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The Duty to contract in good faith: What does it *actually* mean?

JULY 2024 | PREPARED BY NOBUHLE MATHABA



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1. INTRODUCTION

The duty of good faith is a principle that has formed the foundation of society as we know and the basis of agreements across cultures and nations for centuries. In a South African context, the duty of good faith can be widely understood to encompass the principle of Ubuntu which informs the fundamental ideals embodied in our Constitution. Therefore, the duty to contract being recognised as an underlying principle in the South African law of contract is only natural. However, did the SCA judgment in *Capitec Bank Holdings Ltd and Another v Coral Lagoon Investments 194 (Pty) Ltd and Others* [1] (“*Capitec Holdings*”) reiterate the idiom “every rule has an exception”? This article aims to explore the decision in *Capitec Holdings* and its effect on the interpretation and application of the duty to contract in good faith.

2. THE FACTS OF CAPITEC

Capitec Bank Holdings Limited (“*Capitec Holdings*”), Coral Lagoon Investments 194 (Pty) Ltd (“*Coral*”), and Ash Brook Investments 16 (Pty) Ltd (“*Ash Brook*”), concluded a subscription of shares and shareholders agreement (“the subscription agreement”) in terms of which, Coral, wholly owned by Ash Brook, would subscribe for shares in Capitec Holdings (BEE shares) for Capitec Holdings to increase its black shareholding, and thereby fulfil its black economic empowerment obligations. Coral later sought to sell the BEE shares as fulfilment to a settlement agreement obligation. Coral requested Capitec Holdings’ consent to the sale of the shares on the grounds of a clause in the subscription agreement, which limited the rights of Coral to sell its shares. Capitec Holdings refused to grant Coral the consent. Coral and Ash Brook brought an urgent application to the High Court for a declaratory order stating that the withholding by Capitec Holdings of its consent for the disposal of the sale shares was unreasonable and in breach of duty of good faith required by the agreement, or alternatively in dereliction of its duty under common law of contractual good faith. The issue that lied at the heart of the appeal was, was Capitec Holdings’ consent required before Coral could sell the sale shares, and if it was, did Capitec Holdings owe duties of good faith and reasonable to Coral, which Capitec Holdings breached in failing to consent to the sale? [2]

[1] 2022 (1) SA 100 (SCA)

[2] 2022 (1) SA 100 (22) SCA 107



3. KEY PRINCIPLES

The courts commenced its analysis with the provisions of the subscription agreement that had relevance for deciding whether Capitec Holdings' consent was indeed required.[3] The court cited passages from *Natal Joint Municipal Pension Fund v Endumeni Municipality* [4] which offers guidance as to how to approach the interpretation of the words used in a document. *"It is the language used, understood in the context in which it is used, and having regard to the purpose of the provision that constitutes the unitary exercise of interpretation. I would only add that the triad of text, context and purpose should not be used in a mechanical fashion. It is the relationship between the words used, the concepts expressed by those words and the place of the contested provision within the scheme of the agreement (or instrument) as a whole that constitute the enterprise by recourse to which a coherent and salient interpretation is determined. As Endumeni emphasised, citing well-known cases, '(t)he inevitable point of departure is the language of the provision itself"* [5]

Vally J, in the High Court, relied upon his minority judgment in *Atlantis Property Holdings CC v Atlantis Excel Service Station CC* (Atlantis Property) [6] as the basis upon which the doctrine of good faith required Coral to secure Capitec Holdings' consent. This judgment offered an expansive interpretation as to how the Constitutional Court had, in various judgments, recognized the principle of good faith to ensure fairness in the law of contract.[7] The SCA in Capitec did not further concern itself with the Atlantis citing that the Constitutional Court had decisively spoken in *Beadica 231 CC and Others v Trustees, Oregon Trust and Others*. [8]The four principles laid out in *Beadica* are as follows:

- Contracts freely and voluntarily entered into must be honoured and this remains central to the law of contract;
- Our common law read with the Constitution determines how the freedom to contract should be exercised;
- the scope of public policy and its application, to invalidate contract terms, should be undertaken with circumspection and only in clear cases; and
- good faith and fairness are not substantive, free-standing principles to which direct recourse may be had to decline the enforcement of a contractual term.

The SCA makes it clear that *Beadica* provides the authoritative interpretation of the cases both in the SCA and the Constitutional Court that explains the role that good faith plays in the law of contract.[9] The SCA further highlights that the concept of good faith cannot be used as a mechanism to re-engineer agreements.

The SCA found that the provision in dispute did not require Capitec Holdings' consent and that the High Court had erred in its finding, Unterhalter AJA highlighted that even if Capitec Holdings consent was required in accordance with the finding of the High Court, Capitec's ethical or moral duties according to the High Court's view did not impute a duty on Capitec Holdings to give consent to the sale. Capitec Holdings would have still enjoyed the right to either grant the consent or refuse to grant it.

[3] 2022 (1) SA 100 (22) SCA 107 para 25

[4] 2012 (4) SA 593 (SCA)

[5] 2022 (1) SA 100 (22) SCA 108 -109 para 25

[6] 2022 (1) SA 100 (22) SCA 118 para 62

[7] 2022 (1) SA 100 (22) SCA 118 para 62

[8] 2020 (5) SA 247 (CC)

[9] 2022 (1) SA 100 (22) SCA 118-119 para 64

4. CONCLUSION

In conclusion, the case of Capitec highlights that the inclusion of the duty to contract in good faith duty does not lend weight to the further terms of a contract as the doctrine of good faith is a doctrine already fundamental to our law of contract. Furthermore, consents and approvals conferred to a party, particularly, which is left to the discretion of that party, remain their right to exercise. The party's election to refuse consent does not automatically offend the public policy. It is important to draw from Capitec that the invocations of the principle of good faith cannot be used to alter the contractual rights and duties of parties to a contract. Good faith cannot be invoked to determine the terms of a contract, nor does it justify imposing a duty to give consent.

