The horizontal application theory and its influence on freedom of agreement in the law of contract – a South African perspective

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1 HORIZONTALITY, RADIATION AND PRIVATE LAW IN GENERAL

It now seems clear, when interpreting the wording of the relevant sections of the 1996 Constitution,[1] and particularly section 8,[2] in the light of the main tenets of interpretation advanced by the Constitutional Court in *Du Plessis v De Klerk*,[3] that direct horizontal application of the basic rights protected in Chapter 2 of the Constitution to private relations regulated by "private law", is possible.[4] Private law is, of course, not so "private", and that goes equally for the law of contract – certainly contract is and must be largely a private matter, but we should remind ourselves, even leaving the Bill of Rights aside for the moment, that objective values, norms and public policy play a decisive role in the creation and validity of contracts – reasonable reliance on consensus can create contractual liability and legality is a requirement for validity. Also, these limitations on private autonomy are becoming increasingly important in respect of the enforcement of validly created contractual rights[5] and the remedies for breach of contract.

Whether a right is directly enforceable in terms of the Constitution and whether a new remedy may be created in the process will of course depend on the nature of the right and of the duty imposed by the right. In this regard I suppose the *preponderant weight of the social interests* involved over the private interests at stake, will play a role. Social interests relate to rights of general application and enforceability subject to other such rights which are regarded as weightier in the circumstances, while private interests (recognised and protected by society, of course) are

1 Act 108 of 1996.
2 Also ss 36 and 39.
3 1996 3 SA 850 (CC) 876-903.
4 Cf in general Woolman and Davis 1996: 361; Cockrell 1996: 1.
5 Cf some recent articles on the topic Van der Merwe and Van Huyssteen 1995: 549; Cockrell 1997: 26.

always relative and subject to a process of balancing the interests of the individuals concerned.[6] Thus, and in the first place, if the case is a matter within the "public domain" (where social interests are dominant), direct enforceability is indicated. This approach would satisfactorily and properly provide space for the application of the limitations clause (section 36) in terms of which only social interests are considered – this test would obviously be too unsophisticated if private interests had to be balanced, considering also social interests.

Where direct enforceability is not possible because *private interests are paramount or at least indicative of the relative weight to be attached to competing social interests*, the interpretation section of the Bill of Rights (section 39) comes into play, which mandates a court, when developing the common law, to promote the spirit, purport and objects of the Bill of Rights. Section 8, by making the Bill applicable to all law and binding also the judiciary, lays the foundation, in the context of indirect horizontality, for a mandatory and overt "constitutional audit" by the court in every relevant case.[7]

There is some support for the view that this may be so even if a litigant does not bring a protected right in issue or even if the case does not strictly concern "development", that is, the extension of open-ended principles to a particular case. On the other hand, practicality and the general approach by the courts thus far that the Bill of Rights was not intended to "meddle" in every aspect of private relations, would require a party to allege and prove the relevance and applicability of a particular right.[8] However, it appears that the Constitutional Court would then be able to reassess a decision on the basis that it does not properly give effect to section 39, and refer the case back for that to be done.[9]

The main difference in substance between direct and indirect horizontality is that in the latter type of case the court must also take the private interests of the parties in the particular circumstances of the case into account and balance them, whereas in a case of direct horizontal application a rule of general applicability is formulated, subject only to limitation.[10]

2 FREEDOM OF CONTRACT

Freedom of contract as such is not expressly listed in the Bill of Rights, which may support the hierarchical argument that it is necessarily sub-

6 See the examples given below. For a discussion of the concepts of social and private interests and their relationship to each other see Van der Merwe and Van Huyssteen 1995: 560-561 and the sources cited there. Cf also *Reeves & Another v Marfield Insurance Brokers CC & Another* 1996 3 SA 766 (A) 775 where the Court seems to accept the interests approach as valid in the context of illegal agreements.

7 *Du Plessis v De Klerk* 1996 3 SA 850 (CC) 876-903; *Rivett-Carnac v Wiggens* 1997 3 SA 80 (C) 87.

8 *Knox D'Arcy Ltd v Shaw* 1996 2 SA 651 (W).

9 Cf the position in German law – Strydom 1995: 696.

10 *Knox D'Arcy Ltd v Shaw* 1996 2 SA 651 (W). Cf *Fidelity Guards Holdings (Pty) (Ltd) v Pearmain* 1997 10 BCLR 1443 (SE).

ordinate to any listed right with which it may conflict, such as the rights to freedom of trade, occupation or profession, equality, freedom of association, and access to housing. On the other hand, of course, freedom of contract is not only an expression of the basic values of autonomy, self-expression and individual growth and development (which certainly underlie, in general terms, the whole Bill of Rights[11]), but also forms the direct basis of listed rights such as some of those mentioned above. As such, freedom of contract may form the basis of private interests or social interests, depending on the circumstances.

It will thus clearly not do to take an oversimplified view of the position of freedom of contract in the context of the Bill of Rights. It would also be generally accepted that much weight still has to be attached to the many judicial pronouncements (pre- and post Bill of Rights) that freedom of contract and the concomitant principle of *pacta servanda sunt* are generally favoured by public policy.[12] Depending on the circumstances, freedom of contract remains a weighty factor in the balancing process – in a case of direct application of a protected right it could feature as a limiting factor,[13] and in a case of indirect application it would obviously have to be shown why the agreement should not have full force and effect.

However, as I will attempt to show in more detail below, it appears that the Bill of Rights will provide the impetus for a second or third new age for the law of contract in which freedom of contract and *pacta servanda sunt* will reappear in their proper perspective as part of one of the three great principles of the law of obligations –

- no one shall be unjustly enriched at the expense of another;
- damage wrongfully caused shall be compensated; and
- contractual relations shall comply with the requirements of good faith between the parties.

3 DIRECT APPLICATION OF THE BILL OF RIGHTS

The inclusion of, for example, a racially discriminating clause against subletting in a contract of lease of a theatre for the operation of which a licence from a public authority is necessary, would to my mind clearly be directly impugnable as being against the equality clause, section 9. This would be so even though the lessee had already agreed to the term, since the public and social interest in eradicating discrimination clearly outweighs the sole legitimate private interest of the lessor that his or her contract must be enforced, and moreover, the case probably falls within a broad concept of the public domain.

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11 Cf *Ryland v Edros* 1997 2 SA 690 (C) 707-709; *Knox D'Arcy Ltd v Shaw* 1996 2 SA 651 (W).

12 See e g *Sasfin v Beukes* 1989 1 SA 1 (A) 9; *Knox D'Arcy Ltd v Shaw* 1996 2 SA 651 (W). Cf also *Fidelity Guards Holdings (Pty) Ltd v Pearmain* 1997 10 BCLR 1443 (SE) 1450G where the Court regards the remarks made in this connection in the *Knox D'Arcy* case as "still apposite", that is, in terms of the 1996 Constitution.

13 Cf *Fidelity Guards Holdings (Pty) Ltd v Pearmain* 1997 10 BCLR 1443 (SE) 1450-1451.

Similarly, a term in a property development contract which purports to bind the developer not to sell stands to (for example) Seventh Day Adventists, could be directly attacked with reference to the equality clause,[14] the right to freedom of movement and residence, and the right to access to housing – there are no discernable legitimate private interests to be weighed against the overwhelming social interest in the application of the rights mentioned.

So also would a constitution of an association, for example a chess club, which is affiliated to the national body which issues national colours and which contains a sexually discriminatory clause, be directly under constitutional scrutiny – the social interest as expressed in the equality and freedom of association clauses *prima facie* override the freedom to regulate one's own affairs without interference.[15]

3.1 The application of the freedom of trade clause in the Bill of Rights

A matter which has often come before the courts, in terms of both the interim Constitution and the 1996 Constitution, is that of the application of the freedom of trade clause in the Bill of Rights.[16] The crucial question now is whether section 22 which provides that every citizen has the right to choose their trade, occupation or profession freely, has the effect that a contractual restraint of trade is unconstitutional, unless it can be proved to be acceptable in terms of the limitation clause, section 36.

Under the interim Constitution the courts have consistently, and for various reasons, decided that the current common law position should be maintained – that is, that a restraint which has properly been agreed to is *prima facie* valid, unless it is against the public policy (and thus illegal), that is, unreasonable *inter partes* or infringing the public or social interests in another way.

This approach also seems to be endorsed by the Court under the 1996 Constitution in the *Fidelity Guards*-case, at least in the earlier part of its judgement.[17] On the other hand, some commentators apparently insist that section 22 is without more applicable, either directly,[18] or indirectly,[19] subject of course to potential limitation. In the final analysis, the Court in the *Fidelity Guards*-case appears to favour direct application of the right to free trade, but argues that a reasonable restraint (that is *inter partes* and probably also from the point of view of the public interest) is (automatically?) an acceptable limitation of general application in terms of section 36.[20] Despite this, the Court shrinks from finding that a restraint is *prima facie* unconstitutional and invalid, and that the *onus* to prove

14 Cf Cockrell 1997: 48-49.
15 Cf Woolman and Davis 1996: 361.
16 S 26, now s 22.
17 *Fidelity Guards Holdings (Pty) Ltd v Pearmain* 1997 10 BCLR 1443 (SE) 1450G-I.
18 E g Davis 1996: 29-10ff.
19 Van Aswegen 1995: 66.
20 *Fidelity Guards Holdings (Pty) Ltd v Pearmain* 1997 10 BCLR 1443 (SE) 1450J-1451E.

reasonableness is consequently on the party claiming enforcement of the restraint. The approach of the Court in this case seems too robust, and not in accordance with the primary purpose of the limitations clause – private interests, which are primarily in issue in restraint cases, should not be summarily elevated to matters of public interest and general application.[21]

The answer seems to lie in the analysis put forward above, which in this context is supported by the distinction relating to the kinds of interests involved made in the leading case on contractual restrictions on freedom to trade in *Magna Alloys and Research (SA) Pty Ltd v Ellis*[22] and in the constitutional analysis conducted by van Schalkwyk J in *Knox D'Arcy Ltd v Shaw*.[23] Where the social interest in maintaining freedom of trade, occupation or profession is paramount and overrides the principle that agreements must be fulfilled, (which has at least an important private dimension) then the restraint will be unconstitutional unless it can pass the test of the limitations clause. An example of such a case could be where a partnership agreement between medical general practitioners places an area restriction on the partner leaving the partnership which would result in a serious lack of medical care in the community. In this regard the right to access to health care services (section 27) is also relevant. Where, however, no such social interests appear to be paramount, the matter is one of balancing the private interests of the contractants, that is, whether the restraint is reasonable *inter partes* considering the legitimate protectable interests of the one party, against the restrictions placed on the other. Since such a process certainly accords with the spirit, purport and objects of the Constitution, the *status quo* in the common law as set out above is maintained.[24]

4 INDIRECT APPLICATION OF THE BILL OF RIGHTS

It is probably in this field that we will see the most far-reaching and ultimately radical influence, resulting in a new perspective on the role of contractual freedom and its most relevant consequence, namely that agreements must be kept and should be enforced.

4.1 Validity of an agreement and public policy

The most obvious areas where the Constitution may indirectly impact on freedom of contract is where open-ended policy norms already exist and are already in terms of the common law decisive regarding the validity or enforceability of an agreement. Here the rule that an agreement which offends against public policy is illegal and therefore void or unenforceable is of the greatest relevance, and the influence of the Constitution has

21 Cf in general terms the analysis in *Soobramoney v Minister of Health, KwaZulu-Natal* 1998 1 SA 765 (CC).
22 1984 4 SA 874 (A).
23 1996 2 SA 651 (W) 660D, 661D.
24 *Knox D'Arcy Ltd v Shaw* 1996 2 SA 651 (W).

already been felt regarding the content and interpretation of public policy. In the case of *Ryland v Edros*[25] Farlam J decided that an agreement (a marriage by Muslim rites) in the context of a potentially polygamous marriage was not against the public policy, as is now reflected in the Constitution – in the process not applying a previous appellate decision to the contrary. *In casu* the constitutional principles of equality, tolerance and accommodation as inferred from and stated in the preamble, various sections of the Bill of Rights and postamble were cited as validating such an agreement.[26] Interestingly, in this case the Constitution did not limit but extended freedom of contract. It may of course well be that in a case like this direct application of the Bill of Rights is apposite.

4.2 Enforceability of a contract – a wider context

4.2.1 *The development of good faith*

Another, and wider, area of constitutional influence in the context of public policy and the validity or enforceability of an agreement is the possible recognition and development of a *general norm* regulating the enforceability of a concluded contract and applying to all its phases: the process of conclusion, its validity (legality) and its enforcement.[27] Very recently in a forceful separate judgement in *Eerste Nasionale Bank van Suidelike Afrika Bpk v Saayman*[28] Olivier JA placed the principle of good faith squarely within the realm of public policy in this context, as actually *being part* of public policy.[29] In this connection he found authority in, among others, *Sasfin (Pty) Ltd v Beukes*[30] where the Court applied the norm of "simple justice between man and man" when refusing to enforce a very onerous cession and suretyship which had the result of reducing Beukes to a "slave" of Sasfin.

In so far as good faith in our law of contract is understood to require, in general terms, that a contracting party, while advancing his or her own interests should also show some (reasonable?) respect for the interests of the other party, it certainly accords with the spirit, purport and objects of the Bill of Rights. As such, courts would be mandated by section 39 to develop and apply the norm, in spite of the oft-expressed judicial reluctance based on the perception that the notion of sanctity of contract is practically inviolable. Courts will always have to be mindful of the possibility of reassessment by the Constitutional Court.

Various concepts of the Constitution and the Bill of Rights might play a role in concretising the norm in the particular circumstances of the case. The right to equality comes to mind, the right to dignity, to freedom of

25 1997 2 SA 690 (C).
26 707-709.
27 See Cockrell 1997: 44-49 for a discussion of this issue in relation to the exercise of contractual powers and discretions.
28 1997 4 SA 302 (SCA).
29 408D-E.
30 1989 1 SA 1 (A).

trade, but also the more general values underlying the Bill of Rights – those of mutual respect, communality, abhorrence of subjugation in any form and the right of each individual to freedom to prosper and thrive.

4.2.2 *"Unfair" contract terms*

In cases of alleged unfair terms which, it is argued, should not be enforced, good faith would require that the one party should not be allowed to unreasonably overprotect his own interests to the unreasonable prejudice of the other, considering, for example, the commercial nature and setting of the contract, its purpose, the relationship between the parties and the circumstances surrounding its conclusion. Thus good faith could supply guidelines and give content to the norm of "simple justice between man and man" which is presently generally accepted to be a requirement of public policy when considering the legality and enforceability of an "unfair" contract – at the same time it would widen the scope of application of public policy.

Consequently, it would appear that more accommodation in respect of the enforcement of contracts is at hand. One can foresee that, in particular, the enforcement of suretyship contracts will be affected, since often (clearly not always) the circumstances surrounding their conclusion as well as their contents are inimical to good faith and the Constitution, and that duties of disclosure, explanation and consideration of the surety's interests may be placed on financial institutions.[31]

4.2.3 *Changed circumstances*

It could well be that where the terms of the contract *per se* are not markedly in imbalance, but where the enforcement of otherwise acceptable terms are, in the circumstances as they have arisen later, against the good faith (as developed under the influence of the Constitution) that a court might refuse enforcement.[32] This might be so where the risk of changed circumstances should, as a matter of reasonableness and social interest, be shifted to the other party. That could well be the case where the other party can reasonably be expected to carry the risk, for example where that party is economically better able to protect himself against the risk. An example would be the unreasonableness of calling up a mortgage loan in times of general economic depression, joblessness and high interest rates, where a particular borrower can no longer pay the instalments due to retrenchment and a steep rise in the interest rates.

4.2.4 *Rescission of a contract*

Although there is often in one case a variety of circumstances which might influence a court not to enforce the contract and which relate to and

31 Cf the German case discussed by Strydom 1995: 696. For other such cases compare also Van der Merwe and Van Huyssteen 1995: 549; *Eerste Nasionale Bank van Suidelike Afrika Bpk v Saayman* 1997 4 SA 302 (SCA).

32 This principle is not new – cf the discretion of the court in regard to specific performance, and supervening impossibility of performance.

overlap with the different phases of contract at the same time, and although theoretically it probably is ultimately not desirable to make a clear distinction between the various phases and the applicable remedies,[33] it may be practical in this context to look at the conclusion phase separately. We know that subjective consensus is only one basis of contract, reasonable reliance being the other. We know that if there is a so-called "defect of will" the contract may be rescinded. We appreciate that "defect of will" refers to wrongful conduct which unacceptably limits unfettered freedom of decision and self-determination. This must be fertile soil for the values of the Constitution to take root and influence the development of the common law. The extension of the trite grounds for rescission (misrepresentation, duress and undue influence) seem indicated – at least to cater for abuse of circumstances other than personal ascendancy or power. What particularly comes to mind here is abuse of economic necessity, abuse of dire need for housing, abuse of personal inexperience and lack of judgement, and abuse of inequality of bargaining power. This extension just described should ideally be only a first step to the development and recognition of a general principle upon which rescission may be based. The principle itself is obvious – improper conduct, conduct against the good faith, even an extended notion of wrongful conduct in a contractual setting. Call it what you wish. What of course is not so obvious is the application and boundaries of the principle. However, that should not deter the courts – they make similar judgments every day.

5 CONCLUSION

In conclusion it is probably safe to say that the new era of constitutionalism in South Africa will either directly or indirectly impact on freedom of contract – it will most often result in some limitation of the rather unfettered freedom which has enured to the benefit of the stronger party and will require that the reasonable interests of the community and of the other party be considered when concluding and enforcing a contract.

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