on the part of both cedent and cessionary of depriving the debtor of the right to raise a counter-claim against the cedent, the debtor will be able to raise his or her counter-claim as a defence against the cessionary. The cessionary will then have to defend him- or herself against the counter-claim.

In general, cession is effected without formality. The parties can make clear their intention to cede by any means, be it orally, or by delivery of the document evidencing the right, or by an endorsement on the document itself. However, delivery of the document evidencing the right is not required in order to effect a valid cession.

The parties to a contract may, of course, also stipulate that the right created by the contract will be transferable only in a certain way, for example, in writing or with the consent of the debtor.

12.2.1 The consequences of cession

The transfer of the right from the cedent to the cessionary has several consequences:

(a) The right now forms part of the patrimony of the cessionary and not that of the cedent.
(b) The cessionary alone has the right to collect the debt.

(c) Once the cedent has ceded his or her claim to one person, it can no longer be ceded to another person. The cessionary can cede the right further.
(d) After a cession, the debtor can no longer perform validly to the cedent. However, if the debtor pays the original creditor (the cedent) in good faith, the debtor is released from his or her liability. Although it is not generally a requirement for the validity of a cession that the debtor be informed of the cession, the cessionary always runs the risk that the debtor might be discharged from his or her liability should the debtor pay the original creditor (that is, the cedent) in good faith. The cessionary would, therefore, be well advised to give the debtor notice of the cession. A debtor who is aware of the cession will not, as a rule, be in good faith if he or she performs to the cedent, but if the debtor can prove that, in spite of his or her knowledge, the act was in good faith, he or she will be released.
(e) The claim is transmitted to the cessionary in its entirety together with all benefits and privileges such as security or interest. For example, if the cedent holds something belonging to the debtor as pledge to ensure that he or she does not suffer damage if the debtor fails to perform, the cessionary's claim will be protected by that same security. The cessionary receives the benefits and privileges attached to the ceded principal debt only and cannot, for example, hold a surety liable for undertakings made by the surety to the cedent in respect of other debts of the same debtor.
(f) The cessionary also receives the right with all the disadvantages attached to it. Since the cessionary obtains his or her right from the cedent, it follows that the right which the cessionary so acquires cannot be a better right than that held by the cedent. As a rule, therefore, any defence which the debtor could raise against the cedent at the time of the cession may also be raised against the cessionary. The debtor will therefore be in a position to claim, as a defence against the cessionary, that the contract creating the right is voidable owing to misrepresentation, duress or undue influence.

12.3 Discharge

The primary purpose in creating contractual obligations is that they should be fulfilled by due and proper performance, which will then also bring the legal relationship between the parties to an end. Performance of the obligation undertaken is called 'discharge' (fulfilment) and is the natural way in which a contractual relationship is terminated.

Discharge can be either a bilateral or a unilateral juristic act. Where the debtor's obligation is of such a nature that he or she needs the creditor's co-operation for fulfilment, for example where the creditor has to receive goods, discharge by the debtor involves a bilateral juristic act. Where the debtor does not require the creditor's co-operation for the fulfilment of his or her obligation, for example, where the debtor has to refrain from performing a certain act, discharge involves a unilateral juristic act. A bilateral contract is discharged in full only when both parties have complied with their respective obligations.

Except in cases where performance is identified with the person of the debtor, for example, where a well-known singer undertakes to perform at a concert, it is not important who discharges the debt, that is, whether it is the debtor in person, the debtor's representative or surety or anyone else, provided that the person who performs has the intention of discharging the debtor's obligation. The debtor is released even if the discharge occurs without the debtor's knowledge or against his or her will. If the creditor refuses to accept due and proper performance tendered by a third party, he or she commits breach of contract.

Performance must take place against the creditor or his or her representative, who must be authorised to receive performance. The parties can, of course, also agree that the debtor will perform to a third party.

It goes without saying that the debtor has to perform in compliance with the terms of the contract, that is, the debtor has to tender the agreed performance at the agreed place and within the agreed period of time. For this reason discharge is not accomplished by defective performance. The creditor may also reject an offer to perform piecemeal, such as an offer to pay in instalments.

If an obligation comprises the payment of a sum of money, it has to be made in cash, unless the parties have agreed otherwise, or unless a contrary commercial practice exists. Payment has to be in legal tender, that is, in notes and coins.

A cheque is not legal tender, and is only acceptable if it can be proved that the creditor explicitly or tacitly agreed to accept a cheque, or if it has become a matter of usage between the parties concerned to pay each other by cheque. The acceptance of a cheque as payment is naturally subject to the condition that the cheque be honoured.

Payment offered may be withheld if the creditor refuses to give a receipt. When a debtor who owes a creditor money in respect of several debts makes a payment, the debtor is entitled to stipulate which debt or debts he or she wishes to redeem, subject always to any relevant contractual terms. If the debtor fails to make an allocation, the following principles apply:

(a) Interest is paid before capital.
(b) Due debts are paid before debts which have not yet fallen due.
(c) Onerous debts, for example, debts secured by means of a mortgage bond, have preference over non-onerous debts.
(d) Old debts have preference over new debts.

If the above-mentioned rules are not conclusive, the payment is allocated proportionately to all the debts.

12.4 Rescission and cancellation

The term ‘rescission’ is used to refer to the act of withdrawing from a contract due to reasons other than breach of contract, while the term ‘cancellation’ is used to refer to withdrawal from a contract due to breach of contract.

In the case of voidable contracts, the innocent party has the choice of enforcing the contract or of rescinding it. If the innocent party decides to rescind the contract, the contract is thereby terminated.

Cancellation is one of the remedies for breach of contract. When the innocent party, who has acquired a right of cancellation following the other party's breach of contract, exercises this right, the contract is terminated.

12.5 Agreement

At some stage after the conclusion of their original contract, the parties can agree to end the contractual relationship between them. The parties could also agree in advance, when they enter into the contract, that one or both of them may later unilaterally terminate the contract, usually with reasonable notice to the other party. Such a term, which could be express or tacit, is often included in contracts involving continuous obligations and with an unspecified duration. The exercise of such a contractual right of termination has the same consequences as cancellation following breach of contract.

Sometimes the contract between the parties contains requirements for its termination, for example, that it has to be done in writing. In such a case these requirements must be complied with.

The agreements that the parties to a contract could subsequently enter into for the purpose of terminating contractual obligations are release, novation and settlement.

12.5.1 Release

Release or 'waiver', as it is also often called, is an agreement between the creditor and the debtor in terms of which the creditor releases the debtor from his or her contractual obligations. Release is often accompanied by an intention to donate on the part of the creditor, but it can also be in exchange for something else, for example, that the debtor in turn releases the creditor from an obligation. Since release is an agreement, there obviously has to be an offer and an acceptance. A mere offer of release does not constitute release, since consensus is still lacking.

Like other contracts, release may be concluded expressly or tacitly. The creditor may tacitly offer to release the debtor by acting in a way that would lead a reasonable person in the position of the debtor to conclude that the creditor intends to make an offer of release. When the debtor accepts the tacit offer, his or her obligations are terminated.

12.5.2 Novation

Novation is an agreement between the creditor and debtor in terms of which the old obligation between them is extinguished and a new obligation created in its place. For example, Thapelo and Etienne agree that Thapelo will deliver a horse to Etienne. Subsequently, Thapelo and Etienne agree that Thapelo will no longer deliver the horse, but that, instead, he will pay Etienne the sum of R100. This new

agreement between Thapelo and Etienne terminates the original agreement (for the delivery of the horse). Thus the previous obligation is terminated by mutual agreement and replaced by a new obligation.

Novation only occurs where the parties have the intention of replacing the old obligation with a new one. The existence of a valid initial obligation is a prerequisite for the existence of a valid novation. If, however, the novation is void for some reason or other, the old obligation naturally remains in force, unless, of course, the parties have agreed to abandon it.

Novation can also be made subject to a condition. Let us assume that Ntsietso owes Zena the sum of R200 which can be claimed immediately. If the parties reach an

agreement in terms of which Ntsietso is to pay off the debt in instalments of R40 per month, then, unless there appears to be a contrary intention, it is accepted that a tacit condition of the novation is that the instalments will be paid punctually as they become due. Accordingly, should Ntsietso fail to pay her instalments, Zena can rely on the original debt and claim the entire outstanding balance.

The effect of novation is to extinguish the original debt and therefore to extinguish accessory obligations such as suretyship, to extinguish security, to bring the running of interest to an end, and to purge default. If the novation is void for whatever reason, the old agreement remains valid.

A judgment of a court may also, in certain circumstances, result in the novation of an obligation. However, this must be distinguished from novation by agreement.

12.5.2.1 Delegation

Delegation is a specific form of novation, namely where a new party is introduced. Delegation may involve either a change of creditors or a change of debtors. It means that the old obligation is extinguished, and a new obligation is created in its place. For example, Frasier has undertaken to build a swimming pool for Greg. However, Frasier has too much work and persuades Rebecca to take over the job. Frasier, Greg and Rebecca now agree on this arrangement. The effect of this agreement (delegation) is that a change of debtors has occurred. Frasier's obligation is extinguished and replaced by a new one, namely, Rebecca's obligation.

Delegation, therefore, differs from cession, which is the mere transfer of a personal right. Unlike cession, where the co-operation of the debtor is not required, the co-operation of all three parties is required for delegation.

12.5.3 Settlement *(transactio)*

Settlement, also called 'compromise', is an agreement by which parties settle a dispute between them about an actual or supposed obligation. The validity of a settlement does not require that there must be a valid debt. If a valid debt does, in fact, exist, it is extinguished by the settlement.

Suppose that Carla owes R1 000 to Nell, but asserts that she owes only R600, while Nell is of the view that the debt amounts to R1 200. If the parties reach agreement in terms of which the dispute is settled on the basis that Carla undertakes

to pay R800 to Nell, Carla's old obligation to pay Nell R1 000 is extinguished by the settlement and replaced by her new obligation to pay Nell R800.

The essential difference between settlement and novation is that, in the case of novation, the parties are in agreement on the existence of a valid old debt, whereas in the case of settlement, there is a dispute over whether the debt exists.

An offer of payment 'in full and final settlement' will be regarded as an offer of settlement if it is apparent that the offeror disputes the existence or extent of the indebtedness. By accepting the payment, the creditor will have accepted the offer of settlement and the obligation, if it indeed existed, will have been extinguished through settlement. However, where someone offers money in full and final settlement but it appears that he or she admits liability for (at least) that amount, it is not an offer of compromise and the creditor is entitled to accept the payment and still recover any balance of the indebtedness. The offeror's intention to offer a compromise, rather than to effect payment, is decisive.

If the debtor does not perform according to the terms of the settlement, the creditor may fall back on the original debt (if in fact it does exist) only where it was a term of the settlement that the creditor would have this right.

12.6 Merger *(confusio)*

Merger takes place when a person becomes both creditor and debtor in respect of the same obligation. Since one cannot owe something to oneself, the debt is extinguished by operation of law.

For example, merger would take place where the lessee buys the leased property or where the debtor and creditor conclude a marriage in community of property. Merger automatically terminates the obligation.

12.7 Set-off

Set-off is the extinguishing of debts owed reciprocally by two parties. There are four requirements for set-off:

(a) The debts must be similar in nature, for example, two monetary debts or two debts for the delivery of identical kinds of subject matter. The two debts need not be equal in size, since a debt can also be extinguished partially by set-off. However, two debts for the delivery of different kinds of subject matter, for example, for the delivery of money on the one hand, and for the delivery of goods on the other, cannot be set off against each other.

(b) The debts must be liquidated. A debt is liquidated when its exact monetary value is certain or can easily be ascertained. In so far as set-off is concerned, the requirement that the two debts intended to be set off against each other must be liquidated debts is based quite simply on the principle that what is certain cannot be set off against that which is uncertain. For example, Tshepo owes Dulah the amount of R200 in terms of a cheque (see paragraph 25.2.1 for a definition of a cheque) which is already due. Dulah, on the other hand, has occasioned Tshepo loss by defaming him. However, the amount of such

damages, until determined either by the parties themselves or by a court of law, is uncertain and cannot be set off against Tshepo's debt to Dulah.

(c) The debts must be claimable. A debt which is already claimable cannot be extinguished by one which is not yet claimable. By the same token, an unconditional debt cannot be set off against a conditional debt.

(d) The debts must be between the same persons. The debts must, in fact, be reciprocal, that is, they must exist between the same parties in the same capacities.

If Rhea has a claim against Linda in Linda's capacity as executor of Kirsty's estate, no set-off can take place against a debt that Rhea owes to Linda in her personal capacity.

Set-off automatically terminates the obligations by operation of law.

12.8 Impossibility of performance supervening after conclusion of the contract

Supervening impossibility of performance occurs when, after conclusion of the contract, performance becomes objectively impossible. The impossibility must not be due to the fault of one of the parties, but must be the result of an external factor beyond the control of the parties, such as exceptional forces of nature, war, or death.

Since the legal consequences differ from case to case, it is very important to distinguish supervening impossibility of performance from initial impossibility of performance and from prevention of performance.

Possibility of performance is one of the requirements for a valid contract. If performance is impossible at the conclusion of the contract, no contract is established. Prevention of performance occurs when performance is made impossible through the fault of one of the parties. It is a form of breach of contract.

Supervening impossibility of performance occurs when, at the time of the conclusion of the contract, performance is possible, but factors beyond the control of the contracting parties intervene and result in objective impossibility of performance. Thus a contract does come into being. When supervening impossibility of performances arises, the contract is terminated.

Thus, when performance is impossible, it is important to establish the stage at which performance became impossible, and also if it was due to the fault of one of the parties.

12.8.1 The consequences of supervening impossibility of performance

As a general rule, supervening impossibility of performance extinguishes the obligations of the contract. Supervening impossibility of performance, that is, impossibility of performance which is the consequence of, for example, superior forces or unforeseen circumstances and which is not the result of fault on the side of a party to the contract, relieves both the debtor and the creditor of their respective obligations.

The above-mentioned general rule is not applicable to contracts where one of the parties has agreed to assume responsibility for supervening impossibility. An example of this is those contracts of sale where the risk of damage or destruction already rests on the buyer. The specific risk arrangement for contracts of sale is explained in paragraph 13.4.

As has already been shown, the obligation is not terminated where performance becomes impossible after the debtor has fallen in *mora*, since one of the consequences of *mora* is that it perpetuates the obligations flowing from the contract.

Where the debtor has accepted the risk of supervening impossibility, the obligation is also not terminated.

12.8.2 Objective and subjective impossibility of performance

Another important aspect of supervening impossibility of performance to be borne in mind is that subjective impossibility of performance, that is, the specific debtor's inability to perform, does not relieve him or her of liability. Only objective impossibility has this consequence. A change in commercial circumstances which makes it difficult, expensive or unaffordable for the debtor to comply with his or her contractual obligations does not mean that performance is objectively impossible. Examples of objective impossibility of performance are the following: the specific horse that David has to deliver to Bashaar is killed by lightning; the rented premises are expropriated by the state.

Objective impossibility of performance that is not the fault of the debtor not only terminates the obligation in question but, where the obligations are reciprocal (that is, the one is undertaken in exchange for the other), it also extinguishes the counter-obligation. For example, David and Bashaar agree to exchange horses, but prior to delivery David's horse is killed by lightning. Not only is David relieved of his obligation to deliver his horse, but Bashaar's obligation to deliver his horse is also extinguished.

12.8.3 Temporary and partial impossibility of performance

Cases where performance becomes partially impossible will also have to be determined in accordance with the principles set out above. Where a divisible performance becomes partially impossible, the whole obligation is not terminated — the debtor is released only proportionately, and the counter-performance is naturally also reduced proportionately. If an indivisible performance becomes partially impossible it will have the same consequences as total impossibility of performance, unless the creditor is prepared to accept partial performance. In such a case, the counter-performance is reduced in proportion to the reduced value of the accepted performance.

The same principles ought to apply where performance (in the case of a continuing obligation) becomes temporarily impossible, because this too is a case of partial impossibility. If, for example, an employee contracts out his or her services for a year and then, as a result of illness, is unable to work for two months of that year,

the employee's performance is temporarily (partially) impossible. Thus, the whole obligation is not terminated by the illness of an employee. However, if the illness is of such a long duration that the employer cannot reasonably be expected to remain in uncertainty any longer, the contract may be terminated.

12.9 Prescription

12.9.1 The nature of prescription

One may both acquire rights (acquisitive prescription) and be released from obligations (extinctive prescription) through the passage of time. Extinctive prescription is one of the ways in which contractual obligations may be terminated.

The underlying idea of prescription is to bring about legal certainty. It would not be beneficial to the operation of the law if a state of affairs that has continued for a long period of time were later to prove legally unjustified. The legal position has to be adapted to correspond with the factual situation. For example, it could be very difficult for a debtor to prove a possible defence after the lapse of quite a number of years, since some of the evidence may already have been destroyed.

The basic rule is that prescription starts running as soon as the claim becomes enforceable. Consequently, if on 1 January Jabu borrows R1 000 from Judy, repayable on 1 June, prescription regarding Judy's claim begins to run from 1 June.

Where the debtor wilfully prevents the creditor from gaining knowledge of the existence of the debt, prescription will not begin to run until the creditor becomes aware of the existence of the debt. This rule does not apply to debts arising from agreement.

A debt is not deemed to be claimable until the creditor has knowledge of the identity of the debtor as well as of the facts resulting in the debt. A creditor is deemed to have such knowledge if he or she could have acquired it by exercising reasonable care, or put differently, if the lack of knowledge can be attributed to the creditor's own negligence, he or she is deemed to know of the debt.

Sometimes circumstances arise which make it impossible for a creditor to enforce his or her rights. It would obviously be most unfair if such a creditor were to lose these rights through prescription merely because, through no fault of the creditor, he or she is unable to enforce them.

The Prescription Act 68 of 1969 accordingly provides that completion of prescription may be delayed in certain circumstances, for example, when —

(a) the debtor is outside the Republic
(b) the debtor and creditor are married to each other
(c) the creditor is a minor or is insane or is a person under curatorship or is prevented by superior force from interrupting the running of prescription
(d) the creditor and debtor are partners and the debt arose out of the partnership relationship
(e) the creditor is a juristic person and the debtor is a member of the governing body of such juristic person.

In terms of the Prescription Act a circumstance which delays completion of prescription will have the effect of suspending the running of prescription provided that the circumstance has ceased to exist less than a year before the date for completion of prescription, in which case, completion will be delayed until a year has passed since the cessation of the circumstance. Assume, for example, that prescription begins to run on 1 January 2011 and that the period of prescription is three years. Prescription will then be completed by 1 January 2014. But let us assume further that after prescription has run for one year, delaying circumstances arise which last for six months (that is, until 1 July 2012). Prescription will still be completed on 1 January 2014 (because the delaying circumstances have ceased more than a year before the completion of the prescription). If, on the other hand, the delaying circumstances continue for eighteen months (that is, until 1 July 2013), prescription will be complete on 1 July 2014 (that is, one year after the delaying circumstances have fallen away). If the delaying circumstances continue until 1 January 2015, prescription will be complete on 1 January 2016 (once again one year after the delaying circumstances have ceased).

The Prescription Act also provides for the interruption of prescription by acknowledgement of liability and by service of process. Such interruption of prescription shall lapse, and the running of prescription shall be deemed not to have been interrupted if the creditor does not successfully prosecute his or her claim under the process in question to final judgment, or if the creditor does prosecute his or her claim but abandons the judgment or the judgment is set aside. The Supreme Court of Appeal recently confirmed that an interruption or delay in the running of prescription in favour of a principal debtor interrupts or delays the running of prescription in favour of a surety (see paragraph 23.2 where suretyship is discussed).

12.9.2 Prescription periods

The periods of prescription of debts are as follows:

(a) thirty years in respect of —
  (i) a debt secured by mortgage bond
  (ii) a judgment debt (a claim against a surety who bound him- or herself as surety in respect of a debt which was confirmed by a judgment against the principal debtor)
  (iii) a debt in respect of any taxation imposed or levied by or under any law
  (iv) a debt owed to the state in respect of any share of the profits, royalties or any similar consideration payable in respect of the right to mine minerals or other substances

(b) fifteen years in respect of any debt owed to the state and arising from an advance or loan of money, or a sale or lease of land by the state to the debtor, unless a longer period applies in respect of the debt in question in terms of paragraph (a) above

(c) six years in respect of the debt arising from a bill of exchange or other negotiable instrument or from a notarial contract, unless a longer period applies in respect of the debt in question in terms of paragraph (a) or (b) above

(d) save where an Act of Parliament provides otherwise, three years in respect of any other debt.

12.10 Sequestration and subsequent rehabilitation

When a debtor is unable to pay his or her debts, one or more of his or her creditors may apply to a High Court for the sequestration of the debtor's estate. After sequestration, the debtor's property is transferred to a trustee, who sells the property and divides the proceeds among the creditors. A sequestration order does not, as a general rule,

terminate contracts concluded by the insolvent prior to insolvency. However, some contracts are terminated: for example, a contract of mandate comes to an end when the estate of the mandator is sequestrated. If a contract has not been terminated by sequestration, any remaining obligations of the insolvent will be extinguished when the sequestration is later terminated by rehabilitation, unless the obligation arose from fraud on the part of the insolvent. The law of insolvency is discussed in chapter 28.

Further reading

RH Christie & GB Bradfield *The Law of Contract in South Africa* 6 ed (2011)

AJ Kerr *The Principles of the law of Contract* 6 ed (2002)

S van der Merwe, LF van Huyssteen, MFB Reinecke & GF Lubbe *Contract: General Principles* 4 ed (2012)

Chapter 14
The Contract of Lease

14.1 Introduction
14.2 The essential elements of a contract of lease
14.3 The formation of a contract of lease
14.4 The rights and duties of the lessor and the lessee
14.5 The termination of a lease
14.6 Renewal of a lease
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14.1 Introduction

South African law recognises three forms of the contract of lease. There is the letting and hiring of a movable or immovable thing, the letting and hiring of services, and the letting and hiring of work to be done (for example, a house to be built). This chapter concerns mainly the letting and hiring of immovable property, including a building or part of it. It is concerned with what is also described as a contract of landlord and tenant.

A contract for the letting and hiring (or lease) of a thing is a reciprocal contract in terms of which one party (the lessor, or landlord) undertakes to make temporarily available to another party (the lessee, or tenant) the use and enjoyment of a thing, wholly or in part, in return for the payment of a sum of money, or a share in the fruits of the property.

14.2 The essential elements of a contract of lease

Three essential elements are apparent from this definition. They are:

(a) an undertaking by the lessor to give the lessee the use and enjoyment of something (the object of the lease)
(b) an agreement between the lessor and the lessee that the lessee's right to use and enjoyment is to be temporary
(c) an undertaking to pay rent — in other words an undertaking by the lessee to pay a sum of money — or a share in the fruits of the property, in return for the use and enjoyment which he or she will receive.

14.2.1 The use and enjoyment of a thing (property)

In principle, any corporeal thing, movable or immovable, can be let. It is not required that the contract should confer the full use and enjoyment of the object of the lease. A partial letting and hiring is permissible. Therefore the full use and enjoyment of part of something may be granted, and the limited use and enjoyment of (the whole or part of) the object of the lease may be given. For example, a room in a house may be let, or, as happened in one of the court cases, the surface of one wall may be let for advertising purposes. The parties must agree on the particular property that is to be the subject matter of the lease. The object, or part of it, that is let must be identified or identifiable.

A contract of letting and hiring must confer on the lessee the power to use and enjoy the object that is to be let. If the object of the lease may be diminished, consumed or alienated, the contract does not qualify as one of lease. However, the cutting of trees or

crops which were cultivated to be cut, or which sprout again when cut, is regarded as use of the leased object (the land) and not as a diminution or consumption of it.

14.2.2 Temporary use and enjoyment

A contract in which one person grants the permanent use and enjoyment of an object to another is not invalid, but it is not a contract of letting and hiring. Nonetheless, it is not a requirement for the validity of a lease that it be entered into for a definite time. A contract of lease may stipulate that it will run until the occurrence of an event that is bound to occur, although the time for its occurrence is unknown. The duration of the contract of lease may be indefinite and it may also be expressed to be at the will of either the lessor or the lessee. A typical example is where a lease runs from month to month and can be terminated by either party on due notice.

14.2.3 The rent

The lessee must undertake to pay rent. The rent must be a specified sum of money. There is one exception to this rule, namely, that the rent in a lease of agricultural land may consist of a definite quantity or an agreed proportion of the produce of the property that has been let (for example, where farmer Tony leases his apple orchards to lessee Bill in return for certain portion of the apples produced each season). In other circumstances, if the counter-performance is something other than money, the contract is not one of letting and hiring.

The amount of rent that is payable must be certain. It is considered to be certain if it can be rendered certain, in other words, if it is ascertainable. Parties to a lease normally agree on a specific amount of money or on a specific quantity of produce which is to be paid as rent, but they can also create a valid lease by agreeing to a method or formula by which the rent is to be determined. They may also agree that a specified third person will determine the rent. If a third party fixes the rent at a patently too high or too low amount, it does not have to be accepted. The party

who objects may petition the court to fix a fair price. If the court fixes a rent, the objecting party may still reject it, in which case the contract of lease falls away.

The parties to a contract of lease may also agree that the rent is to be fixed by one of them or by his or her nominee, provided that the determination of the rent is not dependent entirely on the unfettered will of that person. Our courts also accept that contracts of lease may validly be concluded for a market-related rent or for a reasonable rent — 'reasonable' being a question of fact dependent on the particular circumstances of each case.

14.3 The formation of a contract of lease

The ordinary rules of contract apply. Therefore, generally no formalities are required for a valid contract of lease to come into being. A lease, including a lease of land, may therefore be entered into informally. There are some statutory exceptions. A long lease of agricultural land is prohibited by the Subdivision of Agricultural Land Act 70 of 1970 unless the Minister of Agriculture and Land Affairs consents to it in writing. The Subdivision of Agricultural Land Act was repealed by the Subdivision of Agricultural Land Act Repeal Act 64 of 1998. However, the Repeal Act has not come into operation and the Subdivision of Agricultural Land Act 70 of 1970 is therefore still in force.

The Formalities in Respect of Leases of Land Act 18 of 1969 also provides that a long lease must be registered against the title deed(s) of the land let to be valid for more than ten years against creditors and onerous successors (that is, persons who have given value) of the lessor, unless the creditor or successor knew of the lease when he or she became creditor or successor. A long lease can be described as a lease which has been entered into for a period of not less than ten years, or for the natural life of the lessee or any other person mentioned in the lease, or a lease which is indefinitely renewable from time to time at the will of the lessee, or which is renewable for periods which, together with the first period of the lease, amount in all to not less than ten years.

The Rental Housing Act 50 of 1999 provides that a landlord must reduce a lease to writing, if requested to do so by a tenant. This Act is discussed further under paragraph 14.7 below.

14.4 The rights and duties of the lessor and the lessee

Contracts of lease are often embodied in standard-form contracts. The lessor and lessee may not exclude any of the essential elements of a contract of letting and hiring. They must, for example, specify an object which is to be the object of the lease as well as the rent which will be payable. But they may exclude some consequences of the contract of lease which would otherwise have resulted in terms of the common law. The legal position as it exists at common law and as it has been decided upon and described in a particular contract may therefore differ.

If the lessor or the lessee does not fulfill any of his or her obligations, the other party may rely on the normal remedies for breach of contract. If the breach is of a material term of the contract, he or she may elect to abide by the contract, sue for specific performance, and claim such damages as have been suffered; or to regard the contract as cancelled and sue for damages. If the breach is of a non-material term of the contract, he or she may claim damages.

14.4.1 The duties of the lessor

14.4.1.1 The duty to deliver the leased object to the lessee

The lessor must put the use and occupation of the object that has been leased at the disposal of the lessee in such a manner that the latter is able to enter into undisturbed

occupation of it. In the case of a lease of fixed property (for example, a house) the lessor must, for instance, ensure that the property is not occupied by someone other than the lessee. If a lessee (tenant) wants to have a long lease registered, the lessor's duty includes the duty to co-operate in its registration.

The lessor must deliver the object of the lease in a condition that will enable the lessee to use and enjoy it. That condition will usually be determined by agreement between the lessor and the lessee. If there is no such agreement, the object must be delivered in the condition in which it was at the time of contracting. When something is let for a specific purpose, the lessor is deemed to have given a tacit undertaking that it will be reasonably fit for that purpose. Accessories which are essential to the proper use of the property (for example, the keys to a house or a car) must be delivered with it.

Until such time as he or she obtains actual possession of the object of the lease, the lessee only has a personal right against the lessor to claim possession. It is only after he or she has been given possession that the lessee's possession can be protected.

14.4.1.2 The duty to maintain the object of the lease in a proper condition

The property must not only be delivered in a condition which is reasonably fit for the purpose for which it is being leased, it must also be maintained in that state. The contract of lease normally gives rise to obligations of a continuing nature. The lessor must, therefore, allowing for normal wear and tear and excluding repairs caused by the fault of the lessee, continue to maintain the object of the lease in the condition in which he or she was obliged to deliver it. Failure to do this constitutes a breach of the lessor's contractual duties, which exposes him or her to the sanctions afforded by law to the innocent party in the event of a breach of contract.

If the object of the lease is so defective that when it is tendered to the lessee he or she cannot reasonably be expected to accept it, the lessee may elect to cancel the contract without having to give the lessor an opportunity to remedy the defect.

If the object falls into such a serious state of disrepair during the term of the lease that it cannot be reasonably expected of the lessee to continue with the lease, he or she may also elect to cancel the contract, but in this event the lessor must first be given a reasonable time to repair the defect. The lessee remains liable for the rent either until he or she vacates the property leased or until the object is put at the disposal of the lessor again. Should the lessee elect to retain, or remain in possession of, the object of the lease, he or she may not refuse to pay the rent, but may claim a reduction in the rent proportional to its diminished use and enjoyment. If the inconvenience suffered by the lessee is slight, he or she is not entitled to a reduction of the rent.

The lessor will be liable for damages alleged to have been suffered by the lessee only if he or she was aware of the defects or if, as a person with expert knowledge of the kind of property in question, he or she ought to have been aware of them. The courts have a tendency not to order specific performance of the lessor's obligation to maintain the leased premises. So our courts have seldom been prepared to grant an order for specific performance, which, in this context, would amount to an order to effect the necessary repairs. However, the court recently criticised this tendency and made it clear that a lessee is, in principle, entitled to specific performance and that the right to claim specific performance in this context should not be limited simply because the courts struggle to enforce such an order. The court also held that there is no authority for casting the tendency not to order specific performance in this context as an absolute rule. An order for specific performance to effect the necessary change can therefore be granted to the lessee. But the lessee can normally obtain the same result by effecting the necessary repairs him- or herself after unsuccessfully demanding them from the lessor, and subsequently recovering the cost from the lessor, or by deducting it from the rental. Where the lessee (tenant) claims a reduction of the rent because of repairs he or she has had done to the object of the lease, the actual expenditure on the repairs must be proved. The lessee will also have to prove that he or she had the repairs effected after the lessor neglected to respond to a demand to have them done. It is not sufficient for the lessee merely to give an estimate of the cost of remedying the defects. The lessee is responsible for damage that has been negligently or deliberately caused to the object of the lease by himself or herself or by those for whose acts he or she is liable.

Should the lessor have warranted the presence or absence of certain features in the object of the lease, delivery of something which is not in accordance with the warranty constitutes a breach of contract.

The parties to a contract of lease may agree that this common-law duty of the lessor should fall on the lessee or tenant and, in fact, often does. Such an agreement must be clear and unambiguous before our courts will accept that the lessee has undertaken this obligation. If the lessee has undertaken to keep the object of the lease in repair, it does not absolve the lessor of the duty to deliver it in a proper state of repair.

14.4.1.3 The duty to ensure the lessee's undisturbed use and enjoyment

The terms of the lease may warrant that the lessor is the owner of the property let. If they do not, no such warranty exists. In principle, a lease may be valid even though the lessor is not the owner of the property let and had no right to let it. All the lessor warrants is that no one has the right in law to interfere with the lessee's use and enjoyment of the property.

The lessee may not dispute the lessor's title or right to let the property. The actual owner of the property is naturally not bound by the lease, unless he or she has consented to it (for example, by allowing the lessee to remain in occupation of the property and accepting rent from him or her).

Since a lessor undertakes to give the lessee the use and enjoyment of the object of the lease for a certain time, he or she must ensure that the lessee's use and enjoyment is not disturbed by someone with a legal right to the property during that time. The disturbance of a lessee may be caused by the lessor himself or herself, or by third parties, or by operation of natural forces over which the parties have no control. The lessor's liability depends on the person or event that disturbed the lessee in the particular circumstances. The lessor does not, however, warrant that the tenant will not be disturbed by a third person who has no legal right to the property: for example, where a third party with no legal right to the property creates a nuisance.

A lessor who unlawfully disturbs the lessee in the use or enjoyment of the object of the lease is guilty of a breach of contract. The lessee is entitled to the usual remedies for breach of contract, and is therefore entitled to enforce the contract, or, if the breach is serious enough, to cancel it. In both instances damages may be claimed if the lessee has suffered loss. But it must be remembered that interference by the lessor with the lessee's right to use and enjoyment of the object is not always unlawful. For example, a lessor may enter upon premises to do reasonably necessary repairs or to inspect them. If those repairs cannot be effected while the lessee is in occupation, and they are urgently required, the lessor may compel the lessee to vacate the premises temporarily. Refusal to do so by the lessee may be a ground for the cancellation of the contract of lease (by the lessor). A lessee who is, lawfully or unlawfully, deprived of the whole or part of the use and enjoyment of the thing let, is normally entitled to a *pro rata* remission of the rent for the time of deprivation. But if the deprivation is for the lawful purpose of enabling the lessor to effect necessary repairs, remission of rent is not granted if the lessee was aware at the time of contracting that the repairs were required, or if the deprivation is for a short period only.

As was stated above, the lessor must also protect the lessee from being evicted from the use and enjoyment of the whole or part of the property by a third party who claims to have a superior title. This duty is similar to a seller's duty to warrant against eviction, which is discussed in chapter 13. The situation is the same, whether eviction takes place as a result of a defect which existed in the lessor's title at the time when the lease was entered into or as a result of a defect which the

lessor allowed to develop during the currency of the lease. The lessor is in breach of contract if the lessee is evicted, but not if there is only a threatened eviction. The lessee must, however, inform the lessor of a threatened eviction to enable the lessor to defend the lessee or to assist him or her (the lessee) in the defence. Should the lessor fail to assist the lessee, the lessee must put up a strong defence, if there is one. A lessee who has failed to inform the lessor of a threatened eviction, or to put up a strong defence, may still bring an action against the lessor if he or she can prove that the third party's claim was indefeasible because of the lessor's defective title. An evicted lessee is entitled to a reduction of rent pro rata to the diminished use and enjoyment of the object of the lease. A lessee has no claim for damages if he or she entered into the lease in circumstances which indicate that the risk of eviction was assumed.

If the lessee is disturbed in the use and enjoyment of the property let by a superior force over which the parties have no control, the lessor is not guilty of breach of contract. The lessee is, nonetheless, entitled to a proportional remission of the rent, unless he or she assumed the risk of the lessor's performance becoming impossible.

14.4.2 The duties of the lessee

14.4.2.1 The lessee's duty to pay the rent

The payment of rent is an essential element of a contract of lease. It may therefore not be excluded, not even by agreement between the parties. Certain common-law rules relating to the payment of rent may, however, be altered by agreement between the parties. For example, the time of payment is usually determined contractually. In the absence of any specific provision, the general rule is that the rent will be payable at the end of the term of the lease. Rent is payable in money, unless the parties have agreed that it will consist of a share in the fruits or proceeds of the leased property. It may not consist of anything else. An argument put forward in one of the decided cases that the installation of a micro-jetting system to irrigate an orchard constituted the rent was therefore dismissed. Unless the parties have agreed otherwise, a lessor is entitled to insist on being paid in South African currency.

The lessee will not be in default if the lessor causes his or her inability to pay the rent on time.

A lessee can commit a breach of the duty to pay rent in two ways. The lessee can default in payments, or can repudiate liability for rent. If the lessee commits a breach, the remedies for repudiation or *mora debitoris* are available to the lessor. The lessor may elect to uphold the contract and claim the rent. In certain instances he or she may cancel the contract on the ground of the lessee's refusal or failure to pay the rent. If a loss has been suffered, a claim for damages lies, irrespective of whether the lessor has elected to uphold or cancel the contract. A lessor who cancels the lease may claim the rent that has accrued up to the time of cancellation, but, according to case law, not any rent after that time.

14.4.2.2 The lessee's duty of proper use and care of the object of the lease

The lessee may not use the object of the lease improperly or unreasonably. The object of the lease must be maintained in a good condition and, if the parties have agreed on a purpose for which it is let, it may only be used for that purpose. If there is no such agreement a term is implied in the contract that the object should be used for the same purpose as the one for which it was used before the lease. There is no duty on the lessee to keep using the object of the lease, unless there is an express or tacit provision to this effect in the contract of lease. If the lessee breaches his or her duty to use the thing let in a proper manner, the usual contractual remedies will apply.

14.4.2.3 The lessee's duty to return the property undamaged on termination of the lease

Upon termination of the lease, the lessee must return the lease object, or evacuate the premises. This obligation flows from the essential characteristic of a contract of lease that the lessor binds him- or herself to make the temporary use and enjoyment of an object available to the lessee. The leased property must be returned in the condition in which it was received, except for deterioration as a result of reasonable wear and tear.

If a lessee returns the property in a worse condition than the contract requires, or fails to return it at all, he or she commits a breach of contract unless it can be proved that the condition in which the property is returned, or the failure to return it, is not due to his or her fault or to the conduct of persons for whose acts he or she is liable (for example, an employee of the lessee). If, for example, the property was destroyed or stolen, the lessee must show that the destruction or theft cannot be attributed to his or her fault.

Despite the lessee's duty to return the property undamaged upon the termination of a contract of lease, the lessor is still entitled to insure premises or leased property against potential damages caused by the lessee. For example, the lessor may insure premises against fire damage that may be caused by the lessee. Where damage was caused by the lessee and the insurer paid out the lessor for the damage, a lessee may be held liable by an insurer for damage to the leased property, unless there is a contract term to the opposite effect.

14.4.3 The rights of the lessor

14.4.3.1 Non-payment of rent

The lessor has the right to receive the rent agreed upon. There are certain remedies that a lessor may use to protect this right.

Contracts of lease of immovable property often contain a 'cancellation clause', in which the parties agree that the landlord will be entitled to cancel the lease and eject the tenant if the latter breaches specified conditions. The payment of rent is normally included under these conditions. The cancellation clause is similar to the

lex commissoria of the contract of sale. It may be waived by the landlord, either expressly or by implication. Whether the landlord has waived his or her rights under the cancellation clause is a question of fact to be decided on a consideration of all the circumstances of the case.

14.4.3.1.1 The lessor's tacit hypothec for unpaid rent

Whether or not the contract of lease contains a cancellation clause, the lessor or landlord acquires a hypothec over all movables situated on the property as soon as the lessee of immovable property falls into arrear with the rent. This is known as the landlord's tacit hypothec and serves as security in respect of such rent. The hypothec is operative only when and, for as long as, the rent is in arrears. The hypothec arises immediately when the lessee falls in arrear with the rent. However, it is of no force and effect, in other words, it has not yet been perfected, until the lessor makes an attachment (this is done by obtaining a court order directing the officials of court to attach the property) of the goods in respect of which the hypothec is operative, or obtains an interdict (a court order ordering someone to take, or to refrain from, a particular course of action) preventing the tenant who is in arrears with the rent from disposing of or removing the property. In terms of section 4(3)*(c)* of the Rental Housing Act 50 of 1999, a tenant has a right against the landlord not to have his possessions seized, except in terms of a law of general application and if the landlord has first obtained a ruling by a tribunal or an order of court. The Rental Housing Tribunal or a court can therefore give effect to a landlord's hypothec (on the tenant's goods on the leased premises). The Act is further discussed in paragraph 14.7 below.

If the goods are removed from the leased premises before the lessor has made the attachment, the lessor will lose his or her tacit hypothec unless the goods can be pursued and 'arrested' before they arrive at their new destination. The lessor may not, however, physically prevent removal by seizing the goods.

The lessor may only rely on the hypothec when and while the lessee is in arrears with rent. And even while it exists, a third party is not subject to the hypothec. Until the goods have been attached, a third party can have them attached, removed and sold in execution, whether or not the third party had knowledge of the hypothec.

The landlord's tacit hypothec extends to all movables brought on to the leased property. Property belonging to a sublessee is covered only to the extent that the sublessee owes rent to the lessee. Property belonging to a third party is covered by the landlord's tacit hypothec, provided such movables have been brought on to the leased property with their owner's consent for the purpose of remaining there permanently and for the use of the lessee. Such movables will be subject to the tacit hypothec where the third party, being in a position to give the landlord notice of his or her ownership, has failed to do so, and the landlord is unaware that the goods do not in fact belong to the lessee. It is therefore clearly in the interests of the third party to notify the lessor of his or her ownership. The goods of a third party are subject to the landlord's tacit hypothec only to the extent that the lessee's goods are insufficient to secure the arrear rent.

The Insolvency Act 24 of 1936 provides that the landlord's tacit hypothec gives an extraordinary preference over the proceeds of the goods of a lessee on the property let for rent due on the date of the sequestration of his or her estate. The extent of the preferent claim depends on when the rent is payable (for example, weekly, monthly, or at longer intervals). If a claim exceeds the specified amount, the lessor is only a concurrent creditor for the balance.

The ambit of the lessor's hypothec has, to some extent, been curtailed by the Security by Means of Movable Property Act 57 of 1993. If a special notarial bond has been registered over movable property before the hypothec has been perfected, the hypothec

does not apply to property which is in the possession of a person other than the mortgagee, or to which an instalment-sale transaction as defined in the National Credit Act 34 of 2005 relates. (A notarial bond is a bond over movable property. A special notarial bond is registered over specific movable property. Mortgage bonds are discussed in chapter 23, and the National Credit Act in chapter 16.)

The hypothec terminates on payment of the arrear rent by the lessee or any other party. The lessor must return the attached goods to their owner. Termination of the lease does not itself end the hypothec.

14.4.3.1.2 Automatic rent interdict and attachment order under the Magistrates' Courts Act

The Magistrates' Courts Act 32 of 1944 provides for an automatic rent interdict. In terms of the Act, an automatic rent interdict may be obtained when a summons claiming rent is issued. This entails including with the summons a notice that prohibits any person from removing any of the furniture or other effects on the leased property which are subject to the plaintiff's hypothec for rent until the court has made an order. The notice serves as an interdict to any person who knows about the notice not to remove any of the specified goods. The Act also provides that the landlord may apply for the issue of an attachment order. The application may be made on affidavit (a sworn declaration, or one made under oath). The landlord (lessor) must allege that the premises are situated within the jurisdiction of the court; that rent not exceeding the jurisdiction of the court is due and in arrear; that such rent has been demanded in writing for at least seven days and, if not, that the lessor believes that the tenant is about to remove the movable property upon the premises in order to avoid the payment of the rent.

14.4.3.2 Misuse of the object of the lease

If the lessee misuses the leased property, the lessor has the ordinary contractual remedies. If the misuse is material, he or she may cancel the contract and has a claim for damages for any loss suffered as a result of the breach. If the misuse is not material, the claim is restricted to an action for damages, if any have been suffered. Whether the misuse is material or not is a question of fact.

The lessor may also obtain an interdict to prevent the lessee from misusing the leased property, thereby ensuring specific performance of the duty to use it in a proper manner.

14.4.3.3 Failure to return the property

If the lessee fails to comply with the duty to return the object of the lease in a proper condition, the normal contractual remedies lie. The lessor may claim specific performance (in the form of an order to repair the property where it has been returned in a defective condition, or an order to return the property when it has not been returned at all), or damages if he or she has suffered loss. The duty to return the property becomes enforceable only on termination of the lease; therefore, cancellation of the lease is not a remedy for this type of breach.

A lessee who remains in occupation of the lessor's property after the lease has expired commits the delict of unlawful possession of another's property as well as a breach of contract. The claim for damages may therefore also be based on delict. (The law of delict is discussed in chapter 2.)

If the lessee remains in occupation of the property (or 'holds over') after termination of the lease, the lessor may have him or her evicted (subject to the statutory provisions referred to in paragraph 14.7). But the lessor may waive his or her rights and allow the lessee to remain in occupation. A new lease is then implied upon the terms and conditions of the old lease. It may be difficult to determine the term of the new lease in such an instance. It seems that it should be presumed that the new lease is for an indefinite period and can be terminated unilaterally only upon reasonable notice.

14.4.4 The rights of the lessee

The rights of the lessee are largely determined by the duties of the lessor and lessee. But there are other aspects of the lessee's rights which are not apparent from these duties. They are discussed below.

14.4.4.1 Failure to deliver

A breach by the lessor of his or her duty to deliver is material. The lessee may regard the contract as cancelled and sue for damages, or may claim specific performance and damages. The amount of damages is determined in accordance with the ordinary principles of the law of contract (see chapter 11). Since specific performance is a discretionary remedy, it should be kept in mind that there are circumstances under which the courts will not order it.

Where the thing, or object of the lease, has been delivered, but it is not in a proper state of repair, the question whether the breach is material is one of fact. If it is, the lessee may cancel the contract and claim damages. If not, the lessee may claim damages, which will amount to a proportionate deduction of the rent. Courts are reluctant to order specific performance in these instances because of the difficulty in enforcing such an order. But a lessee may, after prior notice to the lessor, have the repairs effected and deduct the repair costs from the rent. The

lessee may also waive his or her rights by conduct that indicates that he or she is prepared to accept the property in its defective condition.

14.4.4.2 Failure to maintain the property

Where the lessor fails to maintain the property in proper repair, the lessee has the same remedies as those discussed under paragraph 14.4.4.1. For example, if the need of repair is so substantial that it causes considerable inconvenience, or has made the property dangerous or uninhabitable, the lessee may cancel the lease and give up occupation. The

determination of the substantiality of the inconvenience depends on the degree of disrepair and for how long it exists.

14.4.4.3 Breach of warranty against interference

If the lessor, or a third party who has a right to the property, interferes with the lessee's use and enjoyment of the property, the lessee may rely on the ordinary rights on breach of contract. He or she may claim damages, or, if the interference is sufficiently material, cancellation of the contract and damages. In addition, the lessee may obtain an interdict to protect his or her rights.

Where a third party without any rights interferes with the lessee's possession, the lessee must take action against the third party and not against the lessor. If the tenant's use of the leased property is interfered with by *vis major* (an 'act of God') or *casus fortuitus* (an 'accidental occurrence') beyond the control of the lessor or lessee, the lessee has a common-law right to remission of rent. If the property is destroyed by such events, the position is governed by the rules of supervening impossibility of performance. These provide that the relationship between lessor and lessee is terminated.

14.4.4.4 Subletting

Unless the contract of letting and hiring prohibits it, a lessee is entitled to sublet (that is, to relet) any thing that has been let without the lessor's consent, provided that the proposed sublessee is not a person to whom the original lessor could reasonably object. The Appeal Court (as it then was) has, however, held that a rural tenement may not be sublet without the lessor's consent. Whether a property is rural or urban is determined by the use to which it is put and not by the place where it is situated.

If the lease prohibits subletting without the lessor's consent, the lessor has an unfettered discretion to refuse consent. But the contract of lease usually provides that the consent should not be unreasonably withheld. The lessee must show that the consent was unreasonably withheld.

The effect of subletting in contravention of an express agreement that the lessee will not be able to sublet without the lessor's consent is that the sublease is void. Subletting in breach of a prohibition against it constitutes so serious a breach of the lease that it entitles the lessor to justify cancellation even in the absence of a cancellation clause.

If the property is sublet, a contract arises between the original lessee and the sublessee. There is no contractual relationship between the original lessor and the sublessee. The sublessee must give up occupation of the thing when the original contract of lease comes to an end.

14.4.4.5 Cession

A lessee may cede his or her rights to a third person like any other creditor, unless the contract of lease prohibits or restricts this right. In the case of a rural tenement, the cession may only take place with the prior written consent of the lessor.

The effect of a cession is that the cessionary becomes the creditor of the original lessor and that the lessee ceases to be his or her creditor. The lessee remains the lessor's debtor, since only the rights, and not the duties, of the lessee are ceded.

As is the case with subletting, the matter is often governed by an express agreement between the parties that the lessee will not be able to cede his or her rights without the consent of the lessor. A cession in contravention of such an express agreement is void. If there is no express agreement, it seems accepted law that the lessee may sublet without the lessor's consent, except in respect of rural land.

14.4.4.6 Assignment

A creditor transfers his or her rights by cession. The duties of a debtor are transferred by delegation (cession and delegation are discussed in chapter 12).

If there is to be a complete substitution of one lessee for another, it must be effected by a combined cession and delegation, or by a delegation of rights and duties. In English law this is termed an assignment. This term has been taken over in our law. The effect of an assignment in the context of a contract of lease is that the assignee becomes the debtor and the creditor of the lessor, while the agreement between the lessor and the original lessee comes to an end. Since an assignment always involves a delegation, it cannot take place without the consent of the debtor.

14.4.4.7 The lessee's relationship with successors of the lessor; the maxim 'huur gaat voor koop'

The lease remains in force on the death of the lessor. The lessor's estate is simply substituted as lessor. However, where ownership is transferred from the lessor by operation of statutory provisions, for example, if leased land is expropriated, the new owner is not bound by the lease.

If a lessor of immovable property sells the property the general rule is that the purchaser is bound by the lease in accordance with the maxim '*huur gaat voor koop*'. This doctrine can be translated as 'hire takes precedence over sale'. It arose from considerations of equity and is relevant only to contracts pertaining to the lease of immovable property (for example, a house or a farm). It refers to the principle that the person to whom such property has been alienated is bound by any contract of lease existing in respect of the property at the time of its alienation. The purchaser (or other person in favour of whom such property has been alienated)

therefore cannot evict the lessee (tenant), but is obliged to abide by the terms of the lease, provided that the lessee continues to pay the rent due under the lease. The owner of immovable property is thus prevented from transferring rights to another (which have already been transferred to a lessee). The lessee therefore acquires a real right to the property. The lessee is bound by the lease and, if the new owner recognises his or her rights, does not have the choice of withdrawing from the contract.

No new lease comes into existence between the new landlord (the buyer) and the tenant. Nor is there a need for a cession of rights or an assignment of obligations. The

purchaser (or other person in favour of whom the property has been alienated) does not assume any obligation owing by the lessor to the lessee (for example, the duties to deliver the object of the lease in a specific condition; to furnish a warranty against eviction, and to compensate the lessee for fixtures and improvements to the property), if such obligation arose prior to the date of sale. The purchaser is also not entitled to any rent or any other benefit which accrued to the lessor in terms of the lease prior to the date of sale.

The maxim only applies where the property is alienated (for example, sold, exchanged or donated), and not, for instance, where the owner's rights are transferred as a consequence of expropriation. It therefore only applies if there has been a succession of rights. The doctrine also does not apply in the law relating to cession of rights or assignment of obligations. Moreover, the Supreme Court of Appeal found that an option in favour of a lessee to purchase leased property is not binding on a lessor's successor in title by virtue of the *huur gaat voor koop* rule.

The maxim '*huur gaat voor koop*' is subject to certain qualifications:

(a) The Formalities in Respect of Leases of Land Act 18 of 1969 provides that certain leases of immovable property (commonly referred to as 'long leases') shall not be binding on a creditor or successor under onerous title (that is, someone who has given value to the property) of the lessor for longer than ten years, unless such lease is registered against the title deed of the property, or unless the creditor or successor had knowledge of such a contract of lease.

(b) The position of lessees for less than ten years (generally referred to as 'short-term lessees') is not governed by legislation. These lessees are protected by the maxim only if they are in occupation of the property let, or if the successor or creditor of the lessor had notice of the existence of the lease at the time when he or she entered into the contract or acquired the real right in the property, or if the successor or creditor of the lessor acquired his or her real right in the property gratuitously. Knowledge will be ascribed to the purchaser where the lessee occupied the premises or property at the time of such passing of ownership. These principles also apply in respect of the first ten years of the term of a long lease which has not been registered against the title deed of the property.

The maxim '*huur gaat voor koop*' binds both the lessor and the lessee. The lessee therefore continues to be bound by the contract of lease, provided that his or her rights continue to be recognised by the new owner.

14.5 The termination of a lease

The obligations flowing from a contract of letting and hiring can be terminated in any of the ways by which obligations are usually terminated (see chapter 12). Performance is the most usual way of terminating a contract of lease.

There are also other ways of termination which are peculiar to this specific type of contract:

14.5.1 Termination by effluxion of time

If a lease is for a fixed period or until the occurrence of a specified event, the obligations arising from it automatically come to an end when the period ends or the event occurs.

14.5.2 Termination by notice

If the contract of letting and hiring is for an indefinite time, but with rent payable periodically (for example, monthly), the obligations flowing from it can be terminated by notice given by the lessor or the lessee. If there is no agreement on the period for such notice, reasonable notice must be given. What will be reasonable notice depends on the circumstances of each case. Some guidelines have emerged from case law. Generally, the notice must expire at the end of a period for which rent is payable and must, in the case of leased premises, give the lessor a reasonable time to relet the premises or the lessee a reasonable time to find other premises.

Where a lease is at the will of any of the parties to it, he or she may terminate it at any time by giving notice. A notice of termination is effective only if it comes to the actual knowledge of the other party. The notice may not be unilaterally withdrawn, but it does not have to be accepted by the other party.

14.5.3 Termination by extinction of the lessor's title

As was stated above, it is not a requirement for a contract of lease that the lessor should have a valid title to the object of the lease. Therefore, the extinction of the lessor's title does not normally terminate the obligations created by the lease. But it does so if the parties intended that it should, or if it must be taken that this was their intention. Also, if a lessor is unable to continue giving the lessee the undisturbed use and enjoyment of the thing because his or her title to it is extinguished, it may lead to the termination of the obligations arising from the lease by supervening impossibility of performance.

14.5.4 Termination by death

A lease is terminated by the death of the lessor or the lessee if the contract so provides, or if the lease was in the will of the deceased. In other instances the rights and duties of a deceased lessor or lessee pass to the heirs of that party on his or her death.

14.5.5 Termination by insolvency

The law of insolvency is discussed in chapter 28. The effect of the sequestration of a natural person on an uncompleted contract of lease is discussed there. Where a company or close corporation is concerned, the position is similar. If the company or corporation is the lessee, the Companies Act 61 of 1973 (which also regulates the position in respect of close corporations) provides that, subject to the consent of the Master, the liquidator may terminate a lease of movable or immovable property before a general meeting is convened to obtain the sanction of the members or creditors of the company for certain matters.

14.5.6 The lessee's right to compensation for improvements

It is not unusual for a lessee to make improvements to the leased property (for example, where Peter rents a house for three years he may want to paint the house, build a tool

shed, or add a roof to the outside entertainment area during that time). Improvements can be useful (if they improve the property and increase its market value); luxurious (if they satisfy the fancy of an individual, whether or not they increase the market value); or necessary (if they are required for the preservation of the property).

The parties to a contract of letting and hiring should agree on the rights of the lessee to remove improvements and on his or her claim to compensation if improvements are not removed. If they have not agreed otherwise, a lessee of rural land may remove annexures constituting luxurious or useful improvements before the lease terminates, provided the property will not be left in a worse condition than when it was received. After termination, everything annexed belongs to the lessor. It seems that this applies also to necessary improvements, although our law is not very clear on this aspect.

The position as described above applies only to rural tenements (land). The *Placaeten of the Estates of Holland* of 1658 and 1696 on which it is based do not apply to urban tenements. Therefore, a lessee in respect of urban land is entitled to remove useful and luxurious improvements before termination of the lease, provided they can be removed without leaving the property in a worse position than it was when received. The lessor can, however, elect to keep the improvements and pay the lessee the value they would have on separation. The lessee is not entitled to remove necessary improvements, but has a claim for all expenses. The lessee is entitled to compensation for useful improvements that are not removable, but usually not in respect of luxurious improvements.

14.6 Renewal of a lease

A contract of lease may be renewed, that is, a new contract of lease is concluded between the same lessor and lessee and commences immediately upon the termination of their existing lease. The agreement to enter into a new lease may be express or tacit.

14.7 Statutory protection of tenants

14.7.1 Introduction

Various statutory provisions, which are aimed at the protection of tenants and lessors, vary the common-law principles relating to contracts of lease. The Formalities in Respect of Leases of Land Act 18 of 1969 has already been referred to above. Constitutional protection of the right of access to housing as a basic human right led to further legislative measures which are discussed below.

Section 26 of the Constitution of the Republic of South Africa provides that —

(a) everyone has the right to have access to adequate housing
(b) the state must take reasonable legislative and other measures, within its available resources, to achieve the progressive realisation of this right, and
(c) no one may be evicted from their home, or have their home demolished, without an order of court made after considering all the relevant circumstances. No legislation may permit arbitrary evictions.

14.7.2 The Rental Housing Act 50 of 1999

The Rental Housing Act 50 of 1999 (as amended by the Rental Housing Amendment Act 43 of 2007) promotes section 26*(b)* of the Constitution. It defines the responsibility of the government in respect of rental housing property; creates mechanisms to promote the provision of rental housing property; promotes access to adequate housing through creating mechanisms to ensure the proper functioning of the rental housing market, and provides for the establishment of Rental Housing Tribunals so that general principles governing conflict resolution in the rental housing sector may be provided and sound relations between tenants and landlords promoted. The Act applies only to leases of residential property.

Sections 4 and 5 of the Act deal with the relations between landlord and tenant. A landlord may not, either in advertising a dwelling for purposes of leasing it, or in negotiating a lease with a prospective tenant, or during the term of a lease, unfairly discriminate against a prospective tenant or tenants, or the members of such tenant's household or the visitors of such tenant, on any of the grounds of discrimination prohibited in the Constitution. These grounds include race, gender, sex, pregnancy, marital status, sexual orientation, ethnic or social origin, colour, age, disability, religion, conscience, belief, culture, language and birth.

A lease between a tenant and a landlord need not be in writing or be subject to the provisions of the Formalities in Respect of Leases of Land Act 18 of 1969 (referred to under paragraph 14.3), but if a tenant requests it, a landlord must reduce the lease to writing.

A lease must include the following information:

(a) the names of the tenant and the landlord and their addresses in the Republic for purposes of formal communication
(b) a description of the dwelling which is the subject of the lease

(c) the amount of rental of the dwelling and reasonable escalation, if any, to be paid in terms of the lease
(d) if rentals are not paid on a monthly basis, then the frequency of rental payments
(e) the amount of the deposit, if any
(f) the lease period, or, if there is no lease period determined, the notice period requested for termination of the lease
(g) the obligations of the tenant and the landlord, which must not detract from the tenant's statutory rights or the regulations relating to unfair practice
(h)

the amount of the rental, and any other charges payable in addition to the rental in respect of the property.

A list of registered defects and a copy of any house rules must be attached as annexures to the lease. It is the landlord's duty to ensure that the lease contains the required information and that these annexures are attached.

The Act protects a tenant's right to privacy for the period that the lease runs. The landlord may only exercise his or her right of inspection in a reasonable manner after reasonable notice to the tenant. The tenant, members of the tenant's household and visitors of the tenant are entitled not to have their person, home or property searched, or possessions seized, except in terms of law of general application and after an order of court or a ruling by a Rental Housing Tribunal has been obtained, or to have the privacy of their communications infringed.

The landlord's rights against the tenant include his or her right —

(a) to prompt and regular payment of a rental or any charges that may be payable in terms of a lease
(b) to recover unpaid rental or any other amount that is due and payable after obtaining a ruling by the Tribunal or an order of a court of law
(c) to terminate the lease in respect of rental housing property on grounds that do not constitute an unfair practice and are specified in the lease
(d) on termination of a lease, to receive the rental housing property in a good state of repair, save for fair wear and tear; to repossess rental housing property having first obtained an order of court, and to claim compensation for damage to the rental housing property or to any improvements on the land on which the dwelling is situated, if any, caused by the tenant, a member of the tenant's household or a visitor of the tenant.

Leases are deemed to include certain terms dealing with payments, inspection of the property and vacation before termination of the lease. These terms are aimed at the protection of both the landlord and the tenant, are enforceable in a competent court and may not be waived by either the landlord or the tenant.

If on the expiration of the lease the tenant remains in the dwelling with the express or tacit consent of the landlord, the parties are deemed, in the absence of a further written lease, to have entered into a periodic lease, on the same terms and conditions as the expired lease, except that at least one month's written notice must be given of the intention by either party to terminate the lease.

Each province may establish a Housing Rental Tribunal consisting of between three and five fit and proper persons appointed after due process by the Member of the Executive Council for that province. The main function of the Tribunal is to investigate and resolve disputes relating to unfair practices, which are defined in the Act as any act or omission by a landlord or tenant in contravention of the Act or a practice prescribed as a practice unreasonably prejudicing the rights or interests of a tenant or a landlord. These Tribunals have 'exclusive jurisdiction' to determine any dispute in respect of an unfair practice, except if it is an urgent matter or where proceedings have already been instituted in any other court before the establishment of a Tribunal. Being in default by not paying rent promptly in terms of the Act would, therefore, also constitute an unfair practice that could be adjudicated by a Tribunal. Nevertheless, although a Tribunal has exclusive jurisdiction to determine any dispute in respect of an 'unfair practice', which would include a dispute in respect of arrear rentals, the Act still allows a landlord to recover arrear rentals by an order of a court of law or by obtaining a ruling by a Tribunal. Unfair practices may include various matters described in the Act: for example, changing of locks, damage to property and intimidation. The Tribunal may determine the rent payable by a tenant, provided that the determination is just and equitable to both tenant and landlord and takes account of prevailing economic conditions of supply and demand and the need for a realistic return on investment for investors in rental housing.

14.7.3 Protection against eviction

It was seen above that the Constitution provides that no one may be evicted from their home, or have their home demolished, without an order of court made after considering all the relevant circumstances, and that no legislation may permit arbitrary evictions.

The Extension of Security of Tenure Act 62 of 1997 and the Prevention of Illegal Eviction from and Unlawful Occupation of Land Act 19 of 1998 strengthen the constitutional protection against eviction. They aim to protect specific classes of occupiers of land.

14.7.3.1 The Extension of Security of Tenure Act 62 of 1997

This Act applies only to rural land. The occupiers and owners of such land have certain rights and obligations. The Land Claims Court has confirmed that the Act can apply despite the existence of a lease between the parties.

An occupier's right of residence may be terminated on any lawful ground, provided that the termination is just and equitable in view of all the relevant factors. An occupier may be evicted only in terms of an order of court issued under the Act. Such order may be granted if the occupier's right of residence has been terminated in terms of the Act, the occupier has not vacated the land within the period of notice given by the owner or person in charge, and the conditions for an order for eviction in terms of the Act have been complied with. The owner or person in charge must, after the termination of the right of residence, give the

occupier, the municipality in whose area of jurisdiction the land in question is situated, and the head of the relevant provincial office of the Department of Land Affairs, for information purposes, at least two calendar months' written notice of the intention to obtain an order for eviction. The notice must contain the prescribed particulars and set out the grounds on which the application for eviction is based. A report must be submitted within a reasonable period by a designated officer on the availability of suitable alternative accommodation to the occupier, indicating how an eviction will affect the constitutional rights of any affected person, including the rights of the children, if any, to education, pointing out any undue hardships which an eviction would cause the occupier, and on any other matter as may be prescribed. If a court orders eviction in terms of the

Act, it must, with due regard to relevant factors, determine a just and equitable date on which the occupier must vacate the land and determine the date on which an eviction order may be carried out if the occupier has not vacated it. The court must further order the owner or person in control to compensate the occupier for structures, improvements and standing crops to the extent that it is just and equitable with due regard to all relevant factors.

The Land Claims Court has exclusive jurisdiction in matters relating to the Act. A magistrate's court or the High Court can, therefore, not hear matters where the Act is relied on.

14.7.3.2 The Prevention of Illegal Eviction from and Unlawful Occupation of Land Act 19 of 1998

This Act applies to all unlawful occupiers of residential property and requires that notice must be served on an unlawful occupier and the municipality with jurisdiction at least fourteen days before the hearing of eviction proceedings. Since the contents and manner of service of such notice must be authorised and directed by an order of court obtained in a separate application, it is clear that two separate processes are required before an eviction can be ordered.

If an unlawful occupier has occupied the land in question for less than six months at the time when the proceedings are initiated, a court may grant an order for eviction if it is of the opinion that it is just and equitable to do so, after considering all the relevant circumstances, including the rights and needs of the elderly, children, disabled persons and households headed by women. If an unlawful occupier has occupied the land in question for longer than six months at the time when the proceedings are initiated, the court must also consider whether land has been made available or can reasonably be made available by a municipality or other organ of state or another land-owner for the relocation of the unlawful occupier.

The Supreme Court of Appeal found that on its present wording, the Act also applies to a tenant whose lease was legally terminated but who refused to vacate the property. The effect of that is that it is now more difficult for a landlord to evict a tenant who is holding over.

Further reading

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Chapter 15
The Contract of Insurance

15.1 History and sources of the law of insurance
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15.3 *Essentialia* of the insurance contract
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15.6 Statutory protection of insured

15.1 History and sources of the law of insurance

Next to the contract of sale, the contract of insurance is probably one of the most frequently concluded contracts in the modern business world. The origin of the contract of insurance can be found in trade usages which existed in the medieval Italian city states to provide for risks attached to sea transport. Initially, marine insurance was the only type of insurance concluded, but with time other forms of insurance have developed. As a result of the important role transport played in the development of the European continent, the practice of insurance spread to other countries where it was adopted and developed. Today the concept of insurance is developed to such an extent that there is hardly a risk one cannot insure against.

The South African law of insurance is primarily governed by Roman-Dutch common law. The fact that Roman-Dutch writers on the law of insurance discuss only marine insurance does not change the situation, since the principles of marine insurance can, where necessary, be extended to and developed for other types of insurance. In cases where Roman-Dutch law does not provide an answer to a certain problem, the courts can do comparative legal research on the applicable law in other legal systems; in this way a South African law of insurance can develop. In this context, the English law of insurance will only be a source of comparative law, and not, as it used to be, the common law of South African insurance law.

Reference must also be made to the Long-term Insurance Act 52 of 1998, the Short-term Insurance Act 53 of 1998 and the Financial Advisory and Intermediary Services Act 37 of 2002. Although these Acts mainly regulate and control insurance business they contain a few provisions which apply to insurance contracts and insurance intermediaries. The Acts also provide some measure of protection to insurance consumers. It must be noted that subject to certain conditions the Consumer Protection Act 68 of 2008 does not apply to contracts of insurance (see chapter 30).

15.2 The nature and basis of the contract of insurance

The basis of insurance refers to the purpose of the contract of insurance: in other words, the reason for entering into a contract of insurance. Traditionally, the purpose of insurance was to indemnify the insured against patrimonial loss as defined by law. This is referred to as the 'principle of indemnity'. The insured concluded a contract with the insurer and the insurer undertook to indemnify the insured. The principle of indemnity was therefore seen as the basis of the contract of insurance. The traditional principle of indemnity could, however, not explain all types of insurance. For example, it could not

explain the basis of non-indemnity insurance (capital insurance). The principle of indemnity has therefore been adapted to include both compensation for patrimonial loss and satisfaction for non-patrimonial loss. In terms of this approach, a contract of indemnity insurance is a contract intended to compensate the insured for patrimonial loss. A contract of non-indemnity insurance is a contract intended to compensate the insured for non-patrimonial loss resulting from the impairment of an abstract interest.

In practice, one effects insurance by contributing to a fund to which other persons that are exposed to the same risks also contribute. The risks that endanger the formation, preservation and development of the insured's estate are thus distributed amongst a group of people who are equally at risk. As indicated above, the law recognises two types of insurance contracts, namely, indemnity insurance and non-indemnity insurance contracts.

15.2.1 Indemnity insurance

In indemnity insurance the insurer undertakes to make good the damage which the insured may suffer through the occurrence of the event insured against. For example, the Fire Insurance Company agrees with Alfred that it will make good the loss which Alfred may suffer if his house burns down. If Alfred's house subsequently burns down, and he can prove that it was worth R100 000, he can recover R100 000 from the Fire Insurance Company. Examples of indemnity insurance are property insurance (for example marine, fire, theft and motor vehicle insurance) and liability insurance.

15.2.2 Non-indemnity insurance (capital insurance)

In the case of non-indemnity insurance, the insurer undertakes to pay the insured or the beneficiary a fixed sum of money if the event insured against takes place. The occurrence of the event causes non-patrimonial harm and creates an abstract need which requires consolation or satisfaction. Non-indemnity insurance includes life and personal accident insurance. For example: Your Life Insurance Company agrees with Brian that it will pay R50 000 to Brian's wife when he dies. Brian dies, and his wife can claim the R50 000 from Your Life Insurance Company.

15.3 *Essentialia* of the insurance contract

The *essentialia* of a contract are those terms which distinguish a particular contract from other types of contracts. It is not easy to identify the *essentialia* of an insurance contract, since the courts have, as yet, given no comprehensive definition. For the present the following will suffice:

(a) an undertaking by the insured to pay a premium
(b) an undertaking by the insurer to compensate the insured for either a patrimonial or a non-patrimonial loss
(c) a term that makes the insurer's obligation dependent on the occurrence of a particular uncertain future event (the risk)
(d) an insurable interest.

15.3.1 The premium

The insured undertakes to pay a premium. The premium is a consideration given or to be given in return for an undertaking to provide policy (insurance) benefits. It is usually in the form of a sum of money, but may also consist of something else. Although the actual payment of the premium is not a requirement for the creation of the contract (an undertaking to pay is sufficient), payment is usually a (suspensive) condition for the policy to take effect. However, in the absence of such a condition in the contract, the general rule applies and the contract, if the other requirements have been met, comes into being when an undertaking to pay the premium has been given.

When a premium is paid in bank notes or coins, the recipient must give the insured a written receipt for it.

15.3.2 An undertaking by the insurer to compensate the insured

15.3.2.1 Determination of the amount payable (non-indemnity insurance)

In the case of non-indemnity insurance, the sum payable will be a predetermined amount. Where, for example, a person insures his or her life for R100 000 (the insured amount), the insurer will have to pay that amount to the estate of the insured or the beneficiary.

15.3.2.2 Determination of the amount payable (indemnity insurance)

In the case of indemnity insurance, the insurer's obligation is to pay a determinable sum of money. The exact amount of the payment is determined after the occurrence of the event insured against, by determining the extent of the damage.

The value of the claim, or the measure of indemnity in respect of the loss of the risk-object, is determined, not by its cost, but by its value at the date and place of the loss. The insured must be placed in the same financial position he or she was in — but not a better financial position — before the occurrence of the event

insured against. The sentimental value of the object is thus ignored and only the present value of the object is considered, irrespective of whether its value has appreciated or depreciated since the conclusion of the contract.

For example, if a house valued at R200 000 is insured against fire and at the time of its subsequent destruction by fire it is worth R250 000, then the insured's loss which he or she may recover from the insurer is R250 000. Normally, however, a maximum value of compensation is stipulated in the insurance contract. In such a case the insurer is liable only for the amount of the insured's loss or the maximum insured value, whichever is the lesser.

Where the object has only been damaged the insurer will be liable for the amount of the partial loss suffered. The extent of partial loss is usually taken to be the cost of

repairing the risk-object. In indemnity insurance contracts the principles discussed in the following paragraphs regulate the undertaking by the insurer to pay a sum of money.

15.3.2.2.1 Valued and unvalued policies

In order to eliminate difficulties regarding proof of the value of the risk-object, the parties may agree at the time of concluding the contract on the value of the risk-object. Such policies are known as 'valued policies' in contrast with 'unvalued policies'. In the case of a valued policy the insured need not prove the exact amount of his or her loss but need only prove that he or she has, in fact, suffered a loss. A valuation in a policy must not be confused with a limitation of liability to a certain amount. In the latter instance, the insured is entitled to claim only the exact amount of his or her loss up to the amount of the sum insured in the policy.

15.3.2.2.2 The insurer's right to repair

An insurer often reserves the right in an insurance contract to have the damaged risk-object repaired, instead of compensating the insured. If a claim has been made under the contract, the insurer must choose, within a reasonable time after the occurrence of the event insured against, whether it wishes to repair the risk-object rather than to compensate the insured. Once the insurer has elected to repair the risk-object, it cannot change its mind later on. The insurer must then have the risk-object completely repaired within a reasonable time.

15.3.2.2.3 The insurer's right of subrogation

Subrogation provides a right of recourse for an insurer who has indemnified its insured. The insurer takes the place of the insured and is allowed to institute an action in the name of the insured. The parties to the lawsuit have the same rights and defences as they would have had, had the claim not been subrogated. Subrogation does not affect the rights and duties of either the plaintiff or the defendant. Where the insured has a claim against a third party who has caused the damage to the risk-object, the insured may not recover compensation from both his or her own insurer and the third party. Accordingly, once the insurer has compensated the insured, the insurer has the 'right of subrogation': that is to say, the insurer itself

may enforce the insured's claim against the third party in the name of the insured. The insurer does not have a right of subrogation unless the insured has been fully compensated for his or her loss. For example, the insured may be under-insured or may be subject to an excess clause. In these circumstances the insured still has a claim against the third party for the balance of his or her loss and the insurer is not subrogated. Once the insurer has a right of subrogation it may recoup, out of the proceeds of the action against the third party, the sum paid to the insured.

15.3.2.2.4 Insuring with several insurers

An insured has the right to insure the same risk-object with as many insurers as he or she wishes. In the event of a loss occurring, the insured may, however, only recover the full amount of the loss and no more. Thus where the insured is over-insured by double insurance, a choice must be made whether to recover the total loss from one insurer or a *pro rata* portion from each of the insurers concerned. Where an insurer pays more than its *pro rata* share of the amount claimed, it has, on the grounds of the 'principle of contribution', a right of recourse against the other insurers of the same risk-object, for a *pro rata* contribution towards the compensation paid to the insured.

15.3.2.2.5 Over- and under-insurance

There is nothing to prevent an insured from insuring for a larger amount than is necessary to secure full compensation in the event of loss of the insured risk-object. In the case of indemnity insurance, however, the insured may recover no more than the total value of the loss.

Where an insured insures for an amount less than the actual value of the insured object, he or she is under-insured. Contracts of insurance often contain an 'average clause' in terms of which the insured is regarded as an insurer for the uninsured balance and, consequently, must him- or herself bear a proportion of his or her loss. For example, if Gary's car, valued at R10 000, is insured for R6 000, and the car is damaged, then according to whether the amount of the damage is R10 000, R7 000 or R5 000, Gary will be able to recover only R6 000, R4 200 or R3 000 respectively: in other words, as he insured for only six-tenths of the value, he can recover only six-tenths of his loss. This aspect is of particular importance with respect to insured objects of fluctuating value.

15.3.2.2.6 Excess clauses

It may be agreed in an insurance contract that the insured may recover only a specified proportion of his or her loss. In motor vehicle and liability insurance, so-called excess clauses are common. In terms of these clauses the insured must bear a specific proportion of the loss him- or herself, for example the first R1 000 of the loss.

15.3.3 The risk

15.3.3.1 Agreement to insure against a particular risk

The uncertain event insured against is known as the risk. Description of the risk in the contract is important because the insurer must know precisely the nature of the risk, and the insured the extent of his or her cover. The parties always agree to insure against the occurrence of a specific (or determinable) event. The insurer's obligations are always coupled with some event which must cause the result mentioned in the contract, for example, a fire which damages the insured's house.

The description of the risk must include:

(a) the object insured, for example, a motor car, or a person's life
(b) the hazard insured against, for example, theft
(c) circumstances affecting the risk, for example, limitation of the insurance to theft of a motor car while it is parked in a specific place.

A number of other factors may also affect the risk. The risk and its circumstances may be further refined by qualifications relating to time and place. For example, the parties may agree that the insurer will only be at risk for a certain time of day, or may limit, define or add exclusions to the risk. An exclusion clause will stipulate that the insurer will not be liable if the risk materialises under certain circumstances. A clause providing that an insurer will not be liable for any damage occurring to a vehicle whilst being driven by an unlicensed driver is an example of an exclusion clause. In insurance contracts, clauses limiting or excluding the insurer's obligation which are expressed in vague or ambiguous terms must be interpreted strictly, and in favor of the insured. Thus an insurer, as the party who usually drafts the insurance contract (containing both its undertaking to perform as well as any limitations or exclusions on that undertaking), bears the duty of expressing its undertaking, and the limitations it wishes to put on it and the risks it wishes to exclude, in clear and unambiguous terms. Where there is ambiguity, the rule that says that in the event of an ambiguity the contract must be interpreted in favour of the insured rather than the insurer will apply.

15.3.3.2 The difference between insurance contracts and wagering contracts

As far as the event insured against is concerned, there is uncertainty about when and, in the case of indemnity insurance, also whether the event will occur. This element of uncertainty which is associated with risk is the one aspect which a contract of insurance has in common with a wagering agreement. Both are contracts of chance, depending on an uncertain event or contingency; and both contain an element of risk. The differences between wagering and insurance contracts are as follows:

(a) A wagering contract is unenforceable in court.
(b) In wagering contracts, the parties choose an arbitrary event on the occurrence of which one party wins and the other loses. The parties thus create their

interest in the event themselves, whereas the parties in an insurance contract have an insurable interest in the non-occurrence of the event. The requirement of an insurable interest is discussed in greater detail below.

(c) An insurance contract does not itself create the risk of loss.

(d) The intention with which the parties conclude an insurance contract can be of the greatest importance in distinguishing it from a wagering contract. The purpose of an insurance contract is to protect a person's estate while that of a wager is to increase the estate.

15.3.4 Insurable interest

An insurable interest exists whenever a particular event causes someone damage or loss. Only those who have an insurable interest can recover on the policy, and then only to the extent to which that insurable interest is damaged or lost. Loss or damage is brought about if a person's estate is diminished or infringed. In the insurance context, loss or damage is therefore defined with reference to insurable interest and an insurable interest is used to determine whether the insured has suffered a loss or not. An insurable interest is also used to distinguish between a wagering and an insurance contract. The insured must have an interest in the non-occurrence of the uncertain future event and such an interest distinguishes an insurance contract from a wager.

15.3.4.1 Indemnity insurance

In indemnity insurance the insured must at least have a financial interest in the non-occurrence of the risk. There is also authority for the point of view that the financial interest must have some legal foundation: for example, the interest must depend on a right in the object at risk, such as a proprietary right or a personal right. When an insured has the required financial interest he or she will suffer damage on occurrence of the event and will therefore be entitled to compel the insurer to honour its obligation to pay a sum of money. The time at which the interest must exist is also clear if the above is kept in mind: the interest must exist at the moment the loss or damage occurs. It is therefore not necessary for the interest to exist at the moment when the contract is concluded.

An owner of a thing has an insurable interest in it. For example, Siphiwe can insure his car. Similarly, a buyer may insure the property he or she has bought and a lessee can insure the property let to him or her. In every case the insurable interest of the insured, be it an owner, buyer, lessee or any other person, will be determined by the loss that such a person may suffer on the occurrence of the event insured against.

15.3.4.2 Non-indemnity insurance

In non-indemnity insurance a distinction must be drawn between insurance on one's own life or the life of a spouse on the one hand and the life of any other person on the other. In the first case an unlimited interest is presumed. Where the life of another is insured, the law requires an insurable interest in the sense of a

financial or pecuniary interest. A creditor therefore has an insurable interest in the life of his or her debtor. The moment at which the existence of an insurable interest is required in the case of non-indemnity insurance is the moment the contract is concluded. Even though the interest might not exist at the moment the risk occurs, the insured or the beneficiary will be able to claim the amount payable in terms of the contract.

15.4 The duty of good faith

Generally, the duty of good faith in insurance contracts relates to the right of the insurer to receive correct and complete information about material facts relating to the risk. This means that the duty is principally regarded as resting on the insured when he or she

completes a proposal form for insurance. This duty is imposed on the insured *ex lege*. This means that the duty of good faith relates to the pre-contractual negotiations between the parties. The duty of good faith requires the insured to refrain from providing information which is not true and to furnish information he or she possesses concerning material facts to the insurer. In other words, the prospective insured may not misrepresent or fail to disclose material facts to the insurer. Therefore the materiality of the information allegedly not disclosed is of great importance. The non-disclosure of a material fact would amount to material breach justifying repudiation of a contract by an insurer. The duty of good faith applies to all types of insurance. In cases of non-disclosure the insurer carries the burden of proving its defences while the insured carries the burden of proving his or her claim.

15.4.1 Misrepresentations

A misrepresentation is a positive act consisting of a pre-contractual statement of fact made by the prospective insured to the insurer. The statement must be incorrect and the insurer must, as a result of it, conclude the contract of insurance. The statement may be made orally or in writing, such as an incorrect or inaccurate answer given by the prospective insured to a question in a proposal form for insurance. Where an insured expresses an opinion, the statement does not amount to a statement of fact. The statement must further be untrue or incorrect and must relate to material facts. Materiality is determined by asking if a reasonable, prudent person would consider that the particular information constituting the representation should have been correctly disclosed to the insurer so that the insurer could form its own view as to the effect of such information on the assessment of the relevant risk.

An insurance contract induced by a misrepresentation of the insured is voidable at the instance of the insurer. In other words, the insurer may elect to uphold or to rescind the contract.

15.4.2 Non-disclosures

In insurance law it is accepted that the insured has a duty to disclose all material facts of which he or she might be aware before the conclusion of the contract.

A non-disclosure differs from a misrepresentation in that the act which creates the wrong impression is not a positive one but an omission. The insured fails to remove a wrong impression by not disclosing a fact that would have done so. The duty to disclose relates to all material facts. However, an applicant for insurance need only disclose those material facts of which he or she has knowledge. Facts he or she is not aware of or which are not material need not be disclosed. The test to determine whether facts which were not disclosed are material is the same as that for misrepresentations. The non-disclosure will be regarded as material if a reasonable, prudent person would consider that the particular information which was not disclosed should have been correctly disclosed to the insurer so that the insurer could form its own view as to the effect of such information on the assessment of the relevant risk. This is to limit the insurer's right to repudiate claims to cases of non-disclosure of material facts. Thus the insured is protected against repudiation of claims based on insignificant inaccuracies or trivial misstatements in insurance proposals.

If the insured does not comply with this duty the contract will be voidable at the instance of the insurer. The insurer can, therefore, dispute the contract not only if the insured makes a positive misrepresentation, but also if the insured does not disclose a material fact. An insurance contract induced by a non-disclosure of the insured is also voidable at the instance of the insurer. If the contract has a term that requires the insured to disclose a specific fact, any question as to the materiality or otherwise of that fact is irrelevant. Thus an insurer may impose the duty of disclosure during the currency of the insurance contract as regards specified facts even if they are not material. However, where the term imposing a duty of disclosure calls for the disclosure of material facts generally, then materiality is relevant.

15.4.3 Warranties

In the context of misrepresentations and non-disclosures, the use of warranties merits specific discussion. A warranty may be described as a strict contractual term by which the insured undertakes that certain representations are accurate or true. In the event of a breach of a warranty, the insurer may rescind the contract and avoid all liability for losses suffered after the occurrence of the breach, notwithstanding that the content of the warranty may not have been material to the risk or may not have contributed to the loss. Warranties previously allowed insurers to withdraw from insurance contracts without having to prove that the representation or non-disclosure involved was material. However, the common-law advantage which warranties afford insurers is curtailed by the Long-term and Short-term Insurance Acts. These Acts contain provisions which provide that an insurer can only rely on a misrepresentation or a non-disclosure, whether warranted or not, if it was of such a nature as to be likely to have materially affected the assessment of the risk. In other words, if the representation or non-disclosure which is warranted is immaterial, the insurer can no longer rely on it to avoid liability under the contract.

15.5 Parties to the contract

Apart from the insurer and the insured, other parties may also be involved when an insurance contract is concluded. These include insurance brokers and insurance agents.

An insurance broker is an independent intermediary who mediates insurance contracts between his or her client, the insured and the insurers. Brokers are not tied to any insurer in the sense that they are compelled to sell the products of one insurer only but may choose the best insurer depending on their client's needs. An insurance broker is primarily the agent of an insured and is mandated to obtain insurance coverage for him or her. As a result of the contract of mandate existing between a broker and the client, the broker owes the client a number of duties. The broker must, for example, act with

reasonable care and skill when mediating the insurance contract, obtain the best insurance available for the insured, assist the insured in disclosing all material facts, advise the insured as to the meaning of the policy and, generally, act in the best interest of the insured.

Insurance agents also mediate insurance contracts but, unlike insurance brokers, they are primarily agents of the insurer. An insurance agent may be either an employee or a mandatary of the insurer. The type of agent the insurance public is most likely to encounter will be a mandatary of the insurer. Such an agent acts under a mandate from the insurer to solicit completed applications forms from prospective insured persons and to transmit these proposals to the insurer's head office. These agents may be described as canvassing agents, insurance consultants or simply as insurance agents. Insurance agents often assist the prospective insured in completing the proposal form. Should the agent complete the form incorrectly, even though he or she may be aware of the true facts, the insurer will not be liable.

The Long-term and Short-term Insurance Acts provide that an agreement whereby the insured agrees that the insurer's agents will be exempted from liability for any act or omission, or whereby it is agreed that the insurer's agent will be deemed to be the insured's agent, is void.

It should be noted that insurance brokers and agents are regulated by the Financial Advisory and Intermediary Services Act 37 of 2002. This Act strives to supervise the way in which insurance intermediaries conduct their business. Contrary to popular belief, the Act does not codify the law relating to insurance intermediaries and all intermediaries are subject to the duty of care and skill as explained above.

15.6 Statutory protection of insured

As has already been mentioned, the Long-term and Short-term Insurance Acts contain some provisions which provide a measure of protection for those who conclude insurance contracts. In terms of these Acts the insured has a free choice in certain circumstances.

Parties who borrow money, lease goods or purchase goods on credit are often required by the creditor, as a condition of these contracts, to make available an insurance policy or the benefits under a policy to protect the interests of the creditor

in the event that proper performance in terms of the contracts does not take place. A creditor who requires a debtor to make such an insurance policy available must give the debtor prior written notification that he or she has a free choice —

(a) whether he or she wishes to enter into a new policy or to make available an existing policy
(b) if a new policy is to be entered into, as to the insurer with whom the policy is to be entered into and the person (if any) who is to act as intermediary
(c) if an existing policy is to be made available, as to the person (if any) who is to act as intermediary
(d) whether or not the value of the policy benefits made available shall exceed the value of the interest of the creditor.

Unless the person whose policy is to be made available to the creditor confirms in writing that he or she received prior written notification of the right to a free choice and that the right was accordingly exercised, it will be deemed that a free choice was not made. The security provided under such circumstances will be void and the creditor will have no claim to it.

Where the insured makes a claim for a benefit under a policy (insurance contract), an insurer is required to accept, reject or dispute the claim or the quantum of the claim within a reasonable period after receipt of the claim. The insured must be informed about the decision on his or her claim in writing, within ten days of an insurer taking the decision. Where the claim is rejected or disputed, the written notification to the insured must inform him or her of the reasons for the decision; the insured's right to make representations to the insurer in respect of the decision within a period of 90 days; the right to lodge a complaint under the Financial Services Ombud Schemes Act 37 of 2004 and the relevant provisions of the Act relating to the lodging of such a complaint in plain and understandable language; where the policy contains a time limitation provision for the institution of legal action, of that provision and the implications of the provision for the insured in an easily understood manner; in the event where there is no time limitation for the institution of legal action, of the prescription period that applies and the implications of that provision for the insured in an easily understood manner. Where another party takes such a decision on behalf of an insurer such person must include in such notice in addition to what is mentioned above, the name and contact details of the insurer and statement that any recourse or enquiries must be directed directly to the insurer. If the insured makes representations to the relevant insurer, that insurer will have 45 days from receipt of the representation to notify the insured of its decision. In case the insurer confirms the decision to reject or dispute the claim, the insurer must, among other things, inform the insured of the reasons for the decision and the facts that informed the decision.

It is also important to note that the insurer is prohibited from allowing the insured to sign any blank or partially completed form in connection with an insurance transaction where another person will be required, permitted or allowed to fill in other required detail, or conclude any such transaction where any such signing and providing of detail have occurred.

Further reading

P Havenga *The Law of Insurance Intermediaries* (2001)

MFB Reinecke, S van der Merwe, JP van Niekerk & P Havenga *General Principles of Insurance Law* (2002)

www.fsb.co.za (Financial Services Board)

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www.saia.co.za (South African Insurance Association)
www.insuranceombudsman.co.za (the Ombudsman for Short-term Insurance)
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Chapter 20
The Law of Agency

20.1 Introduction
20.2 The contract of mandate
20.3 Agency

20.1 Introduction

The term 'agency' is used in a variety of contexts. One of the meanings in which the expression is used is that of an agreement in terms of which one party undertakes to perform a task or commission on behalf of another. In this context agency indicates that the parties conclude a contract from which reciprocal rights and obligations flow. This contract is known as a 'contract of mandate' and is governed by the law of contract in general and by the rules applicable to contracts of mandate in particular.

'Agency' also occurs where one person (the agent) concludes a juristic act on behalf of another (the principal). A juristic act is an act which creates, alters, or extinguishes legal relationships through the expression of will of one or more persons (see also chapter 5). Used in this sense, agency combines the principles of mandate and representation.

Although agency and the contract of mandate are often associated, they are, in fact, two separate legal concepts. In the discussion that follows, the contract of mandate is discussed first. The rest of this chapter deals with agency or representation.

20.2 The contract of mandate

A contract of mandate arises when one party, the mandator, concludes a contract with another, the mandatary, in terms of which the mandatary undertakes to perform a mandate (that is, a commission or a task) for the mandator. The commission need not be undertaken gratuitously.

The mandatary may only perform juristic acts in the name of the mandator if authorised to represent him or her. This authority will frequently be agreed upon in the contract of mandate, or may be inferred from it.

The mandate may entail the performance of a single act, or be a general mandate to conduct all the affairs of the mandator. It may also be a mandate to conduct all business of a specified nature.

20.2.1 The duties of the mandator

20.2.1.1 The duty to compensate the mandatary for expenses

Originally, the contract of mandate was a gratuitous undertaking by the mandatary to perform a task. This is no longer so and the mandator must compensate the mandatary for all expenses incurred, and indemnify him or her in respect of liability which may arise from the execution of the mandate. Expenses include all sums paid on behalf of the mandator and all expenses and losses incurred in connection with the performance of the mandate, provided they were incurred in good faith. The mandatary is not entitled to compensation for expenses and losses incurred as a result of his or her negligence, or which were incurred unreasonably or unnecessarily.

The parties to a contract of mandate may agree that this duty of the mandator be excluded. But the mandator cannot refuse to pay expenses incurred by the mandatary merely because he or she would not personally have incurred them.

The mandatary has a lien (right of retention) in respect of goods acquired or received in the performance of his or her task, until he or she is compensated or indemnified by the mandator. (Liens arise by operation of law and are discussed in chapter 23.)

20.2.1.2 The duty to pay the mandatary the agreed remuneration

The mandator must pay the mandatary the remuneration on which they have expressly or tacitly agreed. The amount of the remuneration may be agreed, or may be determined according to a formula (for example, a commission fixed as a percentage of a determinable amount). When there is no agreement on the amount of remuneration, the remuneration will be determined according to the customary or reasonable rate. If the remuneration is for the completion of the mandate, it is to be paid out of the proceeds of the successful completion of the mandate. The mandatary loses the right to claim remuneration if he or she fails to execute the mandate, or if the object of the mandate is not realised, unless the parties have agreed otherwise.

Parties sometimes dispute whether the mandate has, in fact, been carried out. It may, for example, be argued that an estate agent who has been instructed to find a buyer for the mandator's house did not cause the prospective buyer to make the offer to purchase. This issue requires that it be established whether the mandatary has rendered the services that were required in the particular circumstances and in view of the nature of the particular mandate.

20.2.2 The duties of the mandatary

20.2.2.1 The duty to carry out the mandate

The mandatary undertakes to carry out a particular mandate. It is his or her main obligation to accomplish this task. Thus the mandatary must take reasonable steps to execute the mandate within a reasonable time. If the mandate cannot be fulfilled

through no fault of the mandatary, he or she will not incur liability towards the mandator.

In certain circumstances the mandatary may renounce the mandate. If the renunciation is legal, the obligation to carry out the undertaking comes to an end. If not, the mandatary must compensate the mandator for any damage he or she has suffered as a consequence of the unlawful renunciation.

20.2.2.2 The duty not to exceed the terms of the mandate

The exact scope of the mandate depends on the agreement between the parties. Although the mandatary may have been granted some discretion in the execution of the mandate, he or she may not act outside its ambit. The mandator is usually not bound by an act outside the scope of the mandate. But the mandator may elect to ratify the mandatary's act and to claim damages from the mandatary for acting beyond the scope of the mandate.

20.2.2.3 The duty to perform the mandate personally

The mandator selects the mandatary because of his or her specific skills, qualifications, professional standing, reputation or other relevant considerations. Therefore the mandatary must carry out the task personally, unless the parties have agreed otherwise. In certain circumstances the mandatary may employ someone else to perform the mandate. This may be the case where the mandate requires a service or the performance of an act which the mandatary does not usually perform, or where the mandator knows that the mandatary is not qualified to perform a specific act.

20.2.2.4 The duty to act with care and skill

A mandatary must act with reasonable care and skill in the execution of his or her mandate. The determination of what is reasonable takes into account the general level of skill and diligence possessed and exercised by members of the branch of the profession to which the mandatary belongs.

If the performance of the mandate requires any specific knowledge, skill or expertise, the mandatary warrants that he or she is suitably qualified or competent when the mandate is accepted. If that is not the case, the mandatary is liable for damages arising from the lack of the required skill.

The mandatary must not act negligently. If the mandator suffers damage as a result of negligent carrying out of the mandate, or of the mandatary's negligent failure to execute it, he or she must be compensated by the mandatary.

20.2.2.5 The duty to act in good faith

The contract of mandate creates a fiduciary relationship (a relationship of trust) between the mandator and the mandatary. Consequently, the mandatary must act in good faith when executing the mandate. This entails that the mandatary should act honestly and properly, in the interests of the mandator, and must not intentionally cause him or her harm or injury. If the mandatary has, for example, been entrusted

with the sale of an asset, he or she may not purchase the asset for himself or herself. The mandatary may also not make a profit from the contract of mandate. Any benefit made by the mandatary without the consent of the mandator must be accounted for and handed to the mandator. The mandatary may, moreover, not use any confidential information obtained during the execution of the mandate to the detriment of the mandator.

20.2.2.6 The duty to render accounts

The mandator may request the mandatary to furnish information regarding the progress of the mandate from time to time. The mandatary also has a general duty to render proper accounts as required by the contract of mandate, by statute or by trade usage. The mandatary's statement should reflect all information to which the mandator is entitled, including an inventory of acquisitions and money received and of things transferred, alienated or paid for in the name of the mandator.

The form of and times for rendering accounts may be determined by agreement, statute or trade usage. In the absence of any pre-determined times, the account should be rendered on execution or termination of the mandate.

20.2.2.7 The duty to account

On completion of the mandate the mandatary is accountable to the mandator for everything that fell within the ambit of his or her mandate. This usually entails the transfer of assets or rights to the mandator.

20.2.3 Termination of the mandate

A contract of mandate is terminated in the same ways that other obligations are extinguished (see chapter 12). The circumstances mentioned below are of particular relevance with regard to contracts of mandate.

20.2.3.1 Death of the mandator or the mandatary

Since the mandatary must personally execute the mandate, the contract is terminated when the mandatary dies. It also comes to an end on the death of the mandator. The mandatary is entitled to compensation for expenses incurred after the mandator's death, if the mandate is completed in good faith and in ignorance of the mandator's death.

20.2.3.2 Sequestration of the estate of the mandator or the mandatary

The contract will terminate if sequestration of the mandatary's estate makes it impossible for him or her to perform the mandate. If the mandator's estate is sequestrated, the authority of the mandatary to represent the mandator in the performance of a juristic act is terminated. Sequestration of the mandator's estate also curtails his or her ability to incur expenses, and may therefore, also for this reason, terminate a contract of mandate.

20.2.3.3 Insanity of the mandator or the mandatary

A mandator loses his or her contractual capacity on becoming insane. He or she is therefore regarded as having terminated the mandate. As is the case when the mandator dies, the mandatary is entitled to compensation for expenses incurred after the mandator's insanity, if the mandate is completed in good faith and in ignorance of the mandator's insanity.

The insanity of the mandatary renders him or her incapable of performing juristic acts and brings the mandate to an end.

20.2.3.4 Revocation by the mandator

At common law the contract of mandate was a gratuitous undertaking which could be revoked at any time. This is no longer the position and it seems that the contract may only be revoked by the mandator for a legally acceptable reason. Should no such reason exist, revocation may amount to a breach of contract, for which the usual remedies will lie. The parties may, of course, agree under which circumstances the mandator may revoke the mandate.

20.2.3.5 Renunciation by the mandatary

In the absence of an agreement between the parties, the common-law position that the mandatary could freely renounce the mandate, but would then forfeit any compensation for expenses, no longer seems appropriate in circumstances where the mandatary is remunerated for his or her work. If there are no legally acceptable reasons for renunciation, the mandator is entitled to the usual remedies for breach of contract if the mandatary withdraws from his or her obligations under the contract of mandate.

20.3 Agency

A person who wishes to conclude a contract does not have to do so personally. He or she may prefer, whether for the sake of convenience or for other purposes, to authorise someone else to enter into the contract on his or her behalf or in his or her name. Sometimes representation is essential. A legal entity such as a company or a close corporation cannot, for example, itself conclude a contract. The enterprise must, of necessity, be represented by a natural person or persons.

The concept of agency, or representation, arises when one person, the agent or representative, concludes a juristic act for or on behalf of another, who is called the principal, with the result that a legal tie arises between the principal and a third party or third parties. Any rights acquired and duties assumed by the agent are for the principal and not for the agent. Used in this sense, agency comprises the totality of juristic relationships which arise among these three parties.

Agency serves various needs in modern society. In the first place, the interests of those who have no capacity to act can be protected. Secondly, agency makes it possible for juristic acts to be performed on behalf of persons who are absent. It also allows the use of specialised services of specific agents: for example, for

a power of attorney to be given to a conveyancer (the agent) to register property in the name of someone else on behalf of the principal (the client, who would normally be the seller). Agency in the context of the international sale of goods is regulated in the Convention on Agency in the International Sale of Goods Act 4 of 1986. This aspect is not dealt with here.

For a person to perform an act of representation, certain requirements must be met. In the first instance, the principal must exist. Anyone with the capacity to perform juristic acts can appoint an agent to act on his or her behalf. Secondly, the agent must have

authority to perform the act. This aspect is discussed below. The agent must, in the third instance, make it clear to the third party that he or she (the agent) is acting for someone else and not in a personal capacity. No specific words to this effect are required. But the following expressions, words, or abbreviations are frequently encountered in practice to indicate representation: 'for', 'on behalf of', 'pp', and 'qq'. The agent need not identify the principal. The same person can act as principal and agent simultaneously. For example, if Margaret and Karin wish to buy something jointly, Margaret may act both in her personal capacity and as Karin's agent in concluding the contract of sale.

20.3.1 Authority

An agent has to have authority to conclude juristic acts on behalf of someone else. The authority given by the principal to the agent to represent him or her may be express, or it may be implied by the law or on the facts. Where such authority does not exist, the lack of authority may sometimes be cured by ratification or estoppel, so that agency still arises. Ratification and estoppel are discussed below.

The person relying on the authority has to prove that such authority existed at the time when the juristic act was concluded.

20.3.1.1 Authorisation

The most common source of authority for concluding a juristic act on behalf of another is express authorisation by that other person, in other words a manifestation by the principal of his or her intention that the other party shall act on his or her behalf. Normally no formal requirements are imposed for such authorisation. The authorisation is a unilateral act, although it may be closely linked to a contract. In certain instances, however, a formal appointment by means of a written power of attorney is required (for example, to appoint a conveyancer to register an alienation of property).

Authorisation by way of agreement between the parties does not necessarily have to be express, but can also arise by tacit (silent) agreement. The tacit agreement is established by the fact that the principal's conduct and attitude in respect of the agent is such that the only reasonable inference which may be drawn is that the principal wishes the agent to act on his or her behalf. If, for instance, a farmer were to send his or her cattle to an auction, and the auctioneer sold the cattle to a purchaser, the farmer's conduct would indicate that he or she had given the auctioneer tacit authority to sell the cattle.

20.3.1.2 Other sources of authority

In certain instances the authority is implied by law and does not come about by agreement. In many of these instances the agent's authority is derived from his or her appointment to a particular office. The consent of the principal for such authorisation is not required. For example, the guardian of a minor has the authority to conclude juristic acts on behalf of the minor. Similarly, an insane person's curator has authority to enter into juristic acts on his or her behalf. The curator is appointed by the court. Usually the extent of the curator's authority is also determined by the court.

The authorisation of the directors, or of a particular director, to act on behalf of a company, is normally regulated in the Memorandum of Incorporation of that company. The Memorandum of Incorporation does not constitute a contract between the director(s) and the company. Therefore, the authority of a director should be regarded as an example of authority by operation of law (see chapter 21).

The Close Corporations Act 69 of 1984 provides that any member of a corporation shall, in relation to a person who is not a member and is dealing with the corporation, be an agent of the corporation. Any act of a member binds the corporation to such a third party, whether or not the act is performed for the carrying on of the business of the corporation, unless the member so acting has, in fact, no power to act for the corporation in the particular matter, and the person with whom the member deals has, or ought reasonably to have, knowledge of that fact (see chapter 21).

The contractual relationship between partners is the source of a partner's authority to conclude contracts. In terms of the principle of mutual mandate, every partner has the power to bind the partnership (that is him- or herself together with the other partners) in transactions falling within the normal partnership business.

Sometimes authority that has not been expressly given can be inferred from the principal's conduct. The conduct of the parties must not allow any other interpretation but that they intended a relationship of principal and agent to exist between them. An example from one of the decided cases is where one party allowed another to negotiate for the sale of a hotel to a potential buyer, paid him various amounts of money on several occasions, and wanted him be present at the final negotiations. The court held that the inference of agency was inevitable in the circumstances.

20.3.1.3 Delegation of authority

An agent's authority may include the authority to delegate, that is, to authorise a sub-agent to perform a juristic act for the principal. The power to delegate may be given expressly or tacitly. Whether the principal intended the agent to have the power to delegate is a question of fact. An important consideration is whether performance of the act requires particular skill or expertise, or whether the act can be performed by any person (see also paragraph 20.3.2.3).

20.3.1.4 Termination of authority

A person's authority to conclude juristic acts on behalf of another can be terminated in a number of ways. If the authority was given to conclude a specific juristic act, the authority comes to an end once the agent performs that act, or lapses when the act can no longer be concluded. Should the authority be given for a specified time, it lapses when the time expires. No act is required by the principal to terminate the authority. If the authority was derived from a special relationship, it is extinguished as soon as that relationship ceases to exist. For instance, the authority of a guardian to act on behalf of a minor is extinguished as soon as the minor ceases to be a minor. Authority also terminates when the principal or the agent dies, or if there is any change to the status of the principal which restricts his or her capacity to conclude juristic acts: for example, if

he or she becomes insane, or if the principal's estate is sequestrated. The principal cannot conclude acts through a representative if he or she is not able to do so in person. But, since the representative acts on someone else's behalf, the agent's authority does not come to an end when his or her estate is sequestrated.

The principal may revoke the agent's authority if the authorised act has not yet been concluded. It seems that a representative's authority to conclude juristic acts cannot be rendered irrevocable. But if a contract purports to grant irrevocable authority to an agent, subsequent revocation of the authority by the principal may render him or her liable on a claim for damages for breach of contract.

An agent may renounce his authority at any time on just grounds, for example bad health. In the absence of such good cause, the agent may be liable to the principal for damages based on the ordinary principles of breach of contract.

20.3.1.5 Estoppel

If the principal has culpably created the false impression that another person has the authority to conclude certain juristic acts on his or her behalf, and the third party, to whom this representation has been made, acts to his or her detriment on the strength of that impression, the principal can be prohibited by law from denying the authorisation. If the requirements for estoppel are met, the principal is estopped, or precluded, from denying the authorisation and will be bound to the transaction as if the agent had indeed been authorised to conclude it. For example, someone who sends a domestic assistant to a shop to purchase goods on credit and regularly pays the accounts will remain liable for purchases made by the employee on the same account even after revocation of the employee's authority (provided the shop-owner is unaware of the revocation).

There are three requirements for estoppel. In the context of agency, the principal must, in the first place, by his or her words or conduct, have represented to the third party that the 'agent' had authority to contract on his or her behalf. The representation of authority must be attributable to the principal, or to someone for whose conduct he or she is responsible. In the second instance, although the representation need not have been intended to mislead, it must have been of such a nature that it could reasonably have been expected to mislead the third party.

A court will consider the circumstances of both the third party and the principal in this regard. It must, therefore, be shown that a reasonable person in the position of the third party would have inferred from the conduct or words of the principal that the purported agent was authorised to conclude the particular contract, and also that a reasonable person in the purported principal's position would have expected the words or conduct to induce this belief. Finally, the third party must have acted on the strength of the representation to his or her detriment. The third party cannot rely on estoppel if he or she was unaware of the representation, or if the third party knew that the agent was not authorised, or if he or she is, by law, deemed to know the scope of the agent's authority. For example, the Supreme Court of Appeal held that it could not be assumed that a branch manager of a bank had the authority to bind the bank to stand surety for a very large amount. Failure to confirm the authority in this case led to the finding that the representation had not reasonably been relied on.

A company may be estopped from denying the authority of an individual who purported to act on its behalf.

20.3.1.6 Ratification

If a person purports to act on behalf of another without authority to do so, the 'principal' is not liable. But if the principal ratifies the particular transaction concluded by the 'agent', the principal becomes liable. Ratification is the validation *ab initio* (from the beginning, that is, from the time when the particular transaction was concluded) by a person of a juristic act concluded on his or her behalf by another who did not have the authority to do so. The ratification can be express or tacit. The person who ratifies must, however, have knowledge of the particular juristic act which is being ratified.

Ratification is a unilateral juristic act. Therefore, the person who seeks to ratify does not require the consent of the other parties to the transaction, that is, the third party and the person who concluded the transaction on the ratifier's behalf.

Should the 'agent' not be authorised at the time when he or she concludes the juristic act, and the person, on behalf of whom the 'agent' has concluded it, accepts and ratifies the act at a later stage, the legal position is as it would have been had the 'agent' been authorised from the outset. Ratification is retroactive from the moment when the juristic act was concluded. Thus the transaction in question acquires the same legal force as if the party who purported to conclude it as representative had authority to do so in the first place. After ratification, the parties are treated as though a relationship of principal and agent had already existed at the time when the juristic act was entered into. A direct juristic tie comes into existence between the third party and the principal. They are liable to each other and can claim performance from each other.

Certain requirements have to be met before ratification can have legal effect. The 'principal' must have been in existence when the 'agent' purported to act on its behalf. If that is not the case, the contract cannot be validated retroactively. (The legislature has created some exceptions to this rule, allowing companies and close

corporations to ratify pre-incorporation contracts, that is, contracts entered into by agents on behalf of a company or a close corporation yet to be incorporated, after the incorporation of the particular business entity.) Before ratification can have legal effect, the 'agent' must also have made it clear that he or she was acting as representative of another when the agreement was entered into with the third party. The 'principal' must be named or ascertainable and must, moreover, both have the capacity to ratify and actually ratify the unauthorised contract in its entirety. The ratification must take place within a reasonable time after the act by the 'agent'. An illegal act cannot be ratified.

Before ratification has occurred, the purported principal acquires no rights or obligations in terms of the transaction. The third party is also entitled to undo his or her act before ratification. Even without doing so, the third party can refuse to accept ratification if it has not occurred within a reasonable time. If a specific act is not ratified, the person whose affairs have been managed may incur liability based on unjustified enrichment (see also paragraph 2.2.4.4.4).

20.3.2 The duties of the agent

The agent has the following obligations:

20.3.2.1 The duty to follow instructions

Where the agent has acquired the capacity to act as agent in terms of a contract of mandate, his or her conduct should fall within the parameters of this agreement. An agent is bound to act in accordance with the principal's instructions. Should an agent not follow these instructions to the best of his or her ability, the principal has a right of recourse against the agent.

20.3.2.2 The duty to exercise care and diligence

The agent must use such care, skill and diligence as is reasonably required for the due performance of his or her mandate. The standard of care required of an agent is that of the reasonably prudent person and may vary from case to case. If the business to be conducted requires a high degree of care and skill, the principal is entitled to expect such care and skill from the agent.

20.3.2.3 The duty of good faith

It is acknowledged in South African law that the agent occupies a position of trust and confidence in relation to the principal. This fiduciary relationship requires the agent to conduct those affairs of the principal to which the authority extends, in the interests of the principal and not for his or her own benefit. Four instances can be distinguished:

(a) **Secret profits.** All profits acquired by the agent in agency transactions are acquired for the principal. The agent may not make any secret profit from matters conducted on behalf of the principal. All profit resulting from the relationship with the principal must be disclosed to the principal. The principal

and agent may, however, expressly agree that the agent may personally acquire certain benefits.

(b) **Conflicts of interest.** No agent may place him- or herself in a position where the agent's interests and those of the principal conflict. If such a conflict does, in fact, arise, it must immediately be disclosed to the principal. For instance, should the principal instruct the agent to sell a car belonging to the principal at the highest possible price, the agent must disclose to the principal the fact that he or she wishes to purchase the car for him- or herself. This is so because the principal's interest in a high price for the car is in conflict with the agent's interest in acquiring the car at a low price.

(c) **Disclosure of confidential information.** The agent may not disclose confidential information regarding the principal's affairs obtained during the course of the agency. This duty continues even after termination of the agency.

(d) **Delegation of authority.** Generally, an agent may not delegate his or her authority to another agent, in accordance with the maxim '*delegatus delegare non potest*' (a person to whom authority has been delegated may not himself or herself delegate that authority). But delegation is allowed if the principal has allowed it, either expressly or impliedly.

20.3.2.4 The duty to account properly

An agent must at all times be able to account properly for all matters concerning the agency. This involves that, amongst other things, the principal's property must be kept separate; all books and documents relating to the agency business must be kept up to date; information must be disclosed to the principal when required, and everything belonging to the principal must be handed over on termination of the agency.

20.3.3 The duties of the principal

20.3.3.1 Payment of remuneration

If the parties have agreed on the payment of remuneration and the agent has substantially performed his mandate, the principal must pay him or her the remuneration. The agent must prove that there was an undertaking to pay. The undertaking may be apparent from the nature of the agent's work, commercial usages and so forth. If an agreement is silent on the subject of remuneration, it can be accepted as custom or usage that commercial agency contracts normally imply remuneration. If it has been proved that there was an undertaking to pay, it is presumed that the principal will pay reasonable remuneration. In case of a dispute, the agent has to prove that the remuneration claimed is reasonable. The agent must also prove that the task has been properly completed.

20.3.3.2 Reimbursement

The principal must reimburse the agent for all expenses necessarily incurred in the execution of the mandate. Expenses incurred as a result of the agent's own negligence, default or breach of duty need not be reimbursed.

20.3.3.3 Indemnity

The agent must be indemnified by the principal for all loss or liability incurred in the execution of the mandate, or which has been directly caused by such execution. The right to indemnity applies only to losses incurred directly as a result of the authorised acts. The agent has no right to be indemnified in respect of acts beyond the scope of his or her authority.

20.3.4 Personal liability of the agent or purported agent

Since an agent merely creates the legal relationship between his or her principal and the third party, there is normally no legal relationship between the agent and the third party. Only the juristic act has taken place between them. The only obligations that are created, altered or terminated are those between the principal and the third party. The agent incurs no liability to, nor rights against, the third party, unless he or she has agreed expressly or impliedly to do so. Whether such an agreement can be implied is a matter of fact that will depend on, amongst other matters, the normal business dealings between the parties and trade usage.

The identity of the principal need not necessarily be disclosed by the agent. If a third party is aware that the agent is acting on behalf of a principal, but he or she does not know the identity of the principal, the principal is known as an unnamed principal.

In certain cases the agent, or purported agent, can, however, incur personal liability. The 'agent' can always bind him- or herself by way of agreement in respect of a third person, for example, by a specific (contractual) warranty of authority. The liability of the 'agent' will then depend on the particular agreement.

There can be no representation of a person who does not exist (the statutory exceptions to this rule in respect of companies and close corporations were referred to above). Where a person purports to conclude a juristic act on behalf of another person who does not exist, no legal relationship comes into being. This is the position even when the contemplated principal subsequently comes into being and purports to ratify the representative's act.

An agent who does not disclose to the third party with whom he or she is negotiating that he or she is acting on behalf of a principal can incur personal liability to the third party. The third party can elect to hold either the principal or the agent liable. Similarly, either the principal or the agent can enforce the contract. The doctrine of the undisclosed principal is discussed further below.

An 'agent' who contracts on behalf of the 'principal' without authority, or who exceeds his or her authority, can also be liable on the basis of an implied warranty of authority. If the principal does not ratify the unauthorised conduct, the agent is

liable, not on the contract, but on the basis of the guarantee that he or she had the required authority. If the 'agent' acted fraudulently or negligently, the third party may also claim damages by means of a delictual action.

20.3.4.1 The doctrine of the undisclosed principal

The situation may arise that, by a contract of mandate, an agent is authorised and intends to contract on behalf of his or her principal, but fails to disclose his or her representative capacity to the third party. No contract is then formed between the principal and the third party. However, in terms of the doctrine of the undisclosed principal, derived from English law, the principal is entitled, once the representative has reached agreement (consensus) with the third party, to step into the agent's shoes as the real party to the contract. Similarly, the third party may hold the principal liable.

This doctrine has been criticised for being contrary to basic principles of both contract and agency. For example, it is inconsistent with the principle that only parties to a contract can enforce it and be made to perform it, and with the principle that an agent should make it clear that another person is being represented. Our courts regard the doctrine as too firmly entrenched in our law to be negated. But, because of its anomalous nature, they hold the view that it should be limited in its application.

In order for the doctrine of the undisclosed principal to apply, the agent must be authorised to contract on behalf of the principal. Subsequent ratification by the principal does not suffice. The agent must also intend to act on behalf of the principal. Finally, the agent must fail to disclose his or her representative capacity to the third party. The doctrine does not apply if the agent discloses that he or she is acting for someone else, but does not disclose the name of the principal (the so-called unnamed principal, who was referred to in paragraph 20.3.4).

In instances where the doctrine applies, the undisclosed principal may elect to claim the performance promised to the agent. If the principal does not make this claim, the third party is liable to the agent, who may enforce the contract in his or her own name. If the third party performs to the agent before the principal intervenes, the third party is discharged and performance to the principal cannot be enforced.

The agent's right to performance comes to an end when the principal comes forward and claims performance. The principal acquires no greater rights than the agent, and the third party can raise against the principal any defence which was available against the agent.

On discovery of the facts, the third party can hold either the principal or the agent liable. Once the third party has made this decision, he or she is bound by it.

Where the agent is acting on behalf of more than one principal, the doctrine of the undisclosed principal could expose the third party to a multiplicity of actions, since he or she would be obliged to perform to more than one creditor. It, therefore, does not apply in these circumstances. It also does not apply where the contract itself precludes it (for example, by providing that the 'agent' is not acting as agent

for any person), or where the third party wanted the contract to be concluded with the agent specifically (for example, to perform personal services).

Further reading

BP Wanda '*Agency and Representation'* in WA Joubert (ed) *LAWSA* vol 1

DH Joubert & DH van Zyl '*Mandate and Negotiorum Gestio'* in WA Joubert (ed) *LAWSA* vol 17

JTR Gibson *South African Mercantile & Company Law* 8 ed by Coenraad Visser (gen ed), JT Pretorius, Robert Sharrock & Marlize van Jaarsveld (2003)

AJ Kerr *The Law of Agency* 4 ed (2006)

Chapter 21
Forms of Business Enterprise

21.1 Introduction
21.2 The sole proprietorship (single-owner enterprise)
21.3 The partnership
21.4 Company law
21.5 The close corporation
21.6 The business trust
21.7 The co-operative

21.1 Introduction

Corporate law in South Africa was drastically reformed through the enactment of the Companies Act 71 of 2008, which came into operation on 1 May 2011. The Companies Act 71 of 2008 repealed the Companies Act 61 of 1973 except for Chapter XIV which will remain in operation until it is repealed by a separate Act of Parliament. One of the fundamental changes brought by the Companies Act 71 of 2008 is that it is no longer possible to form or incorporate close corporations (see paragraph 21.4 below)

The entrepreneur wishing to launch a business venture has a choice of several forms of enterprise.

Some available forms which an enterprise may take are:
(a) a sole proprietorship (an enterprise with a single owner)
(b) a partnership
(c) a company
(d) a business trust
(e) a co-operative.

Many factors will influence the entrepreneur's decision as to the form of enterprise he or she wishes to use as vehicle for the business. Some considerations are of a non-legal and practical nature, whereas others concern legal matters such as the number of and liability of participants in the venture, tax implications and the possible separate legal personality of the business entity (which is discussed below).

This chapter comprises only a general, and very basic, introduction to some of the forms a business venture may take and an overview of the law applicable to each enterprise.

21.2 The sole proprietorship (single-owner enterprise)

The most basic form of business enterprise is the sole proprietorship, or enterprise with a single owner. The individual who conducts this form of business acquires all the profits and bears all the risks of the enterprise. The sole proprietorship is, however, limited as a form of business enterprise, because its success depends on one person, the owner, and on that owner's creditworthiness and ability to run the business. The inability to separate the assets of the owner and those of the business also creates certain disadvantages. It means that the owner is fully liable for the debts and liabilities of the business. Furthermore, this type of business venture does not have the same favourable tax implications as some other forms of enterprise.

21.3 The partnership

21.3.1 Introduction

The partnership as a form of business enterprise developed from the notion that if two or more sole owners joined forces a stronger unit would develop because they would then have at their disposal their combined resources, financial and otherwise.

The partnership is possibly one of the oldest commercial institutions known to us. The South African law of partnership is largely governed by common-law principles. The work of the French writer Pothier and the English law of partnership are regarded as strong persuasive authorities.

Some statutes also contain provisions which concern partnerships. For example, the Attorneys Act 53 of 1979 provides that only practising attorneys may draw up, for reward, an agreement establishing or dissolving a partnership, and the Consumer Protection Act 68 of 2008 places a number of restrictions on the name a partnership may have. Other Acts contain provisions which apply to enterprises generally and therefore also to partnerships (for example, the Businesses Act 71 of 1991).

21.3.2 Definition and legal nature of a partnership

A partnership may be described as a legal relationship which arises contractually between two or more persons, in terms of which they agree to each contribute to a common business, with the object of making a profit for division between them.

A partnership is not a separate legal entity with separate legal personality (on separate legal personality, see paragraph 21.4.1 below). But in certain circumstances, a partnership is indeed treated by law as if it were a separate entity. In terms of the Rules of Court a partnership may sue or be sued in its partnership name. Litigation need therefore not be in the names of all the individual partners. And for purposes of sequestration a partnership is treated as an estate which is separate from those of its members. Creditors of the partnership must, in principle, claim against the partnership estate, and private creditors have a claim against the individual estate of the particular partner. These exceptions have been developed

to avoid practical problems and injustices, and do not detract from the general principle that the partnership is not a separate legal entity.

There are various types of partnership. Only the ordinary partnership (as opposed to universal and extraordinary partnerships) is discussed here.

21.3.3 The basic requirements *(essentialia)* of a partnership

Since a partnership agreement is a specific type of contract, it clearly must comply with all the general requirements for a valid contract. Therefore the parties to the agreement must have contractual capacity; they must reach agreement; the contract must be lawful; it must be possible to render performance in terms of the contract, and, if any formalities are prescribed for the contract, they must be adhered to.

Legal entities may be parties to a partnership agreement. For example, a close corporation may enter into a partnership agreement with a company, another close corporation, or a natural person. A partnership agreement may, like any other agreement, not conflict with legislation, public policy, or good morals. The Companies Act 71 of 2008 (discussed in paragraph 21.4) does not provide for any limitation on the number of partners in any partnership.

No formal requirements need be complied with. A valid partnership may therefore be concluded orally, in writing, or tacitly, that is, through conduct. But a written contract is preferable as it creates more certainty about the parties' rights and duties. There are three key elements or *essentialia* of a partnership agreement: each partner must contribute towards the partnership; the partnership must have as its object the making of profit to be divided among the partners, and the partnership business must be carried on for the joint benefit of all the partners. If the *essentialia* are present, and the parties intended to form a partnership, the agreement between them constitutes a partnership.

21.3.3.1 A contribution by each partner

Each partner must contribute something or undertake to contribute something to the partnership. This contribution may be capital (any property, for example, money, movable or immovable property), services, knowledge or skill. It may consist of corporeal or incorporeal (for example, copyright) things, and may also comprise a combination of various types of contributions, for example, labour and money. There is, generally, no restriction on the type of contribution that can be delivered, provided that it has commercial value.

The contribution must be made unconditionally. It must therefore be subjected to the risk of the partnership business. A person who makes a contribution to the partnership on condition that it must be repaid to him or her irrespective of the success of the enterprise is a creditor of the partnership and not a partner. A partner can, however, also be a creditor of the partnership if he or she lends an asset or money to the partnership in addition to making a contribution to it. For example, if partner Mahau contributes R20 000 to the partnership estate on condition that R8 000 be repaid to him after five years, Mahau will be a partner (because he contributed R12 000 unconditionally), as well as a creditor (in respect

of the R8 000), provided the other requirements for a valid partnership have been complied with.

21.3.3.2 The object of making a profit to be divided among the partners

The main object of the partnership must be to make a net profit in which each of the partners may expect to have a share. The net profit is the amount by which the gross income exceeds the expenses and losses. If the parties to the agreement have another objective, such as the advancement of sport or culture, and are not interested in making

a profit, no partnership is formed. If a charitable organisation makes a profit to use for a charitable purpose, this also does not constitute a partnership, because the aim is not to distribute the profit amongst the members.

No partnership can exist without community of profit. Should the parties agree that one or more of them will not be entitled to a share of the profits, no partnership comes into being. The requirement is met if a partner has only a hope or an expectation of sharing in the profit: for example, where the particular partner will share in the profit only when it exceeds a specific amount.

The partners are free to regulate the proportions in which they share profits, with one proviso only: that no one may be entirely excluded from the division. Partners may validly agree that only one or some of them will bear a net loss.

21.3.3.3 Partnership business to be carried out for the joint benefit of the parties

The partnership should be formed in the common interest of the parties: in the sense that the intention should be that each partner will derive a profit from it. Although a partnership is usually formed for the purpose of the continuous running of a business, it may also be formed in order to accomplish a specific project, such as the construction of a building. This requirement therefore implies that the partners should be jointly entitled to the common fund formed by their contributions.

21.3.4 The natural consequences *(naturalia)* of a partnership agreement

The natural consequences of a contract are those consequences which apply to the particular type of contract by operation of law. The specific contract may, however, determine that one or more of these consequences will not apply, without affecting the validity of the contract as a contract of that particular type. A provision in a contract of partnership which excludes certain natural consequences has no effect as far as other persons (often referred to as 'third parties') who have no knowledge of it are concerned, but is effective between the partners. The most common natural consequences *(naturalia)* of a partnership agreement are the following:

21.3.4.1 Mutual mandate

The basic principles of agency are discussed in chapter 20. Unless there is an agreement to the contrary, the general rule is that each partner, individually and without the collaboration of the other partners, has the capacity to perform any legal act concerning the administration of the partnership. Therefore, each partner can bind his or her co-partners as principals by performing any legal act which falls within the business sphere of the partnership. For example, if a partnership has been established to operate a restaurant, an application by one of the partners for a liquor license for the restaurant would fall within the business of the partnership. The purchase of a sports car, however, would fall outside the business of the partnership.

Unless a third party is aware of the partner's lack of authority, the partnership will be bound by a contract concluded between the third party and the partner which falls within the scope of the partnership business, despite the fact that the specific partner's capacity as representative has been excluded or restricted in the partnership contract.

21.3.4.2 The proportion in which the net profit is shared

Although it is an essential element of a partnership agreement that each partner must be entitled to share in the net profits of the partnership, the partners may freely arrange the proportion in which those profits are shared. In the absence of any provisions in a contract, the net profit is divided in the same ratio as the partners' respective contributions. Should it be impossible to value the respective contributions properly, the profit will be divided equally among all the partners.

21.3.4.3 The obligation to share in the net loss

If the trading result of the partnership is a net profit, it follows from the basic requirement that net profit must be divided between the partners, and that they must also share the losses (because losses and expenses are brought into account with the gross income of the partnership in order to calculate the net profit). If the trading result is a net loss, the general rule is that all partners also share in the losses. A partner can, however, be excluded from the obligation to share in the net loss by agreement. But there must be at least one partner who will carry the losses of the partnership.

21.3.4.4 The proportion in which the net loss is shared

In the absence of a provision to the contrary, net losses are shared in the same proportion as net profits. This means that the partner who receives the greatest portion of the profit must also absorb the largest proportion of the net losses. This situation can sometimes be unjust if the proportion in which the profit is shared is not in accordance with the respective contributions by the partners. It is therefore desirable that the partnership agreement should contain an express arrangement in this regard.

21.3.4.5 The proportion in which the assets are divided upon dissolution

If the partnership contract does not determine the ratio in which assets will be divided on dissolution of the partnership, the partnership assets are divided in the same ratio as the profits. If the partners have not come to an agreement regarding the manner in which the profits are to be divided, a pro rata division of the assets is made upon dissolution, in proportion to the partners' respective contributions to the enterprise. Should it be impossible to value the respective contributions, on dissolution the assets will be divided equally between the partners.

21.3.4.6 The proportion in which the partners are co-owners of the assets of the partnership

It was mentioned above that a partnership is not a separate legal entity. Therefore the assets of the partnership do not belong to the partnership, but to the partners jointly. The partners hold the assets as co-owners, in other words, they jointly hold the assets in undivided shares. Unless otherwise provided for, the partners are co-owners of the partnership assets in the same proportion as that in which the assets are divided upon dissolution. If this ratio is unknown, the partners are co-owners in the same ratio as that in which the profits are to be shared.

21.3.5 The rights and duties of partners

Partners have various rights and duties. Some are related to the *essentialia* of a partnership. Others are natural consequences of the partnership agreement, and some may have been expressly agreed upon by the parties to a specific partnership contract.

Partners have a reciprocal fiduciary relationship. This relationship may already arise during negotiation of the partnership agreement, in other words, before the partnership has actually come into being, and continues after dissolution and until the partnership has been finally liquidated. Three broad categories of fiduciary duties may be distinguished. In the first place, a partner must comply with his or her duties in terms of the partnership agreement (for example, the delivery of the partner's contribution). Second, the partner must advance the partnership interests unselfishly. In the third instance, all information relating to the partnership must be disclosed to all co-partners.

Partners are entitled to claim delivery of the contribution promised by a partner. Each partner is, furthermore, entitled to share in the profits of the partnership. When compensation has been agreed upon, it may be claimed. Partnership assets may be used by a partner as co-owner, provided that they are used to further the aims of the partnership. A partner may only use partnership property for his or her own purposes if the consent of the co-partners has been obtained, of if the partner's limited use of the property will not conflict with the interests of the partnership. Partners must also keep proper accounts, and are entitled to access to the accounting records of the partnership.

Unless otherwise agreed, each partner is entitled to participate in the management of the partnership and to perform management functions on its behalf. The principle of mutual mandate, which was discussed in paragraph 21.3.4.1, applies. Reasonable care and expertise must be exercised in the management of the business of the partnership.

Partnership rights can be enforced by one of two actions. The *actio pro socio* is a general partnership action and can be used, for example, to enforce specific compliance with the partnership agreement, or to claim dissolution of the partnership. The *actio communi dividundo* is used to effect physical division of tangible things held in joint ownership by partners.

21.3.6 The termination or dissolution of a partnership

When the partnership dissolves, the legal relationship which was created by the partnership agreement changes. The partnership estate is liquidated, creditors of the partnership are paid and any surplus is divided amongst the partners.

No formalities are required for dissolution of a partnership. Wide publicity should, however, be given to the dissolution, in order to avoid liability to parties acting on the erroneous impression that the partnership is still in existence.

21.3.6.1 Grounds for dissolution

Any agreement may normally be terminated by a subsequent agreement between the parties to terminate. A termination agreement in respect of a partnership may be express or tacit (for example, where the partners' conduct indicates that they consider their partnership to be dissolved).

The duration of the partnership may be determined in the partnership agreement. If the partnership has been formed for a specific term, it terminates automatically on the expiry of that period, unless the partners expressly or tacitly agree to continue the partnership. Before the expiry of that period, a partner may only terminate the agreement unilaterally on lawful grounds. However, should the parties continue the partnership after expiry of the agreed term, any partner may terminate it upon reasonable notice.

A partnership may also be terminated on the occurrence of an event specified in the partnership agreement. If a partnership has been formed for a specific project, for instance, the design of a specific office block, it will be terminated as soon as that object has been achieved.

Any change in membership terminates a partnership. The admittance of a new partner creates a new partnership and automatically terminates the previous one. Legally, it is regarded as an agreement between the existing partners and the prospective partner to form a new partnership jointly, not necessarily on the same terms and conditions as the existing one. The retirement or death of a partner also terminates the partnership. As a consequence, the partnership between the remaining partners is also terminated. They may, of course, (expressly or tacitly) conclude a new partnership agreement. The rule that a change in membership inevitably dissolves the partnership is regarded as too inflexible and economically

disruptive in some jurisdictions. Nonetheless, it is still applied strictly in South Africa.

A partnership will also be dissolved if it becomes objectively impossible for the partnership to function or to achieve its purpose as a result of events beyond the control of the partners, for example, acts of state or extraordinary natural forces.

The sequestration of the private estate of a partner dissolves the partnership. However, it does not necessarily mean that the estate of the partnership has to be

sequestrated. Should the estate of the partnership be sequestrated, the partnership also dissolves.

Personal circumstances such as the protracted illness or absence of a partner, certification that he or she is mentally incapable, or the fact that the partner becomes an enemy subject as a result of war, although he or she is still in the Republic of South Africa, may result in a court order which terminates the partnership agreement. Where a partner becomes a subject of the enemy and is resident in territory of the enemy, any partnership which exists between himself or herself and residents of the Republic of South Africa automatically terminates from the moment when he or she becomes a subject of the enemy. Partners may also apply to court for an order dissolving the partnership on the basis of a breach of the fiduciary relationship between the partners.

A partnership may be terminated by the unilateral act of a partner, if notice is given, or if the partnership is renounced for some lawful cause. Examples of lawful causes for the termination of a partnership are misconduct on the part of one of the partners (which irrevocably destroys the mutual trust and confidence between the partners); breach of a material term of the partnership contract by one of the partners; the fact that there is no longer a reasonable expectation that a profit will be made by the partnership, as well as personal circumstances and misfortunes which affect a partner.

21.3.6.2 Consequences of dissolution

While the partnership is being liquidated (after dissolution), the partners still owe fiduciary duties to one another. The partnership agreement, and the mutual mandate of partners, is terminated.

The rights and duties of the partnership towards third parties remain valid and binding. But the partners generally become jointly and severally liable for the partnership's obligations.

21.3.7 Liquidation of the partnership

Liquidation entails the realisation of the assets of the partnership, the payment of the partnership debts, and the distribution of the remaining assets or liabilities among the partners. The partnership agreement may contain provisions regarding the liquidation procedure. Partners may conduct the liquidation themselves, or they may appoint a liquidator to do so.

21.4 Company law

21.4.1 Introduction

The company as a form of business enterprise provides the advantage of legal personality and allows entrepreneurs to obtain more capital for their business venture. The business also has perpetual succession.

Nonetheless, a company cannot be equated with a natural person for all purposes. It cannot perform inherently human acts, such as the drafting of a will. Since it is primarily a business entity, it can generally only incur those rights and duties that are required for economic activity. It must necessarily act through its organs or agents.

The fact that a company is a separate entity existing apart from its members has important consequences. The company can acquire rights and duties in its own name. For example, it can acquire assets, conclude contracts, and sue and be sued in its own name in court. The company estate is also assessed separately from the estates of individual members. The members' liability is limited to the amount that each of them has invested in the company. Also, the sequestration of members' estates will not lead to liquidation of the company and the liquidation of the company does not necessarily result in the sequestration of members' estates. The perpetual succession or continuity of the company means that changes in its membership do not affect its continued existence. Also, investments in the company are transferable, so that each member can dispose of his or her investment without this affecting the company's continued existence.

In some instances the corporate entity is disregarded. Legislation provides for specific instances: for example, where the business of the company is being carried: on recklessly or with intent to defraud. Our courts have in the past been prepared to disregard the corporate entity, or 'pierce the corporate veil', in instances where they considered that it is being abused. The general policy, however, was not lightly to disregard a company's separate corporate personality, but rather to give effect to and uphold it. The Companies Act 71 of 2008 (see paragraph 21.4.2) confirms that a court may, in any instance where the incorporation, act or use of a company constitutes an unconscionable abuse of the juristic personality of the company, declare that the company is deemed not to be a juristic person in respect of certain rights, obligations, liabilities or parties, as the court decides.

21.4.2 Sources of company law

South African company law has been extensively reviewed and the Companies Act 71 of 2008 was signed by the President and published in *Gazette* 32121 on 9 April 2009. It came into operation on 1 May 2011.

The Act is, however, not a comprehensive codification of South African company law and where the common law has not been expressly excluded, it still applies to the extent that it is not amended by, or in conflict with, the Act. In some areas, for example directors' duties, common law is still an important source of company law. Moreover, developments in the company law of other legal systems,

especially English law (since South African company law was originally based on English law), have persuasive power. In this regard, the Act provides that to the extent appropriate, a court interpreting or applying it may consider foreign company law.

21.4.3 Formation, membership and types of company

The Companies Act of 2008 requires a Notice of Incorporation and Memorandum of Incorporation to be filed with the Companies and Intellectual Property Commission before a company can be registered. The Memorandum of Incorporation sets out the relationship

between the company and its shareholders; directors; other parties within the company, and third parties.

A company acquires legal personality from the moment of registration.

The Act provides for the incorporation of profit and non-profit companies. A profit company has the object of financial gain for its shareholders. It may be incorporated by one or more persons. There is no limit to the number of shareholders that it may have. Four types of entity may qualify as profit companies, namely, public companies, state-owned companies, personal liability companies and private companies.

A public company is identified by its name, which ends with the word 'Limited', or its abbreviation (for example, Eatwell Limited or Eatwell Ltd). All profit companies that are not state-owned companies, private companies or personal liability companies are public companies. Their shares are freely transferable and may be offered to the public. This feature enhances the marketability of the shares, which may be listed on a stock exchange (the shares do not, however, necessarily have to be listed on a stock exchange). At present there is only one stock exchange in South Africa, namely the JSE Limited.

The name of a private company ends with the words '(Proprietary) Limited', or its abbreviation (for example, Andrews Transport (Proprietary) Limited or Andrews Transport (Pty) Ltd). The Memorandum of Incorporation of this type of company prohibits it from making any offer of its securities to the public and restricts their transferability.

A state-owned company's name ends with the expression 'SOC Ltd'. This type of company falls within the meaning of 'state-owned enterprise' in terms of the Public Finance Management Act 1 of 1999, or is owned by a municipality. The South African Bureau of Standards (SABS) is an example of such a company.

A personal liability company meets the criteria of a private company, and its Memorandum of Incorporation must state that it is a personal liability company. Its name ends with the word 'Incorporated', or its abbreviation (for example, Andersons Incorporated or Andersons Inc). The directors and former directors of an incorporated company are jointly and severally liable, together with the company, for the debts and liabilities of the company incurred during their periods of office. Certain professions, for example attorneys, allow their members to form this type of company instead of practising in partnerships.

The name of a non-profit company ends with 'NPC' and its objects must relate to social activities, public benefits, cultural activities or group interests.

An external company is a foreign company conducting business or non-profit activities in South Africa. It must always have at least one office within the Republic.

Companies already registered when the Companies Act of 2008 came into operation are specifically provided for in the Act.

The shareholders of a company exercise their rights and the functions entrusted to them in the Companies Act or the Memorandum of Incorporation by adopting resolutions at shareholders' meetings. Normally a company resolution is passed by an ordinary resolution, which is a resolution by a simple majority of the members present and entitled to vote, and which constitutes a quorum. In certain circumstances a special resolution, as prescribed by the Act, is required. A shareholders' meeting may be called by the board or by any person authorised by the Memorandum of Incorporation. A meeting must be convened if required by the Act or the Memorandum of Incorporation, or demanded by shareholders holding at least 10 per cent of the voting rights that may be exercised at that meeting.

Company law is based on the common-law principle of majority rule. Shareholders may act against directors who have abused their power, and certain remedies enable them to protect their own rights. Personal liability may also be imposed where the separate juristic personality of a company has been abused.

21.4.4 Company organs and officers

The principal organs of the company are the general meeting of members, and the board of directors.

Every private or personal liability company must have at least one director. Public or non-profit companies must have at least three directors, who collectively form the board of directors. A director may conclude a separate service or other contract with the company, but a director is not necessarily an employee of the company. The directors' rights and obligations are determined by any existing contracts with the company, the company constitution, legislation and the common law. At common law, directors owe fiduciary duties and obligations of care and skill to the company. The Companies Act of 2008 introduced a partial codification of directors' duties, which includes duties similar to their common-law fiduciary duties and the duty to perform their duties with reasonable care and skill. However, the common law is not excluded by the statutory provisions and will continue to apply except in so far as it is specifically amended by the Act or is in conflict with one of its provisions.

The codified duties of a director are —

(a) to disclose to the board any personal financial interest in company matters
(b) not to use the position of director, or information obtained as director, to gain an advantage for him- or herself or for another person, or knowingly to cause harm to the company or a subsidiary of the company

(c) to disclose to the board of directors any material information that comes to a director's attention
(d) to act in good faith and for a proper purpose
(e) to act in the best interests of the company
(f) to act with a reasonable degree of care, skill and diligence.

The company secretary is the principal administrative officer of a company. Public companies and state-owned enterprises must have a company secretary, while other types of company may elect to appoint a company secretary. This important company officer is responsible, amongst other things, for guiding the directors in respect of their

duties and advising them of the law and legislation applicable to their company, ensuring that proper minutes are kept of company meetings, certifying in the company's annual financial statements whether the company has filed the required returns and notices, and ensuring that copies of the annual financial statements are sent to everyone entitled thereto. The company secretary is also responsible for the electronic submission of the company's annual return and must report to the company's board any failure on the part of the company to comply with the Memorandum of Incorporation or rules of the company, or with the Companies Act.

The compulsory disclosure of financial information concerning the company plays an important role in protecting the interests of shareholders, investors and creditors. The Companies Act imposes certain minimum financial disclosure requirements on all companies and more stringent disclosure requirements on public companies and certain private companies. Every company must keep in one of the official languages of the Republic such accounting records as are necessary to fairly present the state of affairs and business of the company and to explain the transactions and financial position of the trade or business of the company. A public company or state-owned company is required to appoint an auditor and an audit committee every year at the annual general meeting. Other companies are not required under the Companies Act to appoint an auditor, or an audit committee, but may do so voluntarily. The auditor must report to the company's members in the way, and about the matters, prescribed by the Act, and also has various other statutory duties.

21.4.5 Capital of the enterprise

The share capital of a company is the amount contributed to the resources of the company by the shareholders. A 'share' is the unit of the contribution made to the share capital. The money with which the contribution is made becomes the property of the company. The shareholder obtains certain rights against the company: for example, the right to receive dividends from its profits when such dividends have been properly declared. A shareholder's shareholding is evidenced by a share certificate, or by recording such shareholding in the securities account of a depositary institution acting for the particular company.

The company's Memorandum of Incorporation must state the authorised share capital, namely, the classes and number of shares that may be issued. The board

may subsequently amend the number and classes of shares. Shares are divided into various classes according to the rights afforded by them with regard to voting rights; the right to information; the right to share in profits that have been declared as dividends, and participation in a distribution on liquidation. The classes are preference shares, ordinary shares and deferred shares.

A company may, subject to the conditions stipulated in the Companies Act, purchase its own shares. It may also assist a person to acquire shares and other securities in the company, provided that such assistance is not prohibited by the Memorandum of Incorporation and that certain requirements are met.

21.4.6 Representation of a company

A company, as a legal person, cannot itself perform juristic acts but must act through agents (agency is discussed in chapter 20). When dealing with outsiders, the normal principle of the law of agency that the company agent must have the necessary authority to bind the company, applies. But, over the years, the demands of commercial practice have necessitated the development of specific rules with regard to agency in a company law context.

The Companies Act of 2008 provides that a company has all the legal capacity and the powers of a natural person except to the extent that a juristic person is incapable of exercising any such power or the company's Memorandum of Incorporation provides otherwise. The capacity of a company is not limited by its main or ancillary objects or business as it was under the Companies Act of 1973. Although the company's Memorandum of Incorporation may limit, restrict or qualify the purposes, powers or activities of the company, any such restriction would not render invalid any contract that conflicts with it. The contract remains valid and binding on the company and the other party to the contract. Each shareholder has a claim for damages against any person who fraudulently or owing to gross negligence causes the company to do anything inconsistent with the Act, or a limitation, restriction or qualification on the powers of the company as stated in its Memorandum of Incorporation, unless ratified by special resolution. However, if the company or directors have not as yet performed the planned action (for example, concluded the contract) that is inconsistent with a limitation or qualification contained in the Memorandum of Incorporation, one or more shareholders, directors or prescribed officers of the company may obtain a court order preventing the company or directors from doing so. A third party who did not have actual knowledge of this limitation or qualification and acted in good faith will be able to claim for any damages suffered as a result. Shareholders, directors, prescribed officers and a trade union representing employees of the company may also institute proceedings to prevent the company from doing anything inconsistent with the Act.

Directors may lack the authority to conclude a particular transaction because the Memorandum of Incorporation of the company specifically limits their authorisation. In such a case the company will still be liable on the transaction if the directors have exceeded the limits of their authority. Where the Memorandum

of Incorporation provides that a specific director (or the directors) may be authorised by complying with some internal formality (for example, by obtaining the prior approval of the general meeting for a specific contract), an outsider dealing with the company in good faith may assume that this authorisation has been obtained, unless the person knew or reasonably ought to have known of any failure by the company to comply with its formal and procedural requirements. This is the result of the codification, in such an instance, of the so-called *Turquand* rule, which previously applied in such circumstances. In certain circumstances the company can be held liable on a transaction on the basis of estoppel (estoppel is also discussed in paragraph 20.3.1.5).

The Act permits the conclusion of pre-incorporation contracts on behalf of a company to be incorporated. This constitutes an exception to the general common-law principle that there cannot be an agent in respect of a non-existent principal. A major disadvantage of the statutory provision is that a person who enters into such a contract is held jointly and severally liable for liabilities emanating from the pre-incorporation contract if incorporation does not take place, or the company does not ratify a part of the contract after incorporation. Such personal liability does not arise in terms of the common law and much pre-incorporation will therefore rather be structured under the common-law alternatives (benefit of a third party (*stipulatio alteri*), a trust or cession and delegation).

21.4.7 Winding-up, dissolution and deregistration

The existence of a company is terminated by its dissolution. The process of dealing with the company's affairs prior to its dissolution is known as the winding-up or liquidation of the company. This process entails tracing and realising the company's assets, and applying the proceeds to pay creditors of the company according to their order of preference and to distribute any residue among the shareholders of the company in accordance with their rights (see also paragraph 28.13).

A company that has ceased to trade may be de-registered. This does not necessarily mean that the company ceases to exist, but if it trades after its de-registration, it does so as an association without juristic personality.

21.4.8 Business rescue

The Companies Act of 2008 introduces business rescue provisions into South African company law. The purpose of these provisions is to facilitate the rehabilitation of a company that is in financial distress and appears unlikely to be able to pay its debts as they become due and payable within the following six months, or appears likely to become insolvent within that time.

The business rescue can be initiated by a company resolution or by a court order. During the business rescue period there is a general moratorium on legal proceedings and enforcement of judgments against the company. The disposal of company property during this period is regulated and special provisions apply to employment and other contracts to which the company is a party. A business rescue

practitioner is appointed to manage and control the company and the directors exercise their functions in accordance with his or her instructions. The business rescue practitioner must investigate whether there is a reasonable prospect of rescuing the company and is responsible for drawing up a business-rescue plan setting out how he or she intends to rescue the company. If the practitioner concludes that there is no prospect of rescuing the company, he or she must apply to court for an order discontinuing the business-rescue and placing the company in liquidation. If the company is no longer financially distressed, the business- rescue practitioner must apply to court for a termination order, or file a notice of termination, depending on how the order was initiated. Parties who may be affected by business-rescue proceedings are protected by various general statutory rights.

21.5 The close corporation

21.5.1 Introduction

The need for a smaller business entity with separate juristic personality arose as a result of the complexity of the Companies Act and the rather high costs attached to compliance with its provisions. The Close Corporations Act 69 of 1984 provides for a smaller, less complicated enterprise. A close corporation has characteristics of both a partnership and a company, and carries the advantage of being a legal person which exists separately from its members.

The Companies Act 71 of 2008 provides for the indefinite continued existence of the Close Corporations Act in respect of close corporations that were already in existence when the Act commenced. However, no new close corporations may be registered.

21.5.2 Formation and membership of a close corporation

Since the coming into operation of Companies Act 71 of 2008, it is no longer possible to form new close corporations. Therefore, all provisions in the Close Corporations Act relating to the formation of a close corporation are of no effect. Previously, a close corporation was created by the registration of a founding statement by the Registrar of Close Corporations. A founding statement is comparable to a company's Memorandum of Incorporation.

Although a founding statement is registered, nobody is deemed to have knowledge of its contents merely because it has been registered.

The name of a close corporation must end with the abbreviation 'CC', or its equivalent in any other of the official languages.

Subject to certain exceptions (relating to a juristic person holding a member's interest on behalf of a natural person), a close corporation may have only natural persons as members. At no time may there be more than ten members. If the corporation has two or more members, they may enter into an association agreement, or any other agreement, regulating the internal matters of the corporation, provided

that the agreement is not inconsistent with the provisions of the Act. If such an agreement is not concluded, the internal relations are regulated by the Act.

In a close corporation the members fulfil the roles of both the board of directors and the general meeting of a company. Generally, every member is entitled to participate in the carrying on of the business of the corporation, to exercise equal rights with regard to the management of the business of the corporation and to represent the corporation in carrying out its business. However, the Act precludes certain persons from participating in the management of the corporation. The consent in writing of a member or members holding at least 75 per cent of members' interests is required for certain matters (for example, a change in the principal business of the close corporation).

Members of a close corporation owe fiduciary duties and duties of care and skill to the corporation. These duties are similar to those owed by directors to a company, and are also entrenched in the Close Corporations Act.

The members of a close corporation are, in principle, not liable for its debts, but liability may arise, jointly and severally with the corporation, in circumstances specified in the Act. In addition, the Act provides for members' personal liability if they abuse the corporate form by carrying on the business of the corporation recklessly, fraudulently, or with gross negligence.

21.5.3 Capital of the enterprise

Every person who became a member of the corporation on registration had to make an initial contribution of money, property or services rendered in connection with, and for the purposes of, the formation and incorporation of the corporation. Contributions made at a later stage may not consist of services rendered.

A close corporation does not issue shares. The interest of a member in the corporation is known as a 'member's interest', and is expressed as a percentage of the total members' interests in the corporation. The total of members' interests must be one hundred.

A close corporation's capital is protected by having regard to its solvency and liquidity. Any payment may be made to members by reason of their membership, provided that —

(a) the corporation's assets exceed its liabilities after such payment
(b) the corporation is able to pay its debts as they become due in the ordinary course of business
(c) such payment will not render the corporation unable to pay its debts as they become due in the ordinary course of business.

21.5.4 Representation of a close corporation

The Act allowed the conclusion of pre-incorporation contracts on behalf of a yet-to-be-incorporated close corporation. As was mentioned in respect of companies, this constitutes an exception to the common-law principle that there can be no representation of a person not yet in existence (see also chapter 20).

A close corporation has the capacity and powers of a natural person of full capacity in so far as a juristic person is capable of having such capacity or exercising such powers.

The Act provides that every member of a close corporation is an agent of the corporation in relation to a person who is not a member of the corporation and who is dealing with it. The acts of a member bind the corporation to such a third party, whether or not the act was performed for the carrying on of the business of the corporation, unless the third party knew, or ought to have known, that the member had no power to conclude the transaction.

21.5.5 Conversions

The Close Corporations Act and the Companies Act 61 of 1973 provide for the conversion of a company to a close corporation, and *vice versa*.

The Companies Act 71 of 2008 provides for the conversion of close corporations that existed at the time that the Act came into operation into companies. As was mentioned above, no new close corporations may be incorporated, so conversion from a company into a close corporation is no longer possible.

21.6 The business trust

21.6.1 Introduction

The business trust is a more recent development in South African commercial law. Public business trusts often invite members of the public to invest money in the trust. In exchange they become members of the trust, but normally they are not involved in its management. The Collective Investment Schemes Control Act 45 of 2002, the Companies Act and other statutory measures apply to trusts which acquire investments from the public. The rest of this discussion is restricted to the private business trust, which largely resembles the partnership, private company and close corporation.

21.6.2 Definition

It is very difficult to define a business trust precisely. Generally, a business trust is a trust where the trustees do not merely protect and manage the trust assets, but use the assets for carrying on a business for profit in order to benefit the trust beneficiary or beneficiaries, or to further the aims of the trust. The private business trust is therefore a trust with a specific aim, namely to run a business with the object of making a profit in order to benefit the trust beneficiary or beneficiaries. (Trusts in general are discussed in chapter 27.)

21.6.3 Requirements

The business trust has not been created by statute, but developed from the ordinary trust. It must therefore comply with the normal requirements for a trust. They are:

(a) The founder of the trust must have the serious intention of creating a trust.
(b) The founder must express his or her intention in such a manner that a binding obligation is created.
(c) The trust assets and trust beneficiaries must be readily ascertainable.
(d) The trust object must be defined with reasonable certainty.
(e) The object of the trust must be lawful.

These requirements are discussed in paragraph 27.4.

In addition, the object of a business trust must be certain, and it must be to run a business with the object of making a profit. This further requirement also distinguishes the business trust from an ordinary trust whose object is the protection and preservation of the trust assets.

The typical structure of a private business trust is that the founders create a trust and appoint themselves as trustees and trust beneficiaries. They manage the trust business jointly and often distribute the trust benefits partly as salaries to themselves.

21.6.4 Specific aspects

Similar to an ordinary trust, the business trust is not a separate legal person. Because the trust itself is unable to perform juristic acts, they are performed on behalf of the trust by a trustee. In the case of a business trust it is therefore possible to leave the management of the enterprise in expert care by means of the selective appointment of a trustee or trustees. The trust document provides the trustees with authority to represent the trust in contracts. If there are two or more trustees, the rule is normally that they shall act jointly.

There is no restriction on the duration of a trust. The continued existence of the trust is thus not affected by any possible change in trustees. The duration of the trust is determined in the trust documents and perpetual existence is therefore not excluded. There is also no restriction on the number of persons who may be beneficiaries of a trust.

Despite the fact that it does not have legal personality, the debts of the trust are normally only payable from the trust estate. A trustee is only liable for trust debts in his or her representative capacity and to the extent of the trust assets. The trust beneficiaries also cannot be held liable for trust debts, since the trustee is the owner of the trust assets. The business trust, as a form of business enterprise, therefore has the benefit of limited liability.

Business trusts enjoy benefits similar to those offered by companies and close corporations, but they are not subject to the regulatory rules which apply to these enterprises. This ensures some flexibility, enabling a trust to be structured in such a way that income tax and estate duty benefits can be derived from this form of enterprise. The income tax scales applicable to the income derived by companies and close corporations do not apply to trust income. Normally the trust itself does not incur tax liability in respect of income received by the trust and distributed to the trust beneficiary, since this income is taxable in the hands of the beneficiary.

A business trust must be created with particular care in order to make use of the possible tax benefits.

Legal and natural persons may be parties to a trust. This offers a distinct advantage over a close corporation, which may generally only have natural persons as members (see paragraph 21.5.2).

The relatively little control over the acts of the trustees is, however, an inherent risk of this form of enterprise. Control by the trust founders and beneficiaries is largely dependent on the provisions of the trust deed and the fiduciary obligation of trustees to act according to their instructions as formulated in the trust deed. The risk can be limited by ensuring that all parties to a trust are also trustees, but even so it remains difficult for a trustee to exercise control over co-trustees.

21.7 The co-operative

21.7.1 Introduction

The co-operative society is a voluntary association that developed from the law of partnership. This form of business enterprise is based on the co-operative values of self-help, self-reliance, self-responsibility, democracy, equality and social responsibility. The Co-operatives Act 14 of 2005 recognises that a viable, autonomous, self-reliant and self-sustaining co-operative movement can play a major role in South Africa's economic and social development, in particular by creating employment, generating income, facilitating broad-based black economic empowerment and eradicating poverty, and that the South African economy will benefit from increasing the number and variety of viable and sustainable economic enterprises. The Act provides a legal framework within which co-operatives can operate. Its objectives are to ensure that international co-operative principles are recognised and implemented in South Africa; to enable co-operatives to register and acquire a legal status separate from their members, and to facilitate the provision of targeted support for emerging co-operatives, particularly those owned by women and black people.

A great variety of co-operatives can be formed. The Co-operatives Act recognises, among others, housing, worker, social, and agricultural co- operatives, co-operative burial societies and financial services co-operatives. Other kinds of co-operatives, not specifically mentioned in the Act, may also be registered.

21.7.2 Definition

A co-operative is defined in the Co-operatives Act as an autonomous association of persons united voluntarily to meet their common economic and social needs and aspirations through a jointly owned and democratically controlled enterprise organised and operated on co-operative principles. These principles entail that membership of that co-operative is open to persons who can use the services of that co-operative and who are able to accept the responsibilities of membership, and that each member of a primary co-operative has only one vote. The members provide the capital required by that co-operative to the extent that this is feasible;

that the return paid on member capital is limited to the maximum percentage fixed in accordance with the constitution of the particular co-operative; that at least five per cent of the surplus is set aside as a reserve in a reserve fund and is not divisible amongst its members; and that the co-operative provides education and training to its members and employees.

The constitution of a co-operative may only restrict the persons eligible for membership if the restriction reasonably relates to the business of a co-operative set out

in its constitution and to the commercial ability of a co-operative to provide services to prospective members, and if the restriction does not constitute unfair discrimination.

21.7.3 Registration

Before applying to register a primary co-operative, a meeting or meetings of interested persons is held. The meeting must adopt a constitution of the proposed co-operative and elect its first directors. Application is then made, by a minimum of five people, to the Registrar of Co-operatives to register a co-operative. The application must contain the constitution of the co-operative, signed by the founder members; a list of the founder members; a list of the directors, and the prescribed fee or proof of its payment. There is no restriction on the maximum number of members that a co-operative may have.

A co-operative must have the words 'co-operative' or 'co-op' as part of its name and the word 'limited' or the abbreviation 'Ltd' as the last word of its name, unless the constitution of the co-operative does not limit the liability of its members. The co-operative's name may not be the same as, or so similar to, that of an existing co-operative that it may be misleading, or a name that is undesirable, prohibited or calculated to deceive, or otherwise mislead. A secondary co-operative (a co-operative formed by two or more primary co-operatives to provide sectoral services to its members) must have the words 'secondary co-operative' as part of its name. A tertiary co-operative (a co-operative whose members are secondary co-operatives and whose object is to advocate and engage organs of state, the private sector and stakeholders on behalf of its members — also referred to as a 'co-operative apex') — must have the words 'tertiary co-operative' as part of its name.

When the Registrar registers the co-operative, a certificate of registration with a registration number is issued. The co-operative is incorporated as a legal person with effect from the date on which it is registered, as reflected on its registration certificate. If the co-operative complies with the co-operative principles and consists of black persons, women, youth, disabled persons or persons in the rural areas and promotes equity and greater participation by its members, the Department of Trade and Industry may provide it with the necessary support.

A co-operative must set out its name in legible characters in all contracts, invoices, negotiable instruments, letters, orders and places of business. It is an offence for any entity other than a co-operative registered in terms of the Act to hold itself out as carrying on the business of a registered co-operative or to use or

authorise the use of the words ‘co-operative’, ‘co-op’, ‘co-operative limited’, ‘co-operative ltd’, or ‘co-op ltd’ as part of its name.

A co-operative must maintain a registered office in the Republic at the place set out in its constitution and must keep certain records there.

A co-operative must hold an annual general meeting and appoint an auditor. An audit of the affairs of a co-operative must be conducted annually in respect of each financial year.

21.7.4 Capital of the enterprise

The capital contributed by members may comprise entrance fees, membership fees or subscriptions, the consideration for membership shares or additional shares in the co-operative, member loans or member funds.

The constitution of a co-operative may provide for a member to hold shares in it. All shares issued must be of the same class and ranking. A member’s liability is limited to an amount equal to the nominal value of the shares that the member holds in the co-operative, and for which the member has not paid. If a co-operative determines that the repayment of shares would adversely affect its financial well-being, the co-operative may direct that the repayment be deferred for a period not exceeding two years after the effective date of the notice of withdrawal. Unless a co-operative determines otherwise, the withdrawal of a member from the co-operative does not release the member from any debt or obligation to the co-operative or any contract between the member and the co-operative.

The constitution of a co-operative may provide for the establishment of one or more members’ funds in which the member of a co-operative may be credited for any purpose permitted in terms of the constitution of a co-operative except for writing off of losses.

A co-operative may give financial assistance by means of a loan or the provision of security to any person in the ordinary course of business if the lending of money is part of the ordinary business of the co-operative; to any person on account of expenditures incurred or to be incurred on behalf of the co-operative; to employees of the co-operative or of any of its members to enable or assist them to purchase or erect living accommodation for their own occupation, or in accordance with a plan for shares of the co-operative or any of its members to be held by a trustee; and to members, if the financial assistance is available to all members on substantially the same terms. But the co-operative may not give such financial assistance directly or indirectly, if there are reasonable grounds to believe that it will, after giving the financial assistance, be unable to pay its liabilities as they become due; or that the realisable value of the co-operative’s assets, after giving the financial assistance, will be less than the aggregate of its liabilities, share capital and reserves.

A co-operative must set up a reserve fund in which the co-operative must deposit at least five per cent of the surplus as a reserve, that is indivisible amongst its members, during a financial year. The reserve is monitored for compliance by the Registrar through the audited annual financial statements.

21.7.5 Representation

A person who enters into a written contract in the name of, or on behalf of, a co-operative before it is registered is personally bound by the contract, unless that contract expressly provides otherwise. The co-operative may, within a month after its registration, ratify the pre-incorporation contract by ordinary resolution (majority vote) at a general meeting. The co-operative is then bound by the contract and the person who originally entered into the contract ceases to be bound by it. If the co-operative does not ratify the

contract, the person who originally entered into it continues to be bound by it, unless the contract expressly provides otherwise.

A co-operative may do all things necessary to carry out its objectives, subject to limitations imposed by its constitution, the Co-operatives Act or any other law. If a co-operative performs any act outside its functions, the co-operative and any director of the co-operative who authorised the performance of that act or who performed that act knowing that the co-operative is not empowered to perform that act is guilty of an offence.

The highest decision-making structure of a co-operative is a general meeting of members. Its affairs are managed by a board of directors consisting of such number of persons as the constitution of the co-operative permits. The board of directors must exercise the powers and perform the duties of the co-operative subject to this Act and the constitution of the co-operative. The board must be elected for such period as may be set out in the constitution of the co-operative, which period may not be more than four years. The board of directors is accountable to the general meeting and, between general meetings, to the supervisory committee if a supervisory committee is provided for in the co-operative's constitution.

21.7.6 Conversion and winding-up

A company that intends to conduct its affairs according to co-operative principles, and that passed a resolution at a general meeting that authorises the conversion of that company into a co-operative of a particular kind and form, may apply to the Registrar to be converted.

A co-operative may be wound up voluntarily by a special resolution of at least 75 per cent of its members. The court may order its winding-up if the co-operative is unable to pay its debts; if there is no reasonable probability that it will be able to pay its debts or become a viable co-operative, or if it appears just and equitable to do so. The Minister may, on the recommendation of the Registrar, order that a co-operative be wound up or de-registered if the Minister has reason to believe that the co-operative obtained registration through fraud; was formed for a particular period or until the occurrence of a particular event and that period has expired or that event has occurred; if it has not transacted business during a continuous period of two years; or if it is not operating in accordance with its constitution or in accordance with the Act.

Further reading

ML Benade, JJ Henning, JJ du Plessis, PA Delport et al *Entrepreneurial Law* special ed incorporating *The New Companies Act Manual* (2009)

PA Delport *The New Companies Act Manual including Close Corporations and Partnerships* (2011)

D Davis, F Cassim et al *Companies and Other Business Structures in South Africa 2 ed* (2011)

JJ Henning & HJ Delport 'Partnership' in WA Joubert (ed) LAWSA vol 19

JTR Gibson *South African Mercantile and Company Law* 8 ed (2003) by Coenraad Visser (gen ed), JT Pretorius, Robert Sharrock & Marlize van Jaarsveld

Chapter 23
Security

23.1 Introduction
23.2 The contract of suretyship
23.3 Real security

23.1 Introduction

In chapter 10 we discussed various remedies that are available to the innocent party where a contract has been breached. These remedies may be used to force the debtor to perform in accordance with the particular type of contract, or to pay damages. It is, however, possible that the estate of the debtor may not be sufficient to enable him or her to perform, or to pay damages fully. The debtor could, for example, incur so many liabilities towards various creditors that his or her assets are not sufficient to settle all of them, or the debtor's liability towards one creditor can be so great that full compliance is impossible (in both instances the debtor's liabilities will, therefore, exceed his or her assets). The estate of the debtor will then be insufficient to settle all the claims of the creditors. The available remedies will, in these circumstances, be of little practical value.

It is for this reason that persons entering into a contract frequently require some form of security to ensure performance of the other party's obligations. This security can be obtained in two ways. The creditor can either obtain the right to have the proceeds of property belonging to the debtor applied to ensure proper compliance with the debtor's obligations to the exclusion of the rights of other creditors (real security), or the creditor may require a third party to bind himself or herself in respect of proper compliance with the debtor's obligations (personal security). The contract of suretyship is discussed below as a type of personal security. Various forms of real security are then considered.

23.2 The contract of suretyship

Personal security is given by granting the creditor the right, in case of non-payment of the principal debt, to secure payment by means of a personal right against another party to carry out the stipulated performance.

23.2.1 Definition

The contract of suretyship is an agreement by means of which one person (the surety) renders himself or herself liable towards a creditor of another person

(the debtor) for the proper compliance of the obligations of the debtor. In such a case there are, therefore, two debtors, namely the debtor in the first agreement (the principal debtor) and the debtor in the contract of surety (the surety). The principal debtor remains liable in terms of his or her agreement with the creditor. The liability of the surety is additional to this. It is an essential characteristic of the contract of suretyship that it is accessory to the principal obligation between the original debtor and creditor.

The issue of surety, therefore, cannot arise if there is no valid principal debt. There may be more than one principal debt. In a so-called 'continuing suretyship', for example, the surety may render him- or herself liable for any debt owed by the principal debtor, or

for the liability of the principal debtor arising from a series of transactions (for example, the sale of goods on a running account).

23.2.2 Conclusion of the contract of suretyship

A contract of suretyship is concluded by agreement between the creditor and the surety. The normal requirements for conclusion of a valid contract have to be met. Therefore, there must be a proper offer and acceptance and the parties must have the intention that the surety will be bound as such. The principal debtor does not have to be a party to the contract of surety and, in fact, does not have to know of its existence.

Any person who has contractual capacity can generally be bound as a surety. However, a minor who has been tacitly emancipated cannot do so without the consent of his or her guardian, and a person married in community of property normally needs the consent of the other spouse.

The General Law Amendment Act 50 of 1956 provides that a contract of suretyship shall be in writing and that the written document shall only be valid if it is also signed by, or on behalf of, the surety. This Act thus requires that the principal debtor, the creditor, the surety and the principal debt be identified in the document. If the contract identifies more than one surety and it is the intention that each of them will only be liable if all the others are also liable, the contract must be signed by all the co-sureties.

Since the liability of the surety is accessory to the original agreement between the creditor and the principal debtor, the surety cannot be liable for more than the principal debt. The surety may render him- or herself liable for less than the principal debt.

23.2.3 The liability of the surety

The consequence of a contract of surety is, naturally, that the surety is obliged to perform the obligation of the principal debtor if the latter fails to do so. Thus, the surety is liable to the creditor for payment by the principal debtor of his or her debt, or for a lesser amount if the surety has only bound him- or herself in respect of such lesser amount. As a result of the accessory nature of the surety's liability, he or she may rely on defects in the liability of the principal debtor, for example, duress and

misrepresentation. But the surety may not rely on mere personal defences such as minority, which may be at the disposal of the principal debtor.

Because the surety's obligation is accessory to the principal debt, it becomes enforceable only if the principal debtor defaults in the performance of the principal obligation. If the principal debtor is granted an extension of time, the surety may not be held liable in the meantime. If the debt is for an unliquidated or uncertain amount, the surety is not liable until the amount of the debt has been established: for example, by judgment, a final balancing of accounts, or otherwise.

If the surety has bound him- or herself for no more than a specified sum, he or she is not, in addition, also liable for interest charged against the debtor. But the nature of the debt, or the terms in which the surety has bound him- or herself, may cause him or her to be liable for interest. The surety is also liable for interest from the time he or she is *in mora*. The interest may not exceed the capital sum.

23.2.4 The rights of the surety

The liability of the surety is alleviated by certain benefits. Since these benefits derive from the common law, the surety will enjoy their protection if they are not expressly excluded.

23.2.4.1 The benefit of excussion

This benefit permits the surety to compel the creditor to recover as much as possible of the due debt from the principal debtor before proceeding against the surety. The surety must raise this defence at the beginning of the proceedings against him or her, otherwise it is forfeited. If the attempt by the creditor against the principal debtor proves unsuccessful, the creditor may recover from the surety (who compelled the creditor to first proceed against the principal debtor) any costs incurred as a consequence of this.

The benefit of excussion is not available to the surety if the surety has renounced it, or has bound him- or herself as surety and co-principal debtor (in this case renunciation is implied); or where excussion is not possible or would serve no purpose (for example, because the principal debtor cannot be found, or has a personal defence against the creditor's claim).

23.2.4.2 The benefit of division

This defence is available where there are several sureties in respect of one and the same obligation, and the creditor attempts to recover the entire debt which is due from a single surety. Such surety is then at liberty to demand that the creditor divide his or her claim between the available sureties, so that his or her (the surety's) liability may be restricted to his or her proportionate share of the principal debt.

This benefit is unavailable to the surety if the surety has renounced it, or has bound him- or herself as surety and co-principal debtor. A surety can, furthermore, not insist that the creditor include in the division a co-surety from whom recovery is impractical or impossible (for example, one who falls outside the jurisdiction of the court, or who is absent or insolvent).

23.2.4.3 The benefit of cession of actions

This privilege allows a surety who has rendered performance of the principal obligation to demand that the creditor transfer all rights which the latter may enjoy against the principal debtor and the co-sureties, if any, to the surety. However, it should be mentioned that even in the absence of a cession of actions, a surety who has settled the principal debt will always enjoy a right of recourse against the principal debtor and co-sureties. Cession of actions to him or her still remains advantageous. In addition to the fact that, because he or she is in the position of the creditor, the co-sureties can be sued;

and the surety will be able to recover any interest, expenses or damages that the creditor could have recovered. Any security held by the creditor, like a pledge, hypothec, or preference over other claims, passes to the surety with cession of actions. And by cession of actions the surety may be placed in a position to recover from a stranger who is liable to the creditor for the debtor's debt, for example, a partner or co-debtor for whom he was not surety.

The surety may refuse to pay the creditor where the latter is unable to effect (bring about) cession, for instance, where the creditor has allowed his or her rights against the principal debtor to be destroyed or diminished.

23.2.4.4 The surety's right of recourse against the principal debtor

A surety who has discharged his or her obligations to the creditor has a right of recourse against the principal debtor for the amount paid, as well as for any costs reasonably incurred. As was stated above, this right arises automatically on payment. Therefore no cession of actions by the creditor is required.

The right of recourse is excluded if the surety carelessly neglected to raise a (non-personal) defence which was available to the debtor, or if, after paying the debt, he or she negligently failed to inform the debtor of payment, with the result that the latter also paid the amount to the creditor.

A surety who has not yet discharged his or her obligation to the creditor may, in certain circumstances, compel the principal debtor to pay the principal debt to obtain his or her (the surety's) release from the contract of suretyship. These situations are:

(a) where the debtor and the creditor have allowed the principal debt to remain undischarged for an unreasonable time
(b) if the debtor is recklessly squandering his or her assets
(c) where the creditor has obtained judgment against the surety.

23.2.4.5 The surety's right to a contribution from co-sureties

Normally there is no contractual relationship between co-sureties. A surety is, however, entitled by operation of law to recover a proportionate contribution from each of the solvent co-sureties if he or she has discharged the principal debt fully. This right is not dependent on any cession by the creditor. It arises even where the co-sureties undertook liability independently or in ignorance of each other. If the

surety has indeed obtained cession of actions from the creditor, he or she enjoys all the rights and privileges of the creditor, and all defences available against the creditor may be used against the surety (the cessionary or person to whom the right has been ceded).

If the surety who settled the debt has been reimbursed in part by the principal debtor, his or her claim against the co-sureties is reduced proportionately. It is uncertain whether a co-surety has a right to a contribution where he has only partially discharged the principal debt. Since the right to a contribution is based on enrichment (the co-sureties are released from their obligations to the creditor by the paying surety's performance and are therefore enriched at the expense of the paying surety), it seems to follow that a surety who has paid more than his or her proportionate part of the debt should have a contribution claim against the co-sureties in respect of that excess amount.

The paying surety has no right to a contribution if he or she negligently failed to raise a defence *in rem* (a non-personal defence) which was available to the debtor. If the surety failed to raise the benefit of excussion when this defence was open to him or her, a contribution cannot be demanded until the surety has excussed the principal debtor.

23.2.4.6 The surety's right to reciprocal counter-performance

The creditor may be contractually bound to render a counter-performance to the principal debtor against performance by the debtor of the principal obligation. On discharging the principal obligation, the surety becomes entitled to claim the reciprocal counter-performance, and to set it off against his or her claim against the principal debtor.

23.2.5 Discharge of the surety

Any variation of the terms of a contract of suretyship has to be in writing. A contract of surety may, however, be terminated orally, except if the contract requires cancellation to be in writing.

The surety is discharged (released) in various circumstances:

23.2.5.1 Termination of the suretyship obligation

The suretyship obligation may be discharged in the same way as obligations generally (for example, by payment of the principal debt, merger, or expiry of an agreed time limit).

In the case of a continuing suretyship, the surety may, unless otherwise provided in the contract, terminate his or her future liability by giving reasonable notice to the creditor.

23.2.5.2 Termination of the principal obligation

It follows from the accessory nature of a contract of suretyship that it is automatically terminated when the principal obligation is terminated. If the liability of the

principal debtor is, for instance, terminated by novation or absolution, the surety is accordingly absolved from liability.

If only a part of the principal obligation is discharged, the surety is only released to that extent.

23.2.5.3 Conduct prejudicial to the surety

The surety is released if he or she is prejudiced by the creditor. Therefore, the surety is discharged if the creditor makes his or her liability more arduous, for example, by being too lenient towards the principal debtor, or by neglecting to take reasonable steps to protect his or her rights against the principal debtor.

Defences available to the principal debtor are also available to the surety, unless those defences are personal to the debtor. It should also be noted that the National Credit Act 34 of 2005 applies, with certain exceptions, to all credit agreements, including credit guarantees, made or having effect in the Republic. The definition of a credit guarantee includes surety. If the obligation secured falls within the Act, the surety may rely on its benefits: for example, suspension of his or her obligations under the contract if the credit guarantee was reckless as defined in the Act. The surety is also released if the creditor, without the surety's consent, agrees to a material variation of the principal obligation, or departs (or permits a departure) from its terms in a material respect. The test of materiality in this context is whether the alteration or departure is prejudicial to the interests of the surety and whether the surety would have agreed to become a surety in the absence of the affected provisions.

Mere delay by the creditor in enforcing his or her rights against the principal debtor does not release the surety. But if the creditor grants an extension of time for payment before the due date, and time is 'of the essence', the extension will constitute a material variation which releases the surety. If a co-surety is released by the creditor, the surety is discharged to the extent that he or she is precluded from recovering a contribution from the co-surety.

23.3 Real security

A creditor may also secure the performance of the debtor's obligations by means of real security. Real security is obtained when, either by agreement with the debtor or by operation of law, the creditor acquires the right to be reimbursed from the proceeds of (movable or immovable) property belonging to the debtor in the event of his or her default. As its name implies, real security affords a creditor a limited real right to the object of the security. This applies even, and especially, where the debtor is insolvent, though in that case certain real securities enjoy preference over others. A creditor may, therefore, obtain complete protection against the potential default of the debtor simply by ensuring that the value of his or her real security is adequate. In this respect real security is a far better kind of security than personal security, which affords a creditor a mere personal right against the surety. If the value of the real security is greater than the amount of the debt secured by it, the surplus which remains after the realisation of the security reverts to the debtor or to

the debtor's estate. It should be noted that, like the personal rights which flow from a contract of suretyship, the real rights which arise as a consequence of the creation of a real security are accessory to the obligation secured. Another characteristic of a real security right is that it does not normally provide entitlements of use and enjoyment to the creditor. Different types of security are used for immovable, movable, or incorporeal property. Five types of real security are discussed below.

23.3.1 Pledge

Movable goods may be delivered, or pledged, as security for a debt. Pledge is constituted by agreement between the pledgor, who undertakes to deliver the article, and the pledgee, and the subsequent delivery of the property in question.

Prior to delivery of possession the pledgee still only has a personal right against the pledgor; the pledgee will not be able to claim the article from a third party who, in the meantime, has obtained a real right to the article in good faith. The pledgee will also not have any preference if a judgment creditor attaches the article pledged, or if the pledgor's estate is sequestrated and there are several creditors. Although the pledge may be valid as between the pledgor and the pledgee, even without the delivery of possession, the pledgee has no real security in the absence of delivery of the thing and its retention. If delivery has not yet taken place, the pledgee may claim delivery from the pledgor, but he or she only obtains a real right when delivery has taken place. Delivery by way of *constitutum possessorium* (where the seller retains possession of the *merx*, but on behalf of the purchaser) is not a valid means of delivery in the case of pledge. The reason is that where the pledgor remains in possession of the object of the pledge, the parties can easily disguise the pledge as a contract of sale. This is prejudicial to the rights of creditors. The pledgee acquires a limited real right to the pledged thing (article). This right enables the pledgee to keep the thing in his or her control until the pledgor has paid the principal debt. If the debt is not paid, the thing pledged can be sold in execution. The creditor obtains judgment against the debtor and has a warrant of execution issued. It is enforced by the sheriff or messenger of the court, who will sell the thing pledged in execution to the highest bidder. The proceeds of the sale are used to satisfy the debt. Any surplus will be paid to the debtor, or to the debtor's estate, after recovery of the costs in respect of the sale. The parties to a pledge may also agree that the article will be sold without intervention by law if the debt is not met. Such an agreement is known as a provision of '*parate eksekusie*'. The pledge remains effective for as long as the creditor retains possession of the property. The creditor's security interest is similar to that of a mortgagee of immovable property (see paragraph 23.3.3 below). The pledgor may not alienate (for example, sell or mortgage) the pledged article and the pledgee has a preferential claim to its proceeds. When the pledgor has paid the debt, the pledge is extinguished and the pledged article may be reclaimed. Pledge is of little commercial use owing to the requirement that the creditor must retain possession of the property.

23.3.2 Notarial bonds

There is another manner in which a creditor can obtain a preference over the movable goods of the debtor: that is, by registration of a notarial bond over the movable property of the debtor. A notarial bond is defined by the Deeds Registries Act 47 of 1937 as a bond attested by a notary public, hypothecating movable property generally or specifically.

A general notarial bond (that is, a bond over property described generally, and not over a specific, identifiable thing) does not confer any real security unless the property subject to the bond has been delivered to the bondholder (in such a case it has, effectively, been pledged). Without delivery, the bondholder only has a preference over the property when the debtor becomes insolvent. But the Security by Means of Movable

Property Act 57 of 1993 provides that if a special notarial bond has been registered over specified corporeal movable property after the commencement of the Act, that property is deemed to have been pledged to the bondholder, despite the fact that it has not actually been delivered to him or her.

The bondholder, therefore, obtains real security by the acquisition of a real right to the bonded property. Any property covered by this type of notarial bond is not subject to the landlord's tacit hypothec (see chapter 14).

The mortgagor under a notarial bond retains the use of the property during the currency of the bond.

23.3.3 Mortgage bonds

A mortgage bond arises by agreement followed by registration. The agreement which gives rise to a mortgage bond is similar to that which gives rise to a pledge, except that, whereas the subject-matter of a pledge is movable property, that of a mortgage bond is immovable property. The mortgagor corresponds to the pledgor, and the mortgagee to the pledgee.

The Deeds Registries Act 47 of 1937 defines a mortgage bond as 'a bond attested by the Registrar of Deeds specially hypothecating immovable property'. It affords the only means by which real security over immovable property can be created, other than by operation of law. Registration by the Registrar of Deeds is in accordance with the normal requirements for the transfer of real rights in immovable property. Registration is an essential prerequisite for the existence of any mortgage bond. Once a mortgage bond has been registered in respect of a particular immovable property, the Registrar of Deeds is precluded from attesting or executing a transfer of that property until the bond has been cancelled, or the property has been released from the operation of the bond by the written consent of the mortgagee.

Generally, any immovable asset capable of being private property, whether corporeal or incorporeal, may be mortgaged, provided it does not belong to the mortgagee. Examples are a sectional title unit, an erf (with or without a building on it), a farm, a share in land, and a limited real right in land which is capable of being dealt with separately from the land (for example, a registered long lease).

More than one real right may exist in respect of the same immovable property. For example, if a mortgage bond has already been registered over a farm, a further mortgage bond or servitude may be registered over the same property. The consent of the first bondholder is not required, unless it is a condition of the bond that no further bond will be registered without such consent. If more than one bond is registered over the same property, the bonds rank in preference in the order of their dates of execution. Therefore, the older bond enjoys preference. If the second bondholder wishes to sell the property in execution, the first bondholder may therefore place a reserve price on it. The first bondholder also enjoys preference in respect of the proceeds of the farm. An earlier bondholder may, however, waive preference in favour of another bondholder.

The bondholder whose mortgage bond is registered after other real rights have already been established in respect of the property obtains a weaker right than that of the persons who obtained the real rights, unless they have renounced their rights in favour of the bondholder.

Like the mortgagor under a notarial bond, the mortgagor remains the owner of the property and consequently remains entitled to its use and enjoyment. Unlike other holders of limited real rights in property (for example, the holder of a servitude), a mortgagee is not entitled to use of the property. The mortgagor may not, however, do anything to diminish the value of the property and bond conditions usually contain provisions that restrict the mortgagor's right to use the property.

A mortgage bond may secure an existing or a future debt, or a combination of the two. Where it secures either a future debt, or a combination of a future and an existing debt (for example, a debt in respect of goods to be purchased on credit from time to time), it is known as a 'covering bond'. A '*kustingsbrief*' is a special mortgage bond which is registered simultaneously with transfer of ownership of land, in favour of the seller or a third party, and as security for the outstanding balance of the purchase price. A bond passed by the debtor to secure an obligation for which security has already been given by the debtor is known as a 'collateral bond'. The initial security can, but need not, also be a mortgage bond. The Collective Investment Schemes Control Act 45 of 2002 provides for collective investment schemes in participation bonds. These bonds come into being when a number of investors invest in an investment company which grants loans against registration of a mortgage bond over specific immovable property. After registration, the various investors receive letters of participation confirming that the amount of their investment is secured by the bond. If the bond complies with the Act, each investor acquires a real right in respect of the bonded property.

The execution steps which are taken in the event of non-compliance with the debt are the same as were discussed above under pledge. The mortgagee has the right to execute immediately against the mortgaged property, and does not first have to levy execution against the debtor's movable assets (in accordance with the normal rules). But the mortgagee must first sue and obtain judgment against the mortgagor, and thereafter must have the property sold in execution in accordance with the normal formal procedure. '*Parate eksekusie*' is not permitted by law where a mortgage bond has been registered over immovable property.

Section 26 of the Constitution entrenches the right of access to adequate housing. Recent court decisions have indicated that this provision will only prevent a mortgagee from selling immovable property in execution in limited circumstances. The amount due is one of the factors that will be considered. Special rules apply in respect of the mortgage of South African ships. They cannot be mortgaged as security for a debt by a bond registered in a Deeds Registry, but are mortgaged by the registration in the South African Ships Register of a mortgage instrument by the Registrar of Ships in terms of the Ship Registration Act 58 of 1998. The mortgagee under a registered mortgage is entitled

to recover the amount due under the mortgage in any court that has jurisdiction. The court may direct that the ship, or share in the ship, be sold in execution of the judgment. A term of '*parate eksekusie*' is, however, invalid and the mortgagee may therefore not sell the ship simply by virtue of the mortgage.

Because the mortgagor's security obligation is accessory to the principal obligation, it falls away once the principal obligation is discharged. The mortgagee cannot retain the mortgage as security for another debt incurred by the mortgagor while the mortgage is in force.

23.3.4 Liens and hypothecs

23.3.4.1 Liens

A lien is a right to retain the possession of property (a right of retention). The possessor of someone else's property who has expended money or labour on that property acquires the right to retain it in his or her possession until he or she has been compensated according to agreement, if there was one, or, if there was no agreement, until compensation has been made for the actual expenses or the increase in value of the property (whichever is the lesser). All liens arise by operation of law and not as the consequence of agreement between the parties.

The person claiming the lien must be in possession of the property which is the object of the lien. If possession is lost the lien automatically also lapses. The lien does not revive if possession of the property is recovered. But if physical control of the object of the lien was lost as a result of force, fraud or any other unlawful action, it is revived as soon as effective control is recovered. A lien can also be revived after it has been lost, provided that the control was lost in terms of an agreement and was regained afterwards in terms of the same agreement.

There are three types of lien:

(a) liens for the storage or salvage of property (salvage liens)
(b) liens for the improvement of property (improvement liens)
(c) liens for contractual debt (debtor and creditor liens).

A lien for contractual debt is encountered where, in terms of a contract, the creditor has done work to the property of the debtor, which property is still in possession of the creditor. This type of lien is effective only against the debtor himself, and therefore does not give a real security. If, for example, Arthur leaves his motor car to be repaired at Bob's garage, Bob has a lien over the motor car until Arthur has

paid in full for the repairs. Should it transpire that Dorothy is actually the owner of the vehicle, Dorothy is entitled to claim it from Bob with the *rei vindicatio* (the action with which the owner claims possession). If the true owner (Dorothy in the example) is, therefore, someone other than the debtor (Arthur), the creditor (Bob) may not rely against such true owner (Dorothy), on a defence which he would have been able to raise against the *rei vindicatio* of the debtor (Arthur), were Arthur indeed the true owner.

Both salvage liens and improvement liens are enrichment liens. Such liens, in contrast to liens for contractual debt, are enforceable against any person and not only against a contracting party. This leads to the question whether Bob in the above example would not also have had a lien against Dorothy. The current legal position seems to be as follows:

(a) In respect of any expense which is either necessary or useful, a contracting party has an enrichment lien enforceable against any person to the extent of the enrichment, as well as a debtor-and-creditor lien against the debtor for the full amount of the contract price: an enrichment lien and a debtor-and-creditor lien can therefore overlap completely or partially.

(b) In respect of luxurious expenses a party to a contract can only obtain a debtor-and-creditor lien.

Certain liens originate from statute. It is not always possible to categorise them as either enrichment or debtor-and-creditor liens. The extent of these liens must be determined with reference to the Acts which establish them. Examples are maritime liens in terms of the Merchant Shipping Act 57 of 1951, the enforcement of which is subject to the Admiralty Jurisdiction Regulation Act 105 of 1983, and liens over goods retained under the Customs and Excise Act 91 of 1964.

23.3.4.2 Hypothecs

Like liens, hypothecs are a form of real security which arise by operation of law and not as a consequence of agreement between the parties. But unlike liens, possession is not a prerequisite for a hypothec.

The two main kinds of hypothec are the landlord's tacit hypothec (which is discussed in chapter 14, under the contract of lease) and the statutory hypothec which accrues to the seller under an instalment agreement (as described in the National Credit Act 34 of 2005, which is discussed in chapter 16) in respect of the object of the sale upon the purchaser's insolvency.

23.3.5 Cession to secure a debt

Cession to secure a debt (cession *in securitatem debiti*) is encountered where cession of a personal right (for example, a right in respect of shares, or a right to payment in terms of an insurance policy) is effected as security for a debt. This would be the situation, for example, where creditor Vusi who has a personal right against debtor Molapho applies his personal right against Molapho as security for his own debt against his creditor, Nonzizwe, by ceding his personal right

against Molapho in security of his (Vusi's) debt to Nonzizwe. Nonzizwe now not only has her original personal right against Vusi, but also a personal right against Molapho should Vusi fail to honour his obligations to her. It is usually the intention of the parties that the right ceded by means of the cession *in securitatem debiti* will be ceded back to the cedent (in this case, Vusi) by the cessionary (in this case, Nonzizwe) when the cedent's debt to the cessionary has been discharged. While the cession exists, the cedent has no claim against the debtor (in this case, Molapho). The cedent is, however, entitled to a reverse cession by the cessionary when the secured debt is paid, or, alternatively, where

the proceeds of the personal right ceded have exceeded the amount necessary for discharge of the debt secured, the cedent is entitled to the balance.

Cession to secure a debt can also be constituted by means of the 'pledge' of a personal right. It will depend upon the intention of the parties whether one is dealing with a 'pledge' or with an out-and-out cession of a personal right to secure a debt. Where the cession to secure a debt is effected through out-and-out cession, coupled with the intention that the cedent will be entitled to reverse cession if the debt is discharged, the ceded right becomes part of the cessionary's estate. Where the cession has been effected through pledge, the ceded right remains part of the estate of the cedent-pledgor. This distinction is of importance if one of or both the parties (that is, the cedent or the 'pledgor' on the one hand, or the cessionary or the 'pledgee', on the other hand) become insolvent.

Whether a personal right may indeed be 'pledged' has been doubted for a long time, since it is a type of security which (as was indicated above) pertains to movable things. However, the Supreme Court of Appeal has decided that personal rights can indeed be 'pledged'. In this case, the right of 'pledge' simply lapses when the secured debt is settled. No reverse cession therefore takes place in order again to render the 'pledgor' fully entitled to the 'pledged' personal right. An out-and-out cession of a personal right to secure a debt, however, still remains possible.

Further reading

CF Forsyth & JT Pretorius *Caney's The Law of Suretyship 6* ed (2010)

JTR Gibson *South African Mercantile & Company Law* 8 ed by Coenraad Visser (gen ed), JT Pretorius, Robert Sharrock & Marlize van Jaarsveld (2003)

TJ Scott & S Scott Wille's Law of Mortgage and Pledge in South Africa 3 ed (1987)

Chapter 24
Banking Law: Selected Topics

24.1 Introduction
24.2 Conclusion

24.1 Introduction

Banks play an important part in the functioning of the economy by performing various roles, including that of payment and loan intermediary.

The private banking sector in South Africa is presently divided between commercial banks (regulated by the Banks Act 94 of 1990), mutual banks (regulated by the Mutual Banks Act 124 of 1993) and co-operative banks (regulated by the Co-operative Banks Act 40 of 2007).

Since the banking activities of commercial banks are more diversified than those of mutual banks, and since mutual banks account for only a relatively small portion of the market, in chapters 24, 25 and 26 we will restrict ourselves to a discussion of some aspects and methods of payment relevant to the relationship between commercial banks and their customers.

The traditional role of banks has been that of loan intermediary: the bringing together of borrowers and lenders. Persons and institutions having surplus funds at their disposal deposit or invest such funds with banks. Banks, in turn, lend these funds to entrepreneurs, who use them to launch new businesses or develop existing ones, and to consumers who use the funds for personal spending. Money is thus channeled from sectors where it would otherwise have accumulated without being used, to sectors where it can be put to productive use. This, in turn, ensures a healthy circulation of money.

Banking law is that part of our law that regulates the registration, operation and day-to-day activities of banks. It also regulates the relationship between the bank and its customers.

Strictly speaking, banking law is not an autonomous branch of the law, but rather an application of concepts of the general law of obligations (contract and delict) as well as the law of things. Banking law includes a wide range of topics relevant to the bank-customer relationship. We will briefly discuss three of these topics in chapter 24:

- the bank–customer relationship (see paragraph 24.1.1);
- the South African Code of Banking Practice (see paragraph 24.1.2); and
- the bank's duty of confidentiality and secrecy and the effect of money-laundering legislation on this duty (see paragraph 24.1.3).

Banks offer a wide range of services to their customers. The capacities in which a bank renders services to its customers are diverse and include that of depositary (for example, safe-keeping of valuable items); borrower (for example, when the bank accepts money on fixed deposit); collection agent (for example, collection of cheques); lender and financier (for example, by providing overdraft facilities); guarantor (for example, in sale of land agreements); miscellaneous services (for example, buying and selling of shares and administration of estates); and most importantly for present purposes, payment

intermediary (for example, to make payment on cheques, letters of credit and credit cards, and to comply with instructions regarding the electronic transfer of funds).

Chapters 25 and 26 will be devoted to the legal principles underlying the bank's functions as a payment intermediary. In chapter 25 we will deal with the legal principles underlying cheques. In chapter 26 we will discuss a number of paying instruments and paying methods other than cheques.

24.1.1 The bank-customer relationship

The bank-customer relationship is a multi-faceted relationship. It invariably involves various types of contract, for example, mandate, loan for use, *depositum* and deposit-taking.

The relationship between a bank and its customer arises from contract. It is generally accepted that the contractual relationship between a bank and its customer underlying the operation of a current account is that of creditor and debtor. The most common example of a current account is a cheque account.

In a recent decision it was ruled that a bank has a choice in deciding whom it wants as a client. It was further ruled that a bank may terminate the contract between it and its client unilaterally (that is, by merely giving notice of the cancellation to the client).

The parties to the bank-customer relationship may, depending on the circumstances, fulfil the role of either debtor or creditor. For example, if a customer deposits money in his or her savings account, the customer is the lender and the bank is the borrower. But if the same customer applies for an overdraft on a current account, the roles are reversed and the bank would be the lender and the customer the borrower. This phenomenon results in a multi-faceted relationship between bank and customer, which involves various potentially competing legal principles.

The contract founding the relationship between a bank and its customer is in essence one of mandate. In terms of this contract of mandate, the customer lends money to the bank on current account, and the bank undertakes to repay it on demand by honouring cheques drawn on it, and to perform certain other services for the customer, such as the collection of cheques, the payment of stop and debit orders, and the keeping and maintaining of the customer's accounts with the bank.

However, the relationship between a bank and its customer often involves other types of contract as well, such as loan for consumption and *depositum*.

In terms of a loan for consumption, the customer deposits money in his or her savings account with the bank and the latter is then entitled to use the money so deposited and later repay the same amount, with or without interest, to the customer. The bank is not obliged to return the same money (that is, the same bank notes and coins deposited with it, if the deposit was made in cash) to the customer.

Depositum is a contract in terms of which one person, the depositor (for example, the customer of a bank), delivers an object to another, the depositary (for example, the bank), which keeps it in its custody without using it and with the obligation to return the same object to the depositor. In the past, banks often acted as depositary when customers handed in valuable possessions (for example, jewellery) for the bank to keep on behalf of the customer in the bank's iron safe. Nowadays, banks usually rent out safety-deposit boxes to customers to store their valuables in and the contract is then one of lease, and not deposit.

Because of the complexity of the relationship between a bank and its customer, the underlying contract has often been called a contract *sui generis* (one of a kind). Perhaps it is safer to say that the banker-customer relationship is a multi-faceted one that may be founded on various contracts. These different contracts should each be dealt with on its own terms, rather than trying to label the relationship as a single type of contract.

For present purposes it is important to keep in mind that the contract between a bank and its customer is not a special type of contract that should be regulated by special rules which, as some would have us believe, are to be found only in English textbooks and reported cases. The contract between a bank and its customer is simply another type of contract and should be governed by the ordinary principles of the South African law of contract. All the contracts referred to earlier, which may underlie the relationship between the bank and its customer, have their roots in Roman law and Roman-Dutch law, and through these contracts, the common law continues to have a real influence on modern South African banking law.

The regulation of banks and their activities, as well as the supervision of bank activities, is governed by the Banks Act 94 of 1990. The Banks Act provides which activities qualify as 'deposit-taking' and the 'business of a bank' and, as a result, whether an institution which performs these activities has to register as a bank with the Registrar of Banks. Generally, the Banks Act does not regulate the bank-customer relationship. The bank-customer relationship is governed by the common-law principles of the law of contract, delict and the law of things, the express or tacit terms of the parties' contract, and the provisions of a number of Acts.

Advice or intermediary services, banking services and related financial services rendered by banks are regulated by the Financial Advisory and Intermediary Services Act ('FAIS') 37 of 2002, but are excluded from the ambit of the Consumer Protection Act.

24.1.2 The South African Code of Banking Practice

24.1.2.1 General

The Financial Services Ombud Schemes Act 37 of 2004 deals with consumer complaints pertaining to financial services providers. The Banking Ombudsman is a voluntary scheme among banks in terms of the Financial Services Ombud Schemes Act. The Banking Ombudsman (or, to use the official wording, 'the Ombudsman for Banking Services') has jurisdiction to deal with matters arising from the National Credit Act (see again chapter 16). Any bank which is a member of the Banking Association of South Africa is bound by the provisions of this statute.

The scope of the activities of the Banking Ombudsman is contained in the *South African Code of Banking Practice* ('the Code') as well as the *Banking Ombudsman's Terms*

of Reference. The *Banking Code* first came into operation on 3 April 2000. The Ombudsman for Banking Services mediates on disputes between banks and their customers. Central to the mediating functions of the Ombudsman is the Code of Banking Practice ('the Code').

The Code sets out the minimum standards for service and conduct a customer can expect from his or her bank with regard to the services and products it offers, and how the banks would like to relate to their customers. The Code only applies to personal and small business customers.

The current version of the Code came into operation on 1 January 2012. Earlier versions of the Code provided guidelines as to its application and interpretation. These versions of the Code provided expressly that none of its provisions 'will give rise to a trade custom or tacit contract or otherwise between a customer and the bank'.

Suffice it to mention for present purposes that the current version of the Code no longer attempts to prevent its terms from possibly attaining the status of a banking practice or trade usage. Subscribing banks expressly consent to the provisions of the Code, including those which create so-called 'entitlements' and 'responsibilities' for banks and their customers, respectively. Apart from the fact that the provisions of the Code are expressly consented to by banks and their customers, it would also be possible to argue that the provisions of the Code may qualify as banking practices or trade usages, provided, of course, that these provisions comply with all the common-law requirements for a banking practice or trade usage to be acknowledged as such.

It has also been argued, correctly, that because subscribing banks advertise the fact that they adhere to the Code and make it available to their customers, its provisions could be treated as implied terms in the contract between the bank and its customer.

Because the Code is amended on a regular basis, banks or their customers may argue that the practices, entitlements and responsibilities described in the Code will not be long-established and will therefore not qualify as trade usages. But the fact that a trade usage is not yet long-established should not prevent it from being classified as such, especially in a fast-developing trade such as banking.

24.1.2.2 The Office of the Banking Ombudsman

The purpose of the Ombudsman for Banking Services is to provide customers of member banks with a dispute resolution mechanism which is easily accessible, informal, quick, affordable and effective, without detracting from the customer's right to resort to litigation at any time if he or she wants to do so.

24.1.2.3 The Code of Banking Practice

The Code has been developed to promote good banking practices by setting minimum standards for banks when dealing with their customers. It further aims to promote transparency and a fair and open relationship between banks and their clients.

The Code was originally developed to address public concerns about the banking sector. The Code formalised standards of disclosure, conduct and fairness which are a valuable safeguard for South African bank customers.

Revised in 2008, the Code took into account the banks' commitment to provide easy access to credit in terms of the Financial Sector Charter and the minimum legal requirements for an efficient and responsible credit industry in accordance with the National Credit Act 34 of 2005 ('NCA').

The 2012 revised version of the Code takes into account the Consumer Protection Act 68 of 2008 ('CPA') and addresses the recommendations made by the 2008 Competition Commission's Banking Enquiry (the Jali enquiry). The Code supplements the regulatory and contractual requirements that govern relationships between banks and their customers by committing banks to providing better service. The 2012 version of the Code of Banking Practice introduces essential elements of consumer education and information by explaining the consumer rights and obligations in a way that is clear, fair, reasonable and not misleading. The 2012 version of the Code is a lengthy document and provides for a number of aspects germane to the bank-client relationship.

What follows below is a very brief summary of some of the provisions contained in the Code.

24.1.2.3.1 Customers' entitlements

The Code provides that a customer of a bank is entitled to expect the bank to, inter alia —

- act fairly, reasonably and ethically towards him or her
- provide him or her with effective and adequate disclosure of information, including the terms and conditions of products and services
- provide information in a plain and understandable language
- provide the customer with at least 20 business days' (or five business days in the case of credit agreements) notice before the implementation of changes in terms and conditions, fees and charges, the discontinuation of products and/or services and the relocation of premises

- acknowledge a formal complaint within three business days and investigate it within a reasonable time
- not use the customer's information for marketing and promotional purposes when the client has opted out of receiving marketing information
- not close the customer's account without reasonable prior notice given to the customer at his or her last known address
- provide the customer with the details of the Ombudsman for Banking Services if he or she is not satisfied with the resolution of a dispute.

24.1.2.3.2 Customers' responsibilities

The Code expects the customers to, inter alia —

- disclose all relevant information as part of any credit application to the bank so that the bank can make an informed decision as to granting credit to a customer
- not extend themselves beyond their financial means
- obtain credit insurance where necessary
- acquaint themselves with the general and specific terms and conditions of banking products (for example, accounts, cards)
- protect bank cards and PINs and not disclose their PIN or other unique means of personal identification to anyone.

24.1.2.3.3 Principles of conduct

In terms of the Code, banks undertake to treat the customer's personal information as private and confidential and, as a general rule, they will not disclose any personal information about the customer or his or her account, save under the following circumstances:

- when the bank is compelled by law to disclose the information
- when the bank has a legal duty to the public to disclose the information
- when the bank has to protect their interests by disclosing the information, for example, to prevent fraud
- when the customer has requested the bank or consented to disclosure of personal information
- when the customer's account is in default and he or she has failed to make satisfactory arrangements with the bank for the repayment of the debt (see also paragraph 24.1.3.1, where the common-law origin of these first four exceptions is explained)
- when the customer's cheque has been 'referred to drawer', in which case the information may be placed on a cheque verification service.

The Code further provides detailed guidelines regarding the use of a customer's personal information for purposes of marketing and advertising of the bank's products to the client. Suffice it to say that a customer has the right to choose not to receive any advertising or promotional material from his or her bank.

The Code contains strict guidelines as to the circumstances under which a bank may offer credit to its customers, including that the bank may not offer credit to a customer who the bank knows cannot afford the credit.

The Code also provides detailed provisions regarding promotions; loyalty and reward programmes; credit insurance; terms and conditions of the bank's products; charges and fees; interest rates, and copies of documents which the customer is entitled to receive.

24.1.2.3.4 Accounts

The Code explains in some detail the rights and obligations of both bank and customer in the opening of bank accounts and switching of accounts from one bank to another.

The Code further obliges banks to provide their clients with information regarding the banks' right of set-off that the latter may claim over credit and debit balances in the customer's accounts. (See paragraph 12.7 above with regard to set-off).

Customers are advised to protect their passwords and PINs and are also obliged to take care of their cheque books; savings account books; bank cards; electronic purses and other documents or devices which may result in unauthorised access to their accounts. The Code provides detailed instructions as to what a customer must do in the event of loss or theft of an account book, password, PIN or other document or device. It also explains which party bears the responsibility of loss caused by the loss or theft of any of these.

24.1.2.3.5 Credit

Section 8 of the Code confirms the rights and protection afforded to consumers by the NCA. These include the right to responsible extension of credit by the bank to its client, in a way that matches the client's borrowing requirements and financial capability (see further chapter 16).

24.1.2.3.6 Payment services

Section 9 of the Code deals with the rights and protection afforded to the customer of a bank with regard to the opening of cheque accounts; the buying of foreign exchange; internet, telephone and cell phone banking; and debit orders.

Suffice it to mention here that the Code ensures the reliable operation of the debit order system, the prevention of unauthorised debit orders and the reliable stopping of debit orders where the customer has instructed the bank to stop the payment of a debit order.

24.1.3 A bank's duty of confidentiality and secrecy

24.1.3.1 Introduction

A bank owes its customer a duty to maintain confidentiality and secrecy about the latter's affairs. In many overseas jurisdictions a statute entrenches the banker's

duty of confidentiality and secrecy. This duty is acknowledged in South African law, and has been amplified in the *Code of Banking Practice* (see again paragraph 24.1.2.3.3).

In South Africa, the duty of confidentiality is a *naturale* of the contract between a bank and its customer (that is, the law regards it as part and parcel of the contract). In this regard it has been held that the duty is a tacit or implied term of the contract between a banker and its customer. In a recent South African case the court held that the right of confidentiality rests with the client and that the bank cannot enforce that right on behalf of a client against a third party who wishes to publish confidential information about the client's bank affairs.

In a much-cited English decision (the *Tournier* case), the court not only recognised the existence of the duty, but also listed a number of exceptions to the rule. In certain circumstances the bank is relieved of its duty of confidentiality and secrecy and either has a duty or is allowed to disclose information about the affairs of its customer. The court classified these exceptions under four heads:

(a) where disclosure is under compulsion by law
(b) where there is a duty to the public to disclose
(c) where the interests of the bank require disclosure, or
(d) where the disclosure is made with the express or implied consent of the customer.

Examples of the first exception will be discussed in paragraph 24.1.3.2. The second exception comprises those cases where danger to the state or a public duty may supersede the duty of confidentiality which rests on a bank.

The third exception usually involves cases where a bank sues a customer for the amount of his or her overdraft and where the amount of the overdraft has to be stated in the court documents.

The fourth exception comprises those cases where a customer authorises the bank to give a reference to a third party, for example, where the customer applies for credit facilities with the third party. In a recent case the facts were that the agreement between the bank and its client provided that the bank would be entitled to provide information about the client's bank affairs to a credit bureau. The court held that such an agreement envisaged specific and individualised requests for information by the credit bureau and that the bank was not entitled to provide routinely and proactively information about its clients' affairs to the credit bureau.

24.1.3.2 Disclosure of confidential information by banks under compulsion of law

In the recent past a number of South African statutory provisions have come into operation which may intrude upon the banker's duty of confidentiality towards its customer. Many of these provisions aim at curbing money-laundering activities. They create various obligations for banks and other financial institutions to monitor the activities of their clients and to report suspicious transactions to the authorities. Some of these provisions and their ramifications for banking confidentiality will be

discussed below. From the discussion it will be clear that serious inroads have been made into South African banking confidentially, particularly by money-laundering legislation and with regard to the compulsion-of-law exception.

24.1.3.2.1 The Prevention of Organised Crime Act 121 of 1998 and regulations 47 and 48 of the Banks Act 94 of 1990

The first statute relevant for the present discussion is the Prevention of Organised Crime Act 121 of 1998 ('POCA'). POCA repealed the Proceeds of Crime Act 76 of 1996 and also repealed the money-laundering provisions of the Drugs and Drug Trafficking Act 140 of 1992.

Money-laundering is the process through which illegal money (for example, money obtained through smuggling or gangsterism) is 'washed'. This 'washing' is done by circulating the illegal money through formal systems (for example, bank accounts) in order to conceal the blemished nature and criminal origin of the money.

POCA now contains most of the South African legislative provisions dealing *specifically* with money-laundering. POCA aims at curbing racketeering, gangsterism and money-laundering and it also provides for confiscation orders and civil forfeiture.

24.1.3.2.2 The National Prosecuting Authority Act 32 of 1998

A second provision that may infringe on the bank's duty of confidentiality and secrecy is contained in section 28(6) of the National Prosecuting Authority Act 32 of 1998 ('NPAA'). The NPAA provides for the establishment of a single prosecuting authority in South Africa and for the appointment of Prosecuting and Investigating Directors, as well as of prosecutors.

Section 28(1) of the NPAA provides that if the Investigating Director has reason to suspect that a specified offence has been, or is being, committed or that an attempt has been made to commit an offence, he or she may hold an enquiry.

Section 28(6)*(a)* of the NPPA provides that the Investigating Director may, for purposes of an inquiry in terms of section 28(1), summon *any person* who is believed to be able to furnish any information on the subject of the inquiry to appear before and to be questioned by the Director. The Director may also summon *any person* who is believed to have any book, document or other object relating to the subject of inquiry to be questioned or to produce such book, document or object. Section 28(6)*(b)* allows the Director to question a person designated by him or her in terms of section 28(6)*(a)* under oath or affirmation.

It would appear that the phrase 'any person' in section 28(6) includes banks.

24.1.3.2.3 The Promotion of Access to Information Act 2 of 2000

Reference must also be made to the provisions of the Promotion of Access to Information Act 2 of 2000 ('PAIA'). The aim of PAIA is to give effect to the constitutional right of access to any information held by the state and any

information that is held by another person and that is required for the exercise or protection of any rights.

Section 64(1) of PAIA limits access to certain information. It provides that the head of a private body, such as a bank, must refuse a request for access to a record of the body, for example, the financial affairs of a customer of the bank, if the record contains, among other matters, financial or commercial information concerning a customer, the disclosure of which would be likely to cause harm to the commercial or financial interests of that customer. Section 65 of PAIA provides that the head of a private body, for example, a bank, must refuse a request for access to a record of the body if its disclosure would

constitute an action for breach of a duty of confidence owed to a third party in terms of an agreement, for example, the contract between a bank and its customer.

Sections 64 and 65 of PAIA confirm the common-law duty of confidentiality and secrecy which rests on certain parties, such as banks, that have a contractual relationship with others, such as their customers.

Because PAIA provides for access to information held by the state or any other person where that information is required for the exercise or protection of any rights, an Investigating Director, or any other state official in his or her official capacity, will not be able to rely on the provisions of PAIA to obtain information for purposes of an investigation under section 28 of the NPAA. Clearly the provisions of PAIA aim at giving subjects of the state access to information held either by the state or by other subjects of the state. PAIA does not envisage access to information by the state or one of its organs in terms of that Act. The provisions contained in sections 64 and 65 of PAIA, which aim at the protection of confidential information, are therefore of little if any relevance in defining the parameters of section 28(6) of the NPAA.

24.1.3.2.4 The Financial Intelligence Centre Act ('FICA') 38 of 2001

FICA, together with POCA, forms the backbone of South African money-laundering legislation. FICA encompasses various established anti-money-laundering measures, the most important of which, for purposes of the present discussion, is the implementation of the internationally recognised 'Know-Your-Customer' standard ('the KYC standard'). In its simplest form the KYC standard requires banks to become acquainted with the identity of their clients and the nature of their clients' businesses and to retain records to this effect.

The main objectives of FICA are the following:

(a) to establish a financial intelligence centre and a money-laundering advisory council to assist with the anti-money-laundering effort; and
(b) to impose specific KYC standard obligations on banks.

In general, FICA complements POCA through the introduction of administrative measures to deter and prevent money-laundering and the financing of terrorist-related activities. FICA imposes various obligations on designated persons (including banks) aimed at identifying and reporting money-laundering activities.

FICA provides a lengthy list of so-called 'accountable institutions' which could be used for money-laundering purposes. This list includes —

(a) attorneys
(b) boards of executors or a trust company
(c) estate agents
(d) financial instrument traders
(e) management companies of unit trusts
(f) mutual trusts
(g) long-term insurance businesses
(h) persons dealing in foreign exchange
(i) banks
(j) persons rendering investment advice, including accountants
(k) persons who issue, sell or redeem travellers' cheques, money orders or similar instruments
(l) the Postbank
(m) members of the stock exchange.

FICA imposes four obligations on financial institutions:

(a) to identify clients
(b) to keep records of transactions
(c) to report suspicious transactions to the Financial Intelligence Centre
(d) to train employees to comply with FICA provisions.

The obligation to identify clients involves, among other things, creating internal account-opening identification procedures to ensure that the client (who, for example, wants to open an account with a bank) and its business are who and what they purport to be. Suffice it to mention here that where the prospective client is a South African citizen, the financial institution will have to verify certain basic information relating to the client and the client's tax number and residential address.

24.1.3.2.5 The Regulation of Interception of Communications and Provision of Communication-Related Information Act ('RICA')

With the advent of mobile banking, that is, bank services offered by cellular companies to their clients, another Act that impinges upon the duty of confidentiality is the Regulation of Interception of Communications and Provision of Communication-related Information Act 70 of 2002 ('RICA'). (For more on mobile banking, see paragraph 26.7.7.5.)

24.2 Conclusion

From the discussion in paragraph 24.1.3 it is clear that serious inroads have been made into South African banking confidentiality, particularly by money-laundering legislation and with regard to the compulsion-of-law exception.

This concludes the discussion of some of the legal principles underlying the bank-customer relationship. In chapters 25 and 26 we will focus on one specific aspect of the bank-customer relationship, namely, the role of banks as payment intermediaries on behalf of their customers.

Further reading

Malan on Bills of Exchange, Cheques and Promissory Notes in South African Law 5 ed by FR Malan, JT Pretorius & SF du Toit (2009)

FR Malan, AN Oelofse & JT Pretorius *South African Banking Legislation* vol I & II (loose-leaf edition)

N J Melville *The Banking Adjudicator's Handbook* (2001)

C Pillay *The Ombudsman for Banking Services Handbook* (2013)
www.banking.org.za (The Banking Association of South Africa)
www.obssa.co.za (The Ombudsman for Banking Services)

Chapter 30
Consumer Protection

30.1 Introduction
30.2 The Consumer Protection Act 68 of 2008

30.1 Introduction

The Consumer Protection Act 68 of 2008 lays the foundation for a consumer era in South Africa by introducing a single comprehensive legal framework for consumer protection. It is the first legislation of this kind in South Africa and it therefore has far-reaching consequences. The Act spells out the rights of consumers and the obligations and responsibilities of suppliers, and codifies parts of the common law in relation to consumer rights. The codification of consumer protection law was long overdue, since existing provisions on consumer protection were outdated and fragmented. The Act fulfils the need for a comprehensive consumer policy to promote the economic welfare of all citizens and to provide a coherent and consistent framework and authority to regulate consumer-business interaction.

30.2 The Consumer Protection Act 68 of 2008

30.2.1 Purpose and structure of the Act

The purpose of the Act is, through various means, to promote and advance the social and economic welfare of South African consumers.

The Act consists of seven chapters and 122 sections. Chapter 1 deals with the interpretation, purpose and application of the Act. Chapter 2, the most important chapter, introduces eight fundamental consumer rights. Chapter 3 deals with the protection of these fundamental rights and the consumer's voice. Chapter 4 deals with business names and industry codes of conduct. Chapter 5 deals with the national consumer protection institutions. Chapter 6 deals with the enforcement of the Act and Chapter 7 deals with general provisions.

The eight rights that the Act introduces are:
(a) the right to equality in the consumer market
(b) the right to confidentiality and privacy
(c) the right to choose
(d) the right to disclosure and information
(e) the right to fair and responsible marketing
(f) the right to honest dealing and fair agreements
(g) the right to fair, just and reasonable terms and conditions
(h) the right to fair value, good quality and safety.

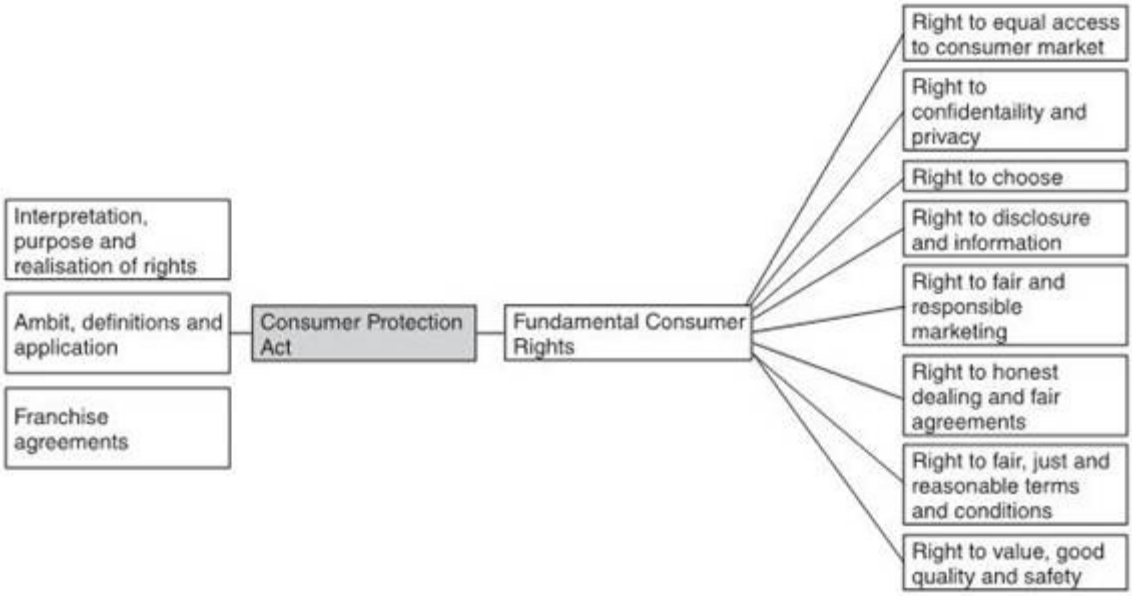


Figure 1: Structure of the Consumer Protection Act

30.2.2 Application of the Consumer Protection Act

Although the Act has a wide field of application, it may not be interpreted so as to preclude a consumer from exercising any rights afforded in terms of the common law.

Basically, the Act applies to every *transaction* occurring within South Africa for the *supply* of *goods* or *services* and to the *promotion* of goods or services and the goods or services themselves, unless the transaction is exempted from the application of the Act. The Act does not apply to the following:

(i) transactions for the supply or promotion of goods or services to the State
(ii) transactions in terms of which, at the time of transaction, the *consumer* is a juristic person whose asset value or annual turnover equals or exceeds the threshold value determined by the Minister (the Act does not apply to a juristic person whose asset value or annual turnover, at the time of the transaction, equals or exceeds the threshold value of R2 million)
(iii) transactions exempted by the Minister after a regulatory authority has applied for an industry-wide exemption
(iv) transactions constituting credit agreements under the National Credit Act, but the goods and services subject to such credit agreement are not excluded from the application of the Act
(v) transactions pertaining to services to be supplied under an employment contract
(vi) transactions giving effect to a collective bargaining agreement in terms of the Labour Relations Act 66 of 1995 or section 23 of the Constitution, or
(vii) a collective agreement in terms of the Labour Relations Act 66 of 1995.

Furthermore, advice or intermediary services, banking services, related financial services, or undertaking, underwriting or assumption of risks to the extent that the service is regulated by the Financial Advisory and Intermediary Act 37 of 2002 are excluded from the definition of service in section 1 and are therefore excluded from the application of the Act.

The Financial Services Laws General Amendment Act 45 of 2013 came into operation on 28 February 2014. It amends the Financial Services Board Act 97 of 1990 to provide that the Consumer Protection Act does not apply to any function, act, transaction, goods or services that is, or are, subject to Financial Services Board legislation, or to the Financial Services Board or a registrar referred to in Financial Services Board legislation.

One must, however, keep in mind that if goods supplied within South Africa in terms of a transaction are exempt from the application of this Act, such goods and the importer or producer, distributor and retailer of those goods are still subject to the provisions in the Act dealing with unsafe goods, safety-monitoring, recall of and damage caused by such goods. For example, where a juristic person does not qualify as a consumer in terms of the Act and goods purchased by the juristic person cause harm to persons in his or her shop or on his or her premises, damage caused by those goods will be regulated in terms of the Act.

To determine the field of application of the Act, the most important definitions contained in the provision on the application of the Act should be analysed. As stated above, the Act applies to every *transaction* occurring within South Africa for the *supply* of *goods* or *services* or the *promotion* of goods or services and the goods or services themselves, unless the transaction is exempted.

30.2.2.1 'Transaction'

The concept of 'transaction' is defined in section 1 of the Act. A transaction refers to transactions in the ordinary course of business. A transaction is an agreement between two or more persons for the *supply* of *goods* or *services* for *consideration*. Once-off transactions (transactions not concluded in the ordinary course of business) and other non-business transactions are therefore not 'transactions' that will be regulated by the Act. An example of a non-business transaction is where Alex sells his car to Peter privately (it is also sometimes described as a private transaction). However, supply for consideration is not always a requirement of a transaction, since certain arrangements must be regarded as 'transactions' irrespective of whether a charge or economic contribution is required. For example, the free supply of energy drinks by a marathon club to its members will constitute a transaction.

Those arrangements that must be regarded as transactions include the supply of goods or services in the ordinary course of business to members of a club, trade union, association, society or an incorporated or corporate voluntary association of people formed for a common purpose.

A solicitation of offers to enter into a franchise agreement also constitutes a transaction. An offer by a potential franchisor to enter into a franchise agreement

with a potential franchisee, a franchise agreement or an agreement supplementary to it, and the supply of goods and services to a franchisee in terms of the franchise agreement, are also regarded as transactions between a supplier and a consumer in terms of the Act. The Act applies to these potential franchises or franchise agreements, irrespective of the exclusionary provision that states that the Act does not apply to transactions where the consumer is a juristic person whose asset value or annual turnover equals or exceeds a threshold value to be determined by the Minister. Therefore the Act applies to the above-

mentioned franchise transactions irrespective of whether the size of the consumer juristic person falls outside the determined threshold.

Furthermore, the Act applies to transactions, irrespective of whether the supplier resides in or has its principal place of business outside South Africa, irrespective of the supplier's nature, and irrespective of a license being required to supply the products or services or part of them to the public. The effect is therefore that the Act also applies to foreign suppliers of goods and services in terms of every transaction occurring within South Africa, even if the supplier has no principal office or residence within South Africa.

30.2.2.2 'Goods'

'Goods' include, but are not limited to, anything marketed for human consumption, any tangible object, literature, music, photograph, motion picture, game, information, data, software, code or other intangible product written on any medium, licences to use such intangible objects, legal interests in land or other immovable property, gas, water and electricity. Bread, compact discs (CDs), electronic appliances and books are therefore all goods.

30.2.2.3 'Service'

'Service' includes, but is not limited to, work performed by a person for the direct or indirect benefit of another: education; information; advice or consultation; banking or similar financial services; transportation of goods or individuals; provision of accommodation; entertainment or access to entertainment; access to electronic communication infrastructure; access or a right of access to an event, premises, activity or facility; or access to or use of property in terms of a rental. Service also includes the right of occupancy of, or power or privilege over, land or immovable property, and the rights of a franchisee in terms of a franchise agreement to the extent provided for in the Act.

Advice in terms of the Financial Advisory and Intermediary Services Act 37 of 2002 is excluded from the definition of service.

30.2.2.4 'Supply'

'Supply' in relation to *goods* includes selling, renting, exchanging and hiring in the ordinary course of business for consideration. In relation to *services* it means to sell services, to perform or to cause services to be performed or provided, and

to grant access to premises, events, activities or facilities in the ordinary course of business for consideration.

30.2.2.5 'Supplier'

In many provisions the Act refers to a supplier. A 'supplier' is any person, including a juristic person, that markets goods or services. 'Market' means to supply or to promote.

30.2.2.6 'Promote'

'Promote' means to advertise, display or offer to supply services or goods in the ordinary course of business for consideration. It also means to make any representation in the ordinary course of business that could be interpreted as expressing willingness to supply services or goods for consideration, or engagement in any other conduct in the ordinary course of business that could reasonably be construed to be an inducement or attempted inducement to a person to engage in a transaction.

30.2.2.7 'Consumer'

A 'consumer' is any person, including a juristic person, to whom goods or services are marketed or supplied in the ordinary course of a supplier's business, unless the transaction is exempted from the application of the Act. However, transactions in terms of which the consumer is a juristic person whose asset value or annual turnover, at the time of the transaction, equals or exceeds the threshold value determined by the Minister, are excluded from the application of the Act.

30.2.3 Franchise agreements and the Consumer Protection Act

Franchise agreements are specifically regulated by the Act (see also paragraph 18.7). The Act provides that a franchise agreement between a franchisee and franchisor must comply with the following requirements:

- the franchise agreement must be in writing and signed by or on behalf of the franchisee
- the agreement must include any prescribed information or it must address any prescribed categories of information as required by the Minister, and
- the agreement must be in plain and understandable language.

The Act makes provision for a cooling-off right where a franchisor and franchisee have entered into an agreement. In terms of the cooling-off right, a franchisee may cancel a franchise agreement for any reason without incurring any cost or penalty within 10 business days after signature of the agreement by giving written notice to the franchisor.

30.2.4 Fundamental consumer rights in terms of the Consumer Protection Act

30.2.4.1 Right of equality

Section 8 of the Act prohibits the supplier of goods and services from unfairly discriminating against a person or category of persons on the grounds listed in the Constitution and the Promotion of Equality and Prevention of Unfair Discrimination Act 4 of 2000. These grounds include race, gender, sex, pregnancy, marital status, ethnic or social origin, colour, sexual orientation, age, disability, religion, conscience, belief, culture, language and birth. Although the Act allows differentiation on reasonable grounds, it does not allow discrimination. For example, it will not constitute a contravention of the Act to market any goods or services in a way that gives preference to a particular group of consumers, if those goods or services are reasonably intended to satisfy a specific need of that group of consumers. So, the marketing of high-heeled shoes for women only will not constitute discrimination. A consumer alleging breach of the equality provisions may institute proceedings before an equality court or file a complaint with the Consumer Commission (see paragraph 30.2.6.1), and if the complaint

appears to be valid, the Consumer Commission must refer it to the equality court. If a court will have to assess the fairness or reasonableness of conduct, all the factors and circumstances of a particular form of conduct will be taken into account.

30.2.4.2 Right to privacy

Sections 11 and 12 protect the consumer's right to privacy by placing restrictions on direct marketing. 'Direct marketing' means to approach a person, in the ordinary course of business, either in person or via mail or electronic communication, for the purpose of promoting or offering to supply goods or services to him or her. It also refers to approaching a person either in person or via mail or electronic communication for the purpose of requesting the person to make a donation.

Section 11 enables a consumer to restrict unwanted direct marketing by giving the consumer the right to refuse to accept direct marketing, to request the discontinuation of direct marketing or to pre-emptively block direct marketing. The Consumer Commission is responsible for a registry in which any person may, without any charge, register a pre-emptive block.

A cooling-off period for sales contracts concluded by direct marketing has been introduced by section 16 for the protection of the consumer. In terms of this cooling-off right, a consumer may without penalty or reason rescind a transaction resulting from direct marketing. The cooling-off right must be exercised by giving notice to the supplier in writing or in any other recorded manner within five business day after the later of the date on which the transaction was concluded or the goods were delivered to the consumer. This cooling-off period does not apply to transactions to which section 44 of the Electronic Communications and Transactions Act 25 of 2002 is applicable.

Section 12 provides for prohibited periods during which direct marketers may not contact a consumer at home: for example, on specific days, dates, public holidays,

or even certain times of the day, unless the consumer has clearly requested or agreed otherwise. These times may be prescribed by the Minister.

30.2.4.3 Right to choose

In this part of the Act, the Act deals with a consumer's right to select suppliers, the expiry and renewal of fixed-term agreements, pre-authorisation of a repair or maintenance service, the right to cancel advance reservations, bookings or orders, the right to choose or examine goods, rights with respect to the delivery of goods or supply of service, and the right to return goods and unsolicited goods or services.

30.2.4.3.1 The consumer's right to select suppliers

In terms of section 13, a supplier may not, as a condition for entering into a transaction, require that the consumer must purchase goods or services from the supplier or a designated third party or enter into an additional agreement for the supply of these goods or services. This is also known as bundling. An example of this would be where a lawnmower retailer requires a consumer to have the lawnmower that he or she is buying serviced at that specific dealership or to buy lawnmower blades from that supplier as a condition of the contract of sale. However, suppliers may use bundling if the supplier can prove that (defences) —

- the convenience of the bundled goods outweighs the limitation of the consumer's right to choose
- the bundling is to the economic benefit of the consumer, or
- the bundled goods are offered separately and at individual prices.

Bundling by franchisors is also regulated in terms of this section. However, it is also a defence to an allegation that a franchisor has contravened this section if any goods or services that the franchisee was required to purchase from the franchisor or a designated third party are reasonably related to the branded products or services that are subject to the franchise agreement. For example, if Pete's Steak House (the franchisor) requires all the branches (franchisees) to purchase plates with the Pete's Steak House's logo on it, this will constitute bundling. If a franchisee then alleges that Pete's Steak House contravened this section of the Act, Pete's Steak House may raise as defence that the required transaction is reasonably related to the branded products of Pete's Steak House that are subject to the franchise agreement.

30.2.4.3.2 Expiry and renewal of fixed-term agreements

Section 14 regulates the expiry and renewal of fixed-term agreements. Fixed-term agreements may not exceed the maximum period prescribed by the Minister for the different categories of consumer agreements. A consumer may cancel an agreement on the expiry of a fixed term without penalty or charge, but the consumer will still be liable for any amount owed in terms of the agreement up to the date of cancellation. A consumer may cancel a fixed-term agreement before its expiry by giving the supplier 20 business days' notice in advance, in writing or

other recordable manner, but the supplier may impose a reasonable cancellation penalty in contemplation of the agreement running its full course.

A notification of impending expiry, in writing or any other recordable form, must be sent by the supplier to the consumer not more than 80 days or less than 40 days before the expiry of a fixed-term agreement. Unless, on the expiry date, a consumer expressly directs a supplier to terminate an agreement or agrees to renew the agreement for a further fixed term, it will automatically continue on a month-to-month basis subject to material changes of which the supplier has given notice.

Banks have been exempted from section 14 of the Act.

30.2.4.3.3 Pre-authorisation of repair and maintenance service

Section 15 deals with the pre-authorisation of repair and maintenance services. This section applies only to transactions or consumer agreements with a price value above the threshold prescribed by the Minister. Furthermore, this section only applies —

(a) if a service provider in respect of a consumer's property or property under the consumer's control—
    (i) supplies a repair or maintenance service, or
    (ii) supplies or installs replacement parts or components, and
(b) if the service provider takes possession of the property, or
(c) if the consumer requested an estimate before any goods of services are supplied.

In terms of section 15, a service provider or supplier may not charge a fee for repairs or maintenance unless a quote was provided that satisfies the prescribed requirements, and the consumer authorised the work. A service provider or supplier may, however, charge a fee if an offer of an estimate was declined and the work authorised, or the consumer pre-authorised charges up to a certain amount. No fees may be charged for preparing an estimate, including any costs of performing diagnostic work. If an estimate was provided for services or goods, a supplier may not charge a price that exceeds the estimate, unless the consumer authorised the work to continue or the service provider informed the consumer of the additional estimated charges.

30.2.4.3.4 The consumer's right to cancel advance reservations, bookings or orders

In terms of section 17, consumers are allowed, subject to a reasonable cancellation fee, to cancel advance reservations, bookings or orders. No cancellation fee may be imposed if a consumer is unable to honour the reservation, booking or order owing to death or hospitalisation. This section does not apply to special-order goods. 'Special-order goods' are goods that a supplier expressly or implicitly was required or expected to procure, create or alter specifically to satisfy the consumer's requirement.

30.2.4.3.5 The consumer's right to choose or examine goods

In terms of section 18, a consumer may not, despite any statement or notice to the contrary, be held liable for loss or damage to goods displayed by a supplier, unless the loss or damage resulted from conduct by the consumer that amounts to gross negligence or recklessness, malicious behaviour or criminal conduct. For example, a notice stating 'Nice to look at, nice to hold, but if you break it, consider it sold' will not be enforceable.

If goods are displayed in or sold from open stock, the consumer may select or reject any particular item from that stock before completing the transaction. If a consumer agreed to purchase goods solely on the basis of a description or sample of goods, the goods delivered to a consumer must correspond with the goods the consumer would have been entitled to expect in all material aspects and characteristics.

30.2.4.3.6 The consumer's rights with respect to delivery of goods or supply of service

In terms of section 19, an implied condition of every transaction for the supply of goods and services is that the supplier will deliver the goods or services at the agreed time, date, place, at his or her own cost and that the goods to be delivered remain at the supplier's risk until the consumer has accepted delivery of them. The parties to the agreement may expressly agree otherwise.

A consumer is entitled to examine goods before taking delivery of them. If non-agreed goods are delivered with agreed goods, the consumer may reject all the delivered goods, accept the delivery of the goods, or pay for the agreed goods and treat the non-agreed goods as unsolicited goods (see paragraph 30.2.4.3.8). Non-agreed goods refer to instances where the supplier delivers the agreed goods mixed with goods of a different description or where the supplier delivered a larger quantity than agreed upon. The same rules apply to instances where goods or services are delivered at a location, date or time other than those agreed to.

Section 19 does not apply to franchise agreements or transactions to which section 46 of the Electronic Communications and Transactions Act 25 of 2002 is applicable.

30.2.4.3.7 The consumer's right to return goods

In terms of section 20, a consumer may, in certain circumstances, return goods to the supplier within 10 business days after delivery to the consumer. This does not replace the right that every consumer has in respect of the return of unsafe or defective goods, or any other right that exists between a supplier and consumer for the return of goods for a refund. The consumer may return goods to the supplier and receive a full refund for consideration paid for those goods, if the supplier has delivered -

(a) goods to the consumer in terms of an agreement arising out of direct marketing and the consumer has rescinded the agreement during the cooling-off period in terms of section 16 (see paragraph 30.2.4.2)
(b) goods that the consumer did not have an opportunity to examine before delivery and the consumer has rejected delivery in terms of section 19 (see paragraph 30.2.4.3.6 above)
(c) goods intended to satisfy a particular purpose communicated to the supplier and within 10 business days after delivery to the consumer, the goods have been found to be unsuitable for that particular purpose.

Goods returned in the case of (a) must be returned to the supplier at the consumer's risk and expense. Goods returned in the case of (b) and (c) must be returned to the supplier at the supplier's risk and expense. Goods may not be returned to a supplier if for reasons of public health, a public regulation prohibits the return of those goods. They may also not be returned to a supplier if the goods have been partially or entirely disassembled, physically altered, permanently installed, attached or added to other goods or property.

The supplier may impose a charge if the goods were opened and the packaging damaged. If, however, the goods have not been opened and are still in their original packaging, the consumer may not be charged anything. Where the goods were opened but repacked in their original packaging, the supplier may charge a reasonable amount for the actual use of the goods or any consumption or depletion of the goods, unless this was necessary to determine whether the goods were acceptable to the consumer.

30.2.4.3.8 Unsolicited goods or services

In terms of section 21, goods or services may become 'unsolicited' under the following circumstances, subject to requirements in subsection 2:

(a) If during direct marketing of goods or services, the supplier left goods with or performed services for a consumer without requiring or arranging payment for them, the goods or services are unsolicited.

(b) If a consumer is a party to an agreement in terms of which goods must be delivered periodically during the life of the agreement and (i) during the course of the agreement the supplier introduces goods or services that are materially different from the goods or services previously supplied or (ii) after the termination of that agreement the supplier delivers further goods or services to the consumer, the new or further goods are unsolicited.

(c) If a supplier delivers goods or performs services at a location, date or time other than those agreed and the consumer rejected delivery in terms of section 19 (see paragraph 30.2.4.3.6), those goods or services are unsolicited.

(d) If a supplier delivers a larger quantity of goods than the consumer agreed to buy, the excess goods are unsolicited, unless the consumer has rejected the entire delivery in terms of section 19.

(e) If goods have been delivered to or services performed for a consumer without the consumer having expressly or implicitly requested the delivery of the goods or services, the goods or service are unsolicited.

However, in the above instances the goods will only be considered unsolicited —

(a) if within 10 business days after delivery the supplier informs the consumer that the goods were delivered in error and the supplier then fails to recover the goods within 20 business days after it informed the consumer, or

(b) if the goods are delivered to a consumer and —

(i) those goods are clearly addressed to another person and have obviously been misdelivered, or

(ii) having regard to the circumstances of delivery, an ordinary alert consumer would have realised that the goods were intended to be delivered to another, and the consumer informed the supplier or deliverer that the goods had been misdelivered and those goods are not recovered within the following 20 business days.

Although this section does not create a duty for a consumer to inform the supplier of a misdelivery, goods will not be unsolicited if the supplier is not informed by the consumer of the misdelivery. If goods are not misdelivered, for example, where goods are intentionally delivered without the consumer having requested the delivery of those goods, the consumer will not have to inform the supplier of that delivery.

Once a consumer is in possession of unsolicited goods, he or she may either return or lawfully retain the goods. If the consumer retains the unsolicited goods, ownership in those goods passes unconditionally to the consumer. The supplier will then be liable to any other person in respect of any right or valid claim to those goods. The consumer then has no obligation to pay for unsolicited goods.

The aim of the provision is also to prevent suppliers from delivering goods or services to potential consumers without the consumer's prior knowledge or request and subsequently demanding of payment for such goods or services (also see paragraph 30.2.4.5.3 on negative option marketing).

30.2.4.4 Right to disclosure and information

30.2.4.4.1 Right to information in plain and understandable language

In terms of section 22, consumers are entitled to information in plain and understandable language. In terms of this section, any notice, document or visual representation that is required in terms of the Act or any other law should be in the form prescribed in the Act, and if no form is prescribed, it must be in plain language. Plain language is language that enables ordinary consumers with average literacy skills and minimal experience as consumers to understand the contents of documents without undue effort. The indicators of plain language that should be taken into account include the context, comprehensiveness, and consistency; the way the representation is done or the style of the document; the way in which the

sentences are structured; and the types of word used and aids used to assist the consumer in reading and understanding the document or representation.

30.2.4.4.2 Disclosure of price of goods and service

In terms of section 23, a retailer must not display any goods for sale without displaying the price of these goods. A price will only be adequately displayed if it is indicated in writing expressed in South African currency. This section makes provision for the indication of prices on labels, packaging, stamps and shelves. The price of an item may

also be indicated in brochures, catalogues or circulars if the brochures, catalogues or circulars are dated or if a time period is specified in them.

A supplier may not require a consumer to pay a higher price than the price displayed, unless the price is regulated in terms of public regulation, such as the price of petrol. If two prices are displayed the consumer will be allowed to pay the lowest price. If a price that was displayed has been covered by a second price, the second price will apply. If however, a displayed price contains an inadvertent and obvious error, the supplier will not be bound to it after the error was corrected and he or she took reasonable steps to inform consumers to whom the erroneous price may have been displayed of the error and the correct price. A displayed price will also not bind the supplier if an unauthorised person altered, covered or obscured the price. The displayed price of goods advertised at a discount or at a reduced price is deemed to include the discount or reduction. Section 23 does not apply if section 43 of the Electronic Communications and Transactions Act 25 of 2002 applies to the transaction or if the supplier supplied an estimate pertaining to the transaction.

30.2.4.4.3 Product labelling and trade descriptions

A 'trade description' refers to any description, statement, direct or indirect indication relating to the number, weight, measure, the manufacturer or producer, the ingredients, material, the place of origin of, the mode of manufacturing or patents, copyright or privilege regarding goods. It includes any statement in respect of the above-mentioned on labels, applied to goods, in signs, letters, invoices and so forth. However, it does not refer to trade marks. Section 24 prohibits suppliers from using trade descriptions while knowing that they are likely to mislead the consumer. Suppliers must also not tamper with a trade description in a manner that could mislead a consumer. The Minister may further prescribe categories of goods that are required to have trade descriptions applied to them, or the rules to be used for the purpose of determining the country of origin of the goods. Producers, importers, packagers or suppliers must also disclose genetically modified ingredients or components.

30.2.4.4.4 Disclosure of reconditioned and grey-market goods

In terms of section 25, a person offering or supplying goods (bearing the trademark of the original producer or supplier) that have been rebuilt, reconditioned or remade, must apply a notice to those goods stating that they have been rebuilt,

reconditioned or remade. A person who markets grey-market goods, that is, goods imported without the approval or licence of the registered trademark owner, must apply a conspicuous notice to those goods in the prescribed manner and form.

30.2.4.4.5 Sales records

In terms of section 26, a written record of each transaction must be given to the consumer, for example, in an invoice or slip. This section also requires certain information to be included in the written record: for example, the supplier's full name or registered business name, VAT registration number, the date of the transaction, the amount of taxes and the total price. This section does not apply to transactions to which section 43 of the Electronic Communications and Transactions Act 25 of 2002 applies or if the Minister has exempted certain categories of goods or services from the application of this section.

30.2.4.4.6 Disclosure by intermediaries

Section 27 regulates the activities of intermediaries whose activities are not regulated in terms of any other legislation. An 'intermediary' refers to an agent or person acting on behalf of another. In terms of this section, the Minister may require an intermediary to keep records of all his or her transactions and relationships.

30.2.4.4.7 Identification of deliverers and installers

In terms of section 28, if a person is engaged in direct marketing at the premises of a consumer while performing services, or delivering or installing goods, that person must visibly wear an identification device such as a badge, or a consumer may request that person to provide suitable identification.

30.2.4.5 Right to fair and responsible marketing

The right to fair and responsible marketing aims to create fair business practices in respect of advertising and selling. In terms of this right, the general standard and specific types of marketing are regulated. Although the Consumer Protection Act does not apply to credit agreements in terms of the National Credit Act, the right to fair and responsible marketing in the Consumer Protection Act can apply to the marketing of credit products.

30.2.4.5.1 General standards for marketing of goods and services

Section 29 basically prohibits a producer's, importer's, distributor's, retailer's or service provider's marketing of any goods or service in a manner that is misleading, fraudulent or deceptive in any way.

30.2.4.5.2 Bait marketing

Section 30 prohibits bait marketing. In terms of section 30, a supplier must not advertise goods or services as being available at a specific price in a manner that will mislead or deceive consumers in relation to the actual availability of those

goods and services. If a supplier expressly stated in an advertisement that a limited number of goods or services will be available at a specific price, those goods or services must be made available to the extent of the expressed limits. It will not constitute bait marketing if a supplier offers to procure another person to supply a consumer with the same or similar goods or services of the kind advertised.

30.2.4.5.3 Negative option marketing

Section 31 basically prohibits a supplier from promoting goods or services on the basis that they are to be supplied unless the consumer declines such offer. This is also known as negative option marketing. A supplier must also not offer to modify an agreement for

the supply of goods of services on the basis that, unless the consumer declines the offer, the modification will automatically come into existence. Any agreement entered into as a result of a negative option will be void. An example of negative option marketing is where Abel receives a book in the post without ordering that book and it is deemed that Abel and the supplier entered into an agreement because Abel failed to reject the offer by sending the book back to the supplier.

30.2.4.5.4 Direct marketing to consumers

Direct marketing is marketing where a person is approached in person, by mail or by electronic communication for the purpose of promoting or offering to supply goods or services or requesting a person to make a donation. Section 32 provides that if a person directly markets goods or services and as a result concludes an agreement or enters into a transaction, the person then has a duty to inform the consumer, in the prescribed form and manner, of his or her cooling-off right in terms of the Act (see paragraph 30.2.4.2). If a direct marketer left goods with a consumer without requiring or arranging payment for it, those goods are unsolicited goods (see paragraph 30.2.4.3.8).

30.2.4.5.5 Catalogue marketing

Catalogue marketing refers to an agreement for the supply of goods or services that is not entered into in person. It includes agreements concluded telephonically or by postal order or fax, or in any similar manner in which, with respect to goods, a consumer does not have the opportunity to inspect the goods before the conclusion of an agreement. In terms of section 33, before entering into an agreement as a result of catalogue marketing, a supplier must disclose certain information to the consumer, which includes the supplier's name, licence number, registration number (if any), physical address of business premises, delivery arrangements, the manner in which a complaint may be lodged and so forth. This section does not apply to transactions to which Chapter 7 (on consumer protection) of the Electronic Communications and Transactions Act 25 of 2002 applies, or to franchise agreements.

30.2.4.5.6 Trade coupons and similar promotions

Some promotional offers use coupons which entitle the consumer to a lower price or added value. A 'promotional offer' is defined as an offer or promise of any prize, reward, gift, free goods or services, price reduction, concession or enhancement of the quality or quantity of goods and services, even if the offer is subject to the offeree entering into any other transaction. Section 34 prohibits a person from making a promotional offer with the intention of not fulfilling it or fulfilling it other than as offered. A document setting out a promotional offer must set out basic information such as the nature of the prize, reward, gift, free goods or services or price reduction, to which goods or service the promotional offer relates, the steps required by a consumer to accept the offer or receive the benefits, the person from whom, the time when and the place where the prize, reward and gift may be received and so forth. A sponsor of a promotional offer has a duty to ensure that the supply of the thing offered is sufficient to fulfill anticipated demands resulting from the offer and not to require consumers to accept goods or services of a quality inferior to those usually available to other consumers. A supplier may, however, in order to accommodate the demand, offer to supply or procure another person to supply comparable goods or services. A promotional offer must not be confused with a promotional competition or a loyalty programme, to which this section does not apply (see paragraphs 30.2.4.5.7 and 30.2.4.5.8).

30.2.4.5.7 Customer loyalty programmes

A 'loyalty programme' is any arrangement or scheme in the ordinary course of business in terms of which a supplier of goods or services, or an association of suppliers, grants loyalty credits or awards in connection with a transaction. A 'loyalty credit or award' is any benefit or right to goods or services accruing to a consumer, such as tokens or points, and it is a legal medium of exchange that can be tendered or offered as consideration for any goods or services offered in terms of a specific loyalty programme. Section 35 prohibits a person from offering participation in a loyalty programme or loyalty credits with the intention of not providing it or providing it other than as offered.

The documents containing the offer to participate in a loyalty programme must set out the nature of the programme or credits, the goods or services to which it relates, the steps required from the consumer in order to participate and the person from whom and the place, date and time at which the consumer may gain access to the programme or the credits. A sponsor or supplier who accepts loyalty credits in exchange for goods or services must ensure that those goods or services must be available sufficiently to accommodate the reasonably anticipated demand for those goods or services. The availability of goods or services under a loyalty programme may only be restricted by a supplier if the consumers in that programme received written notice of that restriction at least 20 business days before the restriction begins. The total period of that restriction must not exceed 90 days per year. No monetary charges must be imposed in respect of the administration of a loyalty credit transaction if the consumer is required to pay a periodic fee to remain a

member of the programme. A supplier may, however, in order to accommodate the demand, offer to supply or procure another person to supply comparable goods or services. Loyalty programmes should be distinguished from prepaid vouchers in terms of section 63 (see paragraph 30.2.5.1).

30.2.4.5.8 Promotional competitions

A 'promotional competition' is any competition, game, scheme, arrangement, system, plan or device distributing a prize by lot or chance, conducted in the ordinary course of business, for the purposes of promoting a producer, goods or services. A 'prize' is any

gift, reward, free goods or services, price reduction and so forth. Only promotional competitions where the prize exceeds the threshold prescribed by the Minister are regulated in terms of the Act. In terms of section 36, no payment or consideration may be required to be paid by a participant in a promotional competition other than the reasonable cost of posting or transmitting an entry form. For example, a car manufacturer promoting a new car in a promotional competition will not be able to charge an entry fee of five rand per SMS entry if the SMS only costs twenty cents. Section 36 further prohibits a person from informing a consumer that he or she has won a competition if no competition was conducted; where the competition is subject to an undisclosed condition; or where the consumer is required to offer further consideration for the prize after the competition results have been announced. It also prohibits a person from informing a consumer that he or she has a right to a prize if the person, in fact, has no right; if the prize were offered to all similarly situated persons or to a class of persons; or if the consumer, before becoming eligible to receive the prize, is required to offer further consideration or to purchase goods or services. A prize may not be awarded to a director, member, partner, supplier, employee, agent or consultant of a promoter.

In order to ensure transparency, before a competition begins, a promoter has to prepare competition rules and make them available to the Consumer Commission and also to any participant on request and without cost. A copy of the rules must be retained by the promoter for a specific period after the competition closed. An offer to participate in a promotional competition must contain certain minimum information such as the benefit or competition to which the offer relates; steps required to participate; the basis on which results will be determined; the closing date; the medium through which the results will be made known, and where and when a person can obtain a copy of the rules.

30.2.4.5.9 Alternative work schemes

Section 37 prohibits any person from making false representations in respect of the availability, actual or potential profitability, risk or any material aspect of work, business or an activity involved in any arrangement for gain. These arrangements include arrangements in terms of which a person invites, solicits or requires persons to conduct work or business from their homes or to invest money from their homes. An advertisement promoting these arrangements must be accompanied by

a cautionary statement in the prescribed wording and form. In this statement the uncertainty of the extent of the work, business or activity and the income or benefit to be derived from it must be set out. The advertisement must set out the full name or registered business name of the promoter, the address and contact number of his or her or primary place of business and the nature of the work, business or activity. A consumer may not be charged any fees, except to the extent that the supplier performed the work or business activity, or made or received the contemplated investment.

30.2.4.5.10 Referral selling

Section 38 prohibits a person from promoting, offering, supplying, agreeing to supply or inducing a consumer to accept goods or services on the representation that the consumer will receive a commission, rebate or other benefit if the consumer subsequently gives the supplier the names of consumers, or helps the supplier to supply goods or services to other consumers, and the commission, rebate or other benefit is contingent upon an event occurring after the consumer agrees to the transaction. An example will be where Freddy accepts an offer to enter into a gym contract with Jolly Gym on the representation that he will receive a discount if he gives the names of other consumers to Jolly Gym or assists Jolly Gym in offering gym contracts to consumers, when the other consumers agree to transactions with Jolly Gym. This prohibition does not apply to franchise agreements.

30.2.4.5.11 Agreements with persons lacking legal capacity

In terms of section 39, an agreement for the supply of goods or services is void if the consumer is subject to an order of a court holding that person to be mentally unfit and the supplier knew or could reasonably have determined that the person was subject to such an order. In terms of this provision, the agreement will be voidable if it was entered into with an unemancipated minor without the consent of an adult responsible for the minor, and has not been ratified by the adult responsible for the minor or the consumer after being emancipated or becoming an adult. Section 39 does not apply if the consumer, or someone acting on behalf of the consumer, by act or by omission, induced a supplier to believe that the consumer had legal capacity to contract, or attempted to suppress the fact that the consumer does not have full legal capacity to contract.

30.2.4.6 Right to fair and honest dealing

The Consumer Protection Act protects consumers against unconscionable, unfair, unreasonable, unjust or improper trade practices. It also protects consumers against any deceptive, misleading, unfair or fraudulent conduct. It specifically regulates unconscionable conduct, false, misleading or deceptive representations, fraudulent schemes and offers, pyramid schemes and other possibly unreasonable conduct and trade practices.

30.2.4.6.1 Unconscionable conduct

Unconscionable conduct refers to conduct having a character contemplated in section 40, or other improper or unethical conduct that would be improper or unethical to a degree that would shock the conscience of a reasonable person. In terms of section 40, a supplier must not use physical force, coercion, undue influence, pressure, duress, harassment, unfair tactics or any other similar conduct in marketing, supply, negotiation, execution, enforcement, demand or in the recovery of goods. A supplier may also not knowingly take advantage of the fact that a consumer was substantially unable to protect his or her interests because of physical or mental disability, illiteracy, ignorance, inability to understand the language of an agreement or any similar factor.

30.2.4.6.2 False, misleading or deceptive representations

In terms of section 41, suppliers are not allowed, in the marketing of goods or services, to use false, misleading or deceptive representation, innuendo, exaggeration or ambiguity, or knowingly to allow consumers to believe false, misleading or deceptive representations. It will constitute a false, misleading or deceptive representation falsely to produce, or imply or fail to correct, a misapprehension on the part of the consumer.

30.2.4.6.3 Fraudulent schemes and offers

Section 42 prohibits any person from promoting, joining or participating in a fraudulent currency scheme or a fraudulent financial transaction. For example, a transaction which involves the proceeds of an unlawful activity, or a transaction entered into with the intention of defrauding a person by representing that someone is capable of increasing a sum of money by some scientific or supernatural means, is prohibited.

30.2.4.6.4 Pyramid and related schemes

Section 43 prohibits a person from joining, promoting or entering into a multiplication scheme, a pyramid scheme, a chain letter scheme or any scheme identified by the Minister.

A multiplication scheme exists when a person offers, promises or guarantees to a consumer an effective interest rate that is at least 20 per cent above the REPO rate (repurchase rate) determined by the Reserve Bank.

A scheme will constitute a pyramid scheme if a participant in the scheme receives compensation that is derived primarily from his or her recruitment of other participants rather than from the sale of goods or services.

A scheme will constitute a chain letter scheme if it has various levels of participation; existing participants recruit new participants and each newly recruited participant is required upon joining the scheme to pay certain consideration. The payment is then distributed to one or some of the previously existing participants, irrespective of whether the new participant received goods or services in exchange

for consideration. Upon joining the scheme, new participants are assigned to the lowest level of participation in the scheme.

30.2.4.6.5 A consumer's right to assume supplier is entitled to sell goods

In terms of section 44, every consumer has a right to assume that a supplier will have a legal right or the authority of the owner to supply, sell or lease goods. The consumer also has a right to assume that between a supplier and a consumer, the supplier is fully liable for any charge or encumbrance pertaining to the goods in favour of third parties, such as outstanding licence fees on a car that is being sold. Furthermore, a consumer has a right to assume that the supplier guaranteed that he or she will have and enjoy quiet possession of the goods, without any charge or encumbrance, unless such charge or encumbrance was disclosed to the consumer beforehand. These rights are implied provisions in every transaction and agreement. If any transaction or agreement for the supply of goods to a consumer infringes a right or claim of a third party pertaining to those goods, the supplier is liable to the third party to the extent of the infringement, except where a charge or encumbrance was disclosed to the consumer before entering into an agreement.

30.2.4.6.6 Auctions

Section 45 regulates several aspects of auctions. An auction in terms of this section includes a sale in execution by auction pursuant to a court order. In terms of this section, a sale by auction is only complete when an auctioneer announces its end by the fall of the hammer or in any other customary manner. When goods are put up for sale by auction in lots, each lot is regarded to be the subject of a separate transaction, unless there is evidence to the contrary. Any bid may be retracted before the end of an auction. If an auction is subject to a reserved or upset price or a right to bid by or on behalf of the owner or auctioneer, notice of this must be given in advance. If this notice was not given in advance, the owner or auctioneer must not bid or employ any person to bid at the auction and knowingly accept any bid from such person. If an auctioneer violates this subsection by bidding by, or on behalf of him- or herself or an owner, without giving the required advance notice, a consumer may approach a court to declare the transaction fraudulent.

30.2.4.6.7 Changes, deferrals and waivers and substitution of goods

In terms of section 46, if goods or services are supplied as a result of a change to an existing agreement, or a deferral or waiver of a right under an existing agreement, it must not be treated as a new agreement for the purposes of the Act, if the change, deferral or waiver is made in accordance with the agreement or the Act. If a transaction was subject to a written agreement or sales record, the supplier has to prepare and deliver to the consumer an amended agreement or sales record, describing the substituted goods, without making any other changes to the original document.

30.2.4.6.8 Over-selling and over-booking

In terms of the section 47, a supplier is not allowed to accept payment or any consideration for goods or services, if he or she has no reasonable intention to supply those goods or services or if he or she intends to supply goods or services that are materially different from the goods or services in respect of which payment was accepted. Furthermore, if a supplier makes a commitment or accepts a reservation to supply goods or services on a specific date or time and he or she then fails to do so because of insufficient stock or capacity to supply those, similar, better or comparable goods or services, the supplier has to refund the consumer the amount, together with interest at the prescribed rate from the date on which the amount was paid until the date of reimbursement; and in addition, the consumer must be compensated for costs directly

incidental to the supplier's breach of contract. A supplier will, however, not be liable for the additional costs of the consumer if the shortage of stock or capacity is due to circumstances beyond the supplier's control and the supplier took reasonable steps to inform the consumer of the shortage of stock or capacity as soon as he or she was able to do so in the circumstances. A shortage of stock or capacity will not be 'due to circumstances beyond the supplier's control' if the shortage results partially, completely, directly or indirectly from a failure on the part of the supplier to carry out diligently any routine matter in his business. An example of this prohibited conduct will be where an airline double-books flight tickets for a specific flight and some consumers are then transferred to other flights as a result of the over-booking.

30.2.4.7 Right to fair, just and reasonable terms and conditions

This part of the Consumer Protection Act contains measures dealing with unfair, unreasonable or unjust contract terms. One of the aims of the Act is to protect consumers against unconscionable, unfair, unreasonable, unjust or improper practices.

30.2.4.7.1 Unfair, unreasonable or unjust contract terms

Section 48 deals with unfair, unreasonable and unjust contract terms on more than one level. First, a supplier must not supply, offer to supply or enter into an agreement to supply goods or services at a price or on terms that are unfair, unreasonable or unjust. Secondly, a supplier is not allowed to market any goods or services, or negotiate or enter into a transaction or agreement for the supply of goods or services, in a manner that is unfair, unjust or unreasonable. Thirdly, a supplier must not require a consumer or a person to whom goods or services are supplied at the consumer's direction to waive any rights, assume any obligation or waive any liability of the supplier on terms that are unfair, unreasonable or unjust, or impose any such terms as a condition of entering into a transaction. A transaction, an agreement, a term or condition or a notice is unfair, unreasonable or unjust if —

- it is excessively one-sided in favour of any person other than a consumer

- the terms of the agreement or transaction are so adverse to the consumer that it is inequitable
- a consumer relied, to his or her detriment, on a false, misleading or deceptive representation or any statement of opinion provided by or on behalf of a supplier (see paragraph 30.2.4.6.2)
- the transaction or agreement was subject to a term or condition or a notice which in terms of section 49 must be brought to the consumer's attention, and the term, condition or notice is unfair, unreasonable, unjust or unconscionable, or the fact, nature and effect of the term, condition or notice was not drawn to the consumer's attention as required by section 49 (see paragraph 30.2.4.7.2).

The court will consider several factors in order to decide whether an agreement or transaction will be unfair, unreasonable, or unjust. These factors include —

- the fair value of the goods and services
- the nature of the parties to the agreement or transaction
- the parties' relationship to each other
- the parties' relative capacity, education, experience, sophistication and bargaining position
- the circumstances of the agreement or transaction that existed or were reasonably foreseeable at the time of the transaction, agreement or conduct, irrespective of whether the Act was in force at that time.

30.2.4.7.2 Notice required for certain terms and conditions

If an agreement contains specific terms and conditions as set out in section 49, it must be brought to the attention of the consumer in the prescribed form and manner. These types of terms are terms that purport to —

- limit in any way the liability or risk of the supplier or someone else
- constitute an assumption of risk or liability by the consumer
- impose an obligation on a consumer to indemnify the supplier or someone else for any cause, or
- be an acknowledgment of any fact by the consumer.

If a provision concerns any activity or facility that is subject to risk of an unusual character or nature, or risks of which the consumer could not reasonably be expected to be aware of, or if it could result in serious injury or death, the supplier must specifically bring the fact, nature and potential effect of the risk to the attention of the consumer in the prescribed form and manner. The consumer has to assent to that provision or notice by signing or initialling the provision.

A supplier can minimise his or her liability for unfair contract terms in this regard by drawing the attention of the consumer to the fact, nature or effect of a clause or notice, in plain language and by giving a consumer adequate opportunity to comprehend the notice or provision.

30.2.4.7.3 Written consumer agreements

In terms of section 50, the Minister may prescribe categories of agreements that should be in writing (see again paragraph 7.3.1). If an agreement between a supplier and consumer is in writing, whether as required in terms of the Act or voluntarily, the agreement will be valid, irrespective of whether the consumer signed the agreement. The supplier must provide a free copy of the agreement to the consumer. The copy can also be free electronic access to a copy of the agreement. An agreement also has to be in plain and understandable language and it must set out an itemised break-down of the financial obligations of the consumer under the agreement. If an agreement is not required to be in writing, a supplier must at least, as prescribed, keep a record of transactions entered into over the telephone or in any other recordable form.

30.2.4.7.4 Prohibited transactions, agreements, terms or conditions

Section 51 of the Act prohibits agreements or terms that have the purpose of defeating the purpose of the Act, misleading or deceiving a consumer, or terms which subject the consumer to fraudulent conduct. A term or an agreement may also not purport to waive or deprive consumers of their rights in terms of the Act; avoid a supplier's duty in terms of the Act; or authorise a supplier to do something that is unlawful in terms of this Act; or fail to do something that is required in terms of the Act. Section 51 further prohibits a supplier from using exemption or indemnity agreements or terms that limit or exempt a supplier from liability for any loss attributable to the gross negligence of the supplier or someone acting on his or her behalf. It also prohibits the use of agreements or terms that constitute an assumption of risk or liability by the consumer for these damages. Furthermore, an agreement or term may not impose an obligation on a consumer to pay for damage to goods displayed by a supplier (see paragraph 30.2.4.3.5).

Section 51 further prohibits the use of certain terms or agreements such as agreements or terms resulting from negative option marketing; falsely expressing an acknowledgement by a consumer that no representations or warranties were made before an agreement was entered into; expressing an undertaking to sign in advance documents relating to enforcement; expressing an agreement by the consumer to deposit a bank card or identity document or provide a pin code or number to be used to access an account, and so forth. Any agreement or term that contravenes section 51 is void to the extent of the contravention.

30.2.4.7.5 Powers of court to ensure fair and just conduct, terms and conditions

Section 52 confers a broad power on the court to ensure fair and just conduct, terms and conditions in those cases where the other provisions of the Act prove to be inadequate. A number of factors are listed in section 52 that the court must take into consideration in the exercise of its discretion. These factors include whether there was any negotiation between the supplier and the consumer, and if so, the extent thereof; the fair value of the goods and services; the nature of the parties to

the transaction, and so forth. Only a court may make an order in respect of the right to fair, just or reasonable terms or conditions.

30.2.4.8 Right to fair value, good quality and safety

30.2.4.8.1 Consumer's right to demand quality service

When a supplier agrees to perform services for a consumer, in terms of section 54, the consumer has a right to timely performance and completion of those services; to timely notice of any unavoidable delay in the performance of the services; and to performance of the services in a manner and quality that persons are generally entitled to expect. The consumer also has a right to the use, delivery or installation of goods that are free of defects; and of a quality that persons are entitled to expect, if the goods are required for the performance of services; and to the return of property or control over property to the consumer in the same condition as it was in when the consumer made it available for the performing of services by the supplier.

If a supplier then fails to perform services to this standard, the consumer may require the supplier to remedy the defect in the services performed or to refund the consumer a reasonable portion of the price, having regard to the extent of the failure.

30.2.4.8.2 Consumer's rights to safe, good-quality goods

Section 55 requires goods to meet a specific standard. It provides that a consumer has a right to receive goods that are reasonably suitable for the purposes they are intended for; are of good quality; in a working condition and free of any defects; will be usable and durable for a reasonable time and comply with any applicable standards. Furthermore, if a consumer has specifically informed the supplier of the particular purpose for which the consumer wishes to acquire goods, and the supplier offers to supply such goods, or acts in a manner consistent with being knowledgeable about the use of those goods, the consumer has a right to expect that these goods are reasonably suitable for the specific purpose that the consumer has indicated. In order to determine whether goods comply with these standards, the circumstances of the supply of goods must be considered. These circumstances include the manner in which, and the purposes for which goods were marketed; the use of any trade description or mark, and so forth. Whether a product failure was latent or patent is irrelevant.

Further, a product failure or defect may not be inferred solely on the ground that better goods have become available. However, this right of a consumer does not apply if the consumer has been expressly informed that particular goods were offered in a specific condition and has expressly agreed to accept the goods in that condition, or knowingly acted in a way compatible with accepting the goods in that condition.

30.2.4.8.3 Implied warranty of quality

In terms of section 56, in any transaction pertaining to the supply of goods to a consumer, there is an implied provision that the producer, importer, distributor and retailer each warrant that the goods comply with the standards set out in the consumer's right to safe, good-quality goods (see paragraph 30.2.4.8.2). If the goods fail to satisfy these requirements and standards, the consumer may, within six months after delivery, return the goods to the supplier, without penalty and at the supplier's risk and expense. The supplier must, at the consumers' choice, either repair or replace the failed, unsafe or defective goods or refund to the consumer the purchase price. This implied warranty and the right to return goods are in addition to any other warranty or condition imposed by common law, legislation and any express warranty or condition stipulated by the producer, importer, distributor or retailer.

30.2.4.8.4 Warranty on repaired goods

In terms of section 57, new or reconditioned parts installed during repair or maintenance work, and the labour to install it, are warranted for a period of three months after the date of installation or for such longer period as the supplier may specify. This warranty will be void if the consumer subjected the part or goods in which it was installed to misuse or abuse. The warranty also does not apply to wear and tear. This warranty is concurrent with any other deemed, implied or express warranty.

30.2.4.8.5 Warning concerning fact and nature of risks

In terms of section 58, a supplier of any activity or facility that is subject to any risk of an unusual nature or character, risk of which a consumer could not reasonably be expected to be aware of or risk that could result in serious injury or death, must bring the fact, nature and potential of that risk to the attention of the consumer (see paragraph 30.2.4.7.2). The same applies to a person who packages hazardous or unsafe goods for supply to consumers. For example, a supplier of chocolates may have to indicate on the packaging that the chocolates were produced in a factory that also processes nuts or peanuts, as these are hazardous to persons who are allergic to nuts.

30.2.4.8.6 Recovery and safe disposal of designated products or components

If any legislation prohibits the disposal or deposit of particular goods, components, remnants, containers or packaging of any goods into a common waste collection system, any person who, in the ordinary course of business, supplies any such object must, in terms of section 59, accept the return of that object from any consumer without charge, irrespective of whether the particular supplier supplied the object to the particular consumer. Any person who in the ordinary course of business produces, imports or distributes any such object as part of the supply

chain by which the goods reach the consumer, must in turn accept the return of any such object.

30.2.4.8.7 Safety monitoring and recall

In terms of section 60, the Consumer Commission has a duty to promote, within industry codes, the development, adoption and application of industry-wide codes of practice providing for systems to receive notice of consumer complaints regarding product failures, defects or hazards and return of goods as a result of that. For example, where the Consumer Commission has received numerous complaints regarding a failure or hazard in a specific car brand, the Consumer Commission will be able to order the manufacturer to recall all the cars of that brand sold to consumers.

30.2.4.8.8 Liability for damage caused by goods

Section 61 deals with so-called product liability. This section introduced strict or no-fault liability, which means that a consumer will not have to prove fault in order to hold the wrongdoer liable for a delict in terms of this provision (see paragraph 2.2.4.4.2 on delicts). In terms of section 61, a producer, importer, distributor or retailer is liable for harm caused to any person by the supply of unsafe goods, product failure, defect or hazard or inadequate instructions or warnings. A producer, importer, distributor or retailer will be liable irrespective of whether the harm resulted from any negligence on its part. A supplier of services who, in conjunction with the performance of those services, supplies, applies, installs or provides access to goods must be regarded, for the purposes of section 61, as the supplier of those goods.

Harm for which a person may be held liable in terms of this section includes death or injury of a person, illness, loss or damage to any property and any economic loss that resulted therefrom.

30.2.5 Supplier's accountability to consumers

30.2.5.1 Lay-bys

A lay-by agreement refers to an agreement in terms of which a supplier agrees to sell goods to a consumer where the consumer pays the purchase price in instalments and the supplier remains in possession of the goods until the full purchase price has been paid. Section 62 regulates lay-by agreements. In every lay-by transaction, each amount paid by a consumer remains the consumer's property until the goods have been delivered to the consumer. The goods remain at the risk of the supplier until they have been delivered to the consumer. If the supplier is unable to deliver the goods after the consumer has paid the full price, the supplier must either, at the option of the consumer, supply the consumer with equivalent or superior goods or refund the consumer the money paid with interest if the inability to deliver the goods is due to circumstances beyond the supplier's control. If, however, the inability to deliver the goods is not due to circumstances beyond the supplier's

control, the supplier must refund the consumer double the amount paid for the goods as compensation for breach of contract. A failure or inability to supply the goods will not be deemed 'due to circumstances beyond the supplier's control' if the shortage results partially or completely from a failure on the part of the supplier diligently to carry out an ordinary or routine matter pertaining to its business.

If a consumer terminates the agreement before fully paying for the goods or fails to complete the payment for the goods within 60 business days after the agreed date of completion, the supplier may charge a termination penalty in respect of those goods.

30.2.5.2 Prepaid certificates, credits and vouchers

Section 63 regulates instances where suppliers accept payment or other consideration from consumers in exchange for a prepaid certificate, card, credit or voucher, commonly referred to as vouchers. The payment is accepted in terms of an agreement to provide goods or services to any person who presents the voucher, up to the value represented by it, for example, prepaid cellphone airtime vouchers. Section 63 provides that a prepaid certificate, card, credit, voucher or similar device does not expire until the date on which its full value has been redeemed in exchange for goods or services or future access to services; or three years after the date on which it was issued; or at the end of a longer or extended period agreed by the supplier.

30.2.5.3 Prepaid services and access to service facilities

Pre-paid services do not refer to prepaid vouchers (see paragraph 30.2.5.2). They refer to periodic membership fees or any amount paid in respect of services or access to services to be provided more than 25 business days after the payment is made. This is regulated by section 64. The amount paid remains the property of the consumer until the supplier deducts a charge against it. Prepaid gymnasium membership fees is an example of prepaid services.

30.2.5.4 Supplier to hold an account for consumer's property

When a supplier is in possession of any prepayment, deposit, membership fee or other money or property belonging to a consumer, the supplier must not treat it as his or her own property. In the handling, safeguarding and utilisation of that property the supplier must exercise the degree of care, diligence and skill that can be reasonably expected from a person responsible for managing property belonging to another person.

30.2.5.5 Deposits in respect of containers, pallets or similar objects

In terms of section 66, the Minister may, in consultation with the Minister of Environmental Affairs and Tourism, prescribe a minimum or maximum deposit that a supplier may or must require a consumer to pay in respect of the return of certain items or devices such as bottles, containers, pallets or reels. If a consumer

then returns the item to any supplier of goods ordinarily sold in that item, the supplier must pay the consumer the amount of the deposit irrespective of whether the person returning the item is the same person who originally paid a deposit for that item or device to the supplier.

30.2.5.6 Return of parts and materials

When a service provider is authorised to perform a service to the goods or property of the consumer, he or she must keep the parts or components that he or she removed from the goods, store them separately from parts that were removed from other goods or components, and return them to the consumer in a reasonably clean container, unless the consumer declines the return of the parts or components. This section (section 67) does not apply to any substance, part or component that is required, in terms of any warranty or insurance claim under which work was carried out or in terms of any public regulation, to be recovered, disposed of at the direction of a producer, insurer or distributor, or disposed of in a safe manner.

30.2.6 Protection of consumer rights

In terms of section 100, the Consumer Commission may issue a compliance notice to any person who engaged in conduct prohibited by the Act. If the person fails to comply with the compliance notice, the Consumer Commission may refer the matter to the National Prosecuting Authority for prosecution, or apply to the Consumer Tribunal (see paragraph 30.2.6.2) for the imposition of an administrative fine.

30.2.6.1 The Consumer Commission

The National Consumer Commission is established in terms of the Act. It is an organ of state which has jurisdiction throughout the Republic. The Commission has several enforcement functions and is responsible for promoting dispute resolution between consumers and suppliers and receiving complaints concerning prohibited conduct or offences. It is also responsible for, among other things, monitoring the consumer market, investigation, issuing and enforcing compliance notices. The Commission has powers in support of investigation such as the power to issue summons and to enter and search premises under warrant. The Commission must also conduct research, liaise with other regulatory authorities, promote consumer protection and make recommendations to the Minister.

30.2.6.2 The Consumer Tribunal

The Consumer Tribunal was established in terms of the National Credit Act 34 of 2005 (see paragraph 16.3.5.3). It conducts hearings into complaints relating to the National Credit Act and the Consumer Protection Act and it may impose penalties in respect of prohibited or required conduct.

30.2.7 Business names

The Act regulates certain aspects of business names in sections 79-81. These aspects include the identification of a supplier, the registration of business names, and criteria for business names. In terms of section 79, a supplier must not carry on business, advertise or promote under any name except the person's full name as recorded in an identity document, in the case of an individual, or, in the case of a juristic person, as registered in terms of a public regulation.

Further reading

T Naudè & S Eiselen (eds) *Consumer Protection Act* (2014) (to be published by Juta)