Determining the consequences of illegal contracts

by

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DECLARATION

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SUMMARY

This thesis investigates the consequences of illegal contracts from a comparative perspective. Illegality usually raises two questions: to what extent may the contract still be enforced and under what circumstances may a plaintiff recover a performance rendered under the contract.

When confronted with these questions, South African courts typically resort to constructs such as the maxims *ex turpi causa non oritur actio* and *in pari delicto potior est conditio defendentis.* These maxims respectively express the propositions that an illegal contract may not be enforced and that a plaintiff who is tainted by illegality may not obtain restitution of any performance rendered under the contract. The problem with these maxims is that they tend to divert attention away from other policy considerations that may also be important. In addition, it is not clear why South African courts find illegal contracts to be void in some cases and valid but unenforceable in others.

In search of a more convincing approach to illegal contracts, the thesis therefore investigates how foreign jurisdictions determine the consequences of illegality. The comparative overview reveals that foreign jurisdictions generally aim to give effect to the same kind of policies when determining the consequences of illegality, although they employ different methods. Some apply strict rules with a limited number of exceptions while others give courts a discretion to determine the consequences in a particular case with reference to a list of policy considerations.

These policy considerations are studied in more detail by analysing three particularly challenging scenarios from a comparative perspective – illegal consumer loans, illegal employment contracts and illegal work performed by contractors in the construction industry.

From these analyses the thesis concludes by developing several claims. The first claim is that the solution to any illegality problem ultimately amounts to a balancing of various factors, irrespective of whether the illegality derives from legislation or public policy. Second, it is argued that the most satisfactory method for determining the consequences of illegal contracts is to give courts a discretion that must be exercised with reference to a range of policy considerations. And finally, it is concluded that South Africa should discard references to the *ex turpi* and *par delictum* maxims and adopt a more flexible approach to determining the consequences of illegality.

OPSOMMING

Hierdie tesis ondersoek die gevolge van ongeoorloofde kontrakte vanuit ’n regsvergelykende perspektief. Ongeoorloofdheid bring gewoonlik twee vrae na vore: tot watter mate die kontrak nog afgedwing mag word, en onder watter omstandighede ’n eiser ’n prestasie wat ingevolge die kontrak gelewer is, mag terugvorder.

Wanneer Suid-Afrikaanse howe met hierdie vrae te doen kry, word daar gewoonlik verwys na konstruksies soos die stelreëls *ex turpi causa non oritur actio* en *in pari delicto potior est conditio defendentis*. Hierdie stelreëls bepaal onderskeidelik dat ’n ongeoorloofde kontrak nie afgedwing mag word nie en dat ’n eiser wat self met ongeoorloofdheid besmet is, nie restitusie van ’n prestasie wat in terme van die kontrak gelewer is, mag vorder nie. Die probleem met hierdie stelreëls is dat hulle die aandag aflei van ander beleidsoorwegings wat ook belangrik mag wees. Verder is dit ook nie duidelik waarom die Suid-Afrikaanse howe soms ’n ongeoorloofde kontrak as nietig en soms as geldig maar onafdwingbaar bestempel nie.

In die soeke na ’n meer oortuigende benadering tot ongeoorloofde kontrakte ondersoek die tesis hoe ander regstelsels te werk gaan. Uit die regsvergelykende oorsig blyk dit dat hierdie stelsels in die algemeen poog om uitdrukking te gee aan soortgelyke beleidsoorwegings wanneer hulle die gevolge van ongeoorloofdheid bepaal. Hulle gebruik egter verskillende metodes vir hierdie doel. Sommige stelsels het streng reëls met ’n beperkte aantal uitsonderings, terwyl ander aan die howe ’n diskresie verleen om die gevolge van ongeoorloofdheid met verwysing na ’n lys beleidsfaktore te bepaal.

Hierdie beleidsfaktore word in meer detail behandel deur die volgende drie besonder uitdagende feitepatrone vanuit ’n regsvergelykende perspektief te bestudeer: ongeoorloofde kredietooreenkomste met verbruikers, onwettige dienskontrakte en onwettige ooreenkomste met kontrakteurs in die boubedryf.

Die tesis sluit af deur verskeie normatiewe stellings vanuit die regsvergelykende analises te ontwikkel. Eerstens word geargumenteer dat die oplossing vir enige ongeoorloofdheidsprobleem uiteindelik daarop neerkom dat verskeie faktore teen mekaar opgeweeg moet word. Dit is die geval ongeag of die ongeoorloofdheid voortspruit uit ’n wetsverbod of openbare beleid. Verder word aangevoer dat die mees bevredigende instrument om die gevolge van ongeoorloofde kontrakte te bepaal 'n regterlike diskresie is wat met inagneming van ’n reeks beleidsoorwegings uitgeoefen moet word. Ten slotte word aanbeveel dat die Suid-Afrikaanse reg verwysings na die

ex turpi- en *par delictum*-stelreëls moet laat vaar en eerder ’n buigsamer benadering moet volg om die gevolge van ongeoorloofdheid te bepaal.

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ABBREVIATIONS

BGB	*Bürgerliches Gesetzbuch* (German Civil Code)
BGH	*Bundesgerichtshof* (Germany)
BLA	Builders Licensing Act 1971 (New South Wales, Australia)
Can J Law Jurisprud	*Canadian Journal of Law and Jurisprudence*
CCA	Consumer Credit Act 1974 (United Kingdom)
CCLA	Contract and Commercial Law Act 5 of 2017
CLJ	*Cambridge Law Journal*
DCFR	Draft Common Frame of Reference
ECHR	European Convention on Human Rights
Edin LR	*Edinburgh Law Review*
ERPL	*European Review of Private Law*
HKK	*Historisch-kritischer Kommentar zum BGB*
HRA	Human Rights Act 1988 (United Kingdom)
ICA	Illegal Contracts Act 1970 (New Zealand)
ICLQ	*International and Comparative Law Quarterly*
ILJ	*Industrial Law Journal*
LQR	*Law Quarterly Review*
LS	*Legal Studies*
MLR	*Modern Law Review*
MüKo	*Münchener Kommentar zum Bürgerlichen Gesetzbuch*
NCA	National Credit Act 34 of 2005 (South Africa)
NJW	*Neue Juristische Wochenschrift*
NZULR	*New Zealand Universities Law Review*
PECL	Principles of European Contract Law
PELJ	*Potchefstroom Electronic Law Journal*
PICC	UNIDROIT Principles of International Commercial Contracts
RabelsZ	*Rabels Zeitschrift für ausländisches und internationales Privatrecht*
Rev dr unif	*Revue de droit uniforme*
RLR	*Restitution Law Review*
SALJ	*South African Law Journal*
SA Merc LJ	*South African Mercantile Law Journal*
SchwarzArbG	*Schwarzarbeitgesetz* 01 08 2004 (Germany)

SLT	Scots Law Times
Stell LR	*Stellenbosch Law Review*
Theoretical Inq L	*Theoretical Inquiries in Law*
THRHR	*Tydskrif vir Hedendaagse Romeins-Hollandse Reg*
TSAR	*Tydskrif vir die Suid-Afrikaanse Reg*
ZEuP	*Zeitschrift für Europäisches Privatrecht*

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CHAPTER 1: INTRODUCTION

1 1 Statement of the problem

Contracts that infringe legal rules may attract a variety of consequences in South African law.[1] While these contracts are typically void, they are sometimes treated as valid but unenforceable.[2] It is not clear why the courts draw this distinction. For example, MacQueen and Cockrell remark that "it is impossible to discern any underlying rationality in the courts' decisions in this respect."[3] One broad justification appears to be that the more serious the legal infringement, the more important it is for the law to require a result of voidness; conversely, where the infringement is not sufficiently serious, the less serious consequence of mere unenforceability, but not invalidity, should follow.[4] However, this explanation may be too simplistic. As will be indicated below, finding that a contract is valid but unenforceable may bring about harsher consequences than finding that it is void.[5] The uncertainty surrounding this differentiation conceals a broader and more fundamental question: what determines the consequences of an illegal contract? The aim of this thesis is to search for an answer.

Two aspects of the research question should be expanded upon. The first is what is meant by 'consequences' of an illegal contract. The taint of illegality in a contract generally raises one of three questions. The first is whether or to what extent the contract may still be enforced. In other words, are any contractual remedies, such as specific performance, still available? The second question is whether any value that has been transferred under the tainted contract may be recovered, typically by means of a claim in unjustified enrichment. Finally, if only some terms of the contract are illegal, the question arises whether the validity of the contract may be preserved by severing those terms. Severability is not considered in this thesis, because it tends to stand apart from the other two consequences. Accordingly, the focus will be on the

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1 See generally S van der Merwe & LF van Huyssteen "The Force of Agreements: Valid, Void, Voidable, Unenforceable?" (1995) 58 *THRHR* 549.

2 *Cool Ideas 1186 CC v Hubbard* 2014 4 SA 474 (CC); *Gibson v Van der Walt* 1952 1 SA 262 (A); *Magna Alloys and Research (Pty) Ltd v Ellis* 1984 4 SA 874 (A) 895C-E.

3 H MacQueen & A Cockrell "Illegal Contracts" in R Zimmermann, D Visser & K Reid (eds) *Mixed Legal Systems in Comparative Perspective: Property and Obligations in Scotland and South Africa* (2004) 143 163.

4 *Gibson v Van der Walt* 1952 1 SA 262 (A) 268H; T Floyd "Legality" in D Hutchison & C Pretorius (eds) *The Law of Contract in South Africa* 3 ed (2017) 181 181-182

5 See 2 5 2 below.

questions of enforceability and restitution, since they often interact in complex ways.

The second aspect relates to the word 'what' in the research question. In South Africa and several other jurisdictions, much of the controversy about illegality has revolved around the application of two civil-law maxims.[6] The first is *ex turpi causa non oritur actio* which roughly means that no action arises from a cause tainted by turpitude. The scope of this maxim is not the same in every jurisdiction, but in South African law it provides that a contract tainted by illegality may not be enforced.[7] The second maxim is *in pari delicto potior est conditio defendentis,* which provides that where both parties are tainted by wrongdoing, the position of the defendant is stronger.[8] In practical terms this is taken to mean that a plaintiff who has rendered performance under an illegal contract and is tainted by the illegality may not recover the performance with a claim in unjustified enrichment.[9]

These maxims express certain policy preferences, such as the idea that the rule of law should not be undermined by enforcing illegal contracts and that the court should not assist a plaintiff who comes to court without clean hands. The problem is that a strict application of these principles may lead to unjust results, since it diverts attention from other factors that may be relevant and require a different result, such as the seriousness of the infringement or whether the infringement was intentional.

As the web of legislation that regulates modern commercial life continues to grow, so too do the potential scenarios of illegality. In view of this increasing complexity, a more-context sensitive approach to illegality, which takes in account a wider variety of policy considerations, is required. The 'what' in the research question therefore refers to these policy considerations. What are they and how do they function in order to determine the consequences of illegality?

1 2 Methodology and overview of chapters

The methodology adopted in this thesis is to investigate the consequences of illegality from a comparative perspective. Illegality is a particularly apt subject for comparative

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6 The ideas expressed by these maxims have also been influential in the common-law tradition; see *Holman v Johnson* (1775) 1 Cowp. 341 343.

7 *National Credit Regulator v Opperman* 2013 2 SA 1 (CC) para 14.

8 In some other jurisdictions such as Germany, the maxim is known as the *in pari turpitudine* rule; G Dannemann *The German Law of Unjustified Enrichment and Restitution: A Comparative Introduction* (2009) 80.

9 *Absa Bank Ltd v Moore* 2017 1 SA 255 (CC) para 47.

study. Commenting on the difficulty of drafting model rules for illegality, Meier remarked:

> "[T]here are considerable differences in the national laws, in particular between the civil and the common law, which have not yet been the object of thorough comparative research."[10]

Legal research often proceeds by outlining a theory and then applying it to a some problem in order to generate new insight. However, the problems that arise from illegal contracts are complex and involves an almost infinite amount of variables, which makes it a difficult area to theorise. This thesis proposes to do the opposite. It conducts a close analysis of the authorities in the first few chapters and then develops a number of theoretical propositions in light of that analysis in the final chapter.

Accordingly, the following structure is adopted. Chapter 2 analyses the consequences of illegal contracts in South African law in order to set the scene for a comparative investigation. After critically reviewing the existing literature on why some illegal contracts are merely unenforceable as opposed to void, the chapter considers several ways in which illegality may be circumvented, such as through statutory interpretation, unjustified enrichment claims, collateral contracts, alternative methods of terminating obligations such as set-off, and estoppel. Finally some parallels are drawn between illegality in the common law of contract and illegality in administrative law.

Chapter 3 investigates the approaches to illegality adopted by foreign legal systems. The jurisdictions of Germany, England, Scotland and New Zealand have been selected as the main subjects for comparison, although reference will also be made at times to relevant cases from other common-law countries such as Canada, Australia and Singapore.

Germany is one of the most prominent jurisdictions in Europe and a good representative of the civilian tradition. The uncodified civil-law sources that formed the foundation of the German Civil Code ("BGB") also underlie much of South African private law. These shared historical roots accordingly make Germany an apt candidate for comparison with South Africa.

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[10] S Meier "Illegality" in N Jansen & R Zimmermann (eds) *Commentaries on European Contract Laws* (2018) 1889. See also D Visser *Unjustified Enrichment* (2008) 424 n 50. The last detailed comparative study of illegal contracts in South African law was by MacQueen and Cockrell and dates back more than fifteen years; MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems in Comparative Perspective* 143.

The UK Supreme Court recently reconsidered the English approach to illegality in *Patel v Mirza*.[11] The decision has also generated a wealth of literature that represents the latest thinking on illegality in the common-law tradition.[12]

Legal comparison between Scotland and South Africa is also well-established, in part because they share the unusual feature of drawing on uncodified civil-law sources, and also because of their mixed heritage.[13] Like South Africa, there is some debate about whether an illegal contract is void or simply unenforceable in Scotland.[14] In addition, some of the prominent Scottish cases on illegality have enjoyed the attention of South African courts.[15]

The final jurisdiction to be considered is New Zealand. Unlike other Common-Law jurisdictions that mostly retained the principles of English law in this area, New Zealand has passed legislation to deal with the problems raised by illegal contracts.[16] Courts are given a wide discretion by the Illegal Contracts Act of 1970 to determine the consequences of illegality in a particular case.[17] This approach is quite unusual and therefore makes for an instructive case study.

Finally attention is paid to the approaches adopted in some supranational model instruments, in particular the Principles of European Contract Law.[18] Although none of these instruments are legally binding in any jurisdiction, they are the product of significant comparative scholarship and thus contain useful insights.

The comparative overview in Chapter 3 will consider whether foreign jurisdictions also experience difficulties in determining the consequences of illegal contracts, and what policy considerations they take into account when dealing with illegality problems. Chapter 4 in turn draws on these considerations in analysing three challenging fact-patterns through a comparative lens. The first scenario concerns the consequences of a loan that infringes credit legislation. In particular, the question is

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11 [2016] UKSC 42.

12 See for example S Green & A Bogg (eds) *Illegality after* Patel v Mirza (2018).

13 R Zimmermann "'Double Cross': Comparing Scots and South African Law" in R Zimmermann, D Visser & K Reid (eds) *Mixed Legal Systems in Comparative Perspective: Property and Obligations in Scotland and South Africa* (2004) 25-31.

14 MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems in Comparative Perspective* 162.

15 *Jajbhay v Cassim* 1939 AD 537 558; *Hubbard v Cool Ideas 1186 CC* 2013 5 SA 112 (SCA) para 25.

16 It has been suggested that South African law should be reformed in line with New Zealand's approach; LE Trakman "The Effect of Illegality in South African Law - A Doctrinal and Comparative Study" (1977) 94 *SALJ* 468 482.

17 The legislation has now been consolidated into the Contract and Commercial Law Act 5 of 2017.

18 O Lando, E Clive, A Prüm & R Zimmermann (eds) *Principles of European Contract Law* Part III (2003).

whether the lender may recover any money from the borrower despite the illegality. The second scenario deals with the position of an employment contract that has been tainted with illegality, and whether any remedies are available to the employee. Finally, attention is paid to the scenario of a contractor who performed work contrary to the applicable laws or regulations. In this scenario the question is typically whether the contractor may enforce the contract, or if not, obtain any restitution for the value that has been transferred to the client.

Chapter 5 synthesises the findings of the previous chapters to develop a proposal for how the consequences of illegality should best be determined. In this regard it is enquired to what extent the solution may lie in discretionary approach that balances various, and sometimes competing, factors. The thesis then concludes by making some recommendations on how South African law may be improved.

CHAPTER 2: THE CONSEQUENCES OF ILLEGALITY IN SOUTH AFRICAN LAW

2 1 Introduction

This chapter analyses the impact of illegality on contracts in South African law. The purpose of the chapter is to explore the problem this thesis aims to address in more detail as well as to set the scene for a comparative study.

As a general proposition, the question of whether a contract is illegal must be distinguished from the question of what consequences should follow once illegality is established. For this reason, it is necessary to consider first how the legality of a contract is determined.

Contracts that violate legal rules are typically divided into to one of two categories. The first category is statutory illegality, meaning contracts that contravene rules contained in statutory provisions. The other category is common-law illegality, which refers to contracts that infringe rules contained in the common law.[1] This kind of illegality was historically a minefield because of the way in which Roman and Roman-Dutch law developed. The Romans were casuistically minded lawyers more interested in whether an action would lie in a particular case than in theorising why an action should be available and what the implications would be.[2] Discerning general principles is therefore a challenge. Roman-Dutch lawyers in turn drew complicated distinctions between concepts such as public interest, public policy and the *boni mores*.[3]

Fortunately the matter was significantly simplified in the latter decades of the twentieth century when the courts accepted that these concepts may all be consolidated under the notion of public policy.[4] Thus on an abstract level, the standard for determining legality under the common law today is whether a particular contract is contrary to public policy.[5] The content of public policy is in turn rooted in

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1 See the examples of common-law illegality listed in H MacQueen & A Cockrell “Illegal Contracts” in R Zimmermann, D Visser & K Reid (eds) *Mixed Legal Systems in Comparative Perspective: Property and Obligations in Scotland and South Africa* (2004) 143 148-149. Typical cases include contracts to commit a crime or delict, certain restraints of trade or contracts aimed at defrauding creditors, to name a few.

2 See generally R Zimmermann *The Law of Obligations: Roman Foundations of the Civilian Tradition* (1996) 679; 697-715.

3 LE Trakman “The Effect of Illegality in South African Law - A Doctrinal and Comparative Study" (1997) 94 *SALJ* 327 238; LF van Huyssteen, GF Lubbe, MFB Reinecke & JE du Plessis *Contract - General Principles* 6 ed (2020) 211.

4 *Sasfin (Pty) Ltd v Beukes* 1989 1 SA 1 (A) 7-9; *Brummer v Gorfil Brothers Investments (Pty) Ltd* 1999 3 SA 389 (SCA) 402H-J; J du Plessis “Some Thoughts on the Consequences of Illegal Contracts” (2021) *Acta Juridica* 177 178.

5 *Barkhuizen v Napier* 2007 5 SA 323 (CC) para 59.

constitutional norms and values.[6] Whether a contract infringes a particular statutory provision is a question of interpretation.[7] The answer requires construction of both the particular statutory provision as well as the scope of the contract.[8] Once it has been established that the contract does infringe the provision, the next question is what consequences should follow, particularly when the statute is silent on the matter. This issue is discussed below.[9] The point made here is only that the question of whether a contract is illegal must be determined first before it can be considered what consequences should arise if illegality has indeed been established.

2 2 Terminological issues surrounding illegality

Once it is established that a contract infringes a legal rule, the next issue is to determine what consequences ought to follow. Describing these consequences can be rather challenging because the concept of an illegal contract is used inconsistently by authors and the courts.[10] It is therefore necessary to clarify the applicable terminology.

A defect in the formation of a contract can lead to different consequences, describable by terms such as valid, void, voidable or unenforceable.[11] The meanings of valid and void are uncontroversial. A valid contract is one that creates legal obligations, while a void one creates no such obligations.[12] In some cases, a contract may be voidable instead, for example where consent has been obtained by improper means.[13] In these instances the contract is valid but may be rescinded by the contracting party who is the victim of the improper conduct, following which the

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6 *Barkhuizen v Napier* 2007 5 SA 323 (CC) para 28. The impact of the Constitution on the common law in this area remains a contested issue; see F Botha "New Developments in the Quest for Fairness in the South African Law of Contract" (2021) 2 *ZEuP* 445.

7 For better or worse the approaches to interpreting statutes and contracts have been merged into a single method in *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 4 SA 593 (SCA) para 18, cited with approval by the Constitutional Court in *Trinity Asset Management (Pty) Limited v Grindstone Investments 132 (Pty) Limited* 2018 1 SA 94 (CC) para 52. The minority judgment in *CSARS v Daikin Air Conditioning* 80 SATC 330 para 29-34 expressed criticism of the proposition that there is no meaningful difference between interpreting statutes or contracts, although these remarks were clearly *obiter.* See generally F Myburgh "Thomas Kuhn's *Structure of Scientific Revolutions*, Paradigm Shifts, and Crises: Analysing Recent Changes in the Approach to Contractual Interpretation in South African Law" (2017) 3 *SALJ* 514.

8 Van Huyssteen et al *Contract* 215; *Moser v Milton* 1945 AD 517.

9 See 2 5 below.

10 Du Plessis (2021) *Acta Juridica* 179

11 S van der Merwe & LF van Huyssteen "The Force of Agreements: Valid, Void, Voidable, Unenforceable?" (1995) 58 *THRHR* 549 551.

12 Van Huyssteen et al *Contract* 223.

13 See GF Lubbe "Voidable Contracts" in R Zimmermann & D Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 261.

contract is rendered void. Both parties may then be required to return any benefits they received under the contract to each other.[14] Finally there is the concept of unenforceability. A contract that is unenforceable means that no action can be founded on it.[15]

With these distinctions in mind, we can consider the different meanings ascribed to the notion of an illegal contract. It has been argued that at least two approaches may be distinguished in this respect – a narrow one and a wide one.[16] Both approaches accept that we are concerned with a contract that infringes some legal rule, irrespective of whether that rule is found in legislation or the common law. What the two approaches differ on is which rule-infringing contracts should be included under the concept of an illegal contract.

Under the narrow approach, legality is regarded as a necessary condition for the validity of a contract.[17] In other words, an illegal contract is invariably void *ab initio*. Under the wide approach, by contrast, an illegal contract may include rule-infringing contracts that are void as well as ones that are not void but merely unenforceable for reasons of public policy.[18]

The difference may be illustrated by the case of *Dodd v Hadley,* which concerned a claim for the payment of money pursuant to a wager staked on a horse-race.[19] The defendant argued that the wagering contract was *contra bonos mores* and therefore illegal and unenforceable. However, consistent with the narrow approach, Innes CJ described the transaction as "not illegal, or *per se* immoral" but that "our courts of law, for reasons of public policy, will not enforce wagers."[20] The wide approach, by contrast, would characterise this transaction as illegal. It is not necessary to express a preference for one approach over the other as long as the difference in usage is kept

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[14] D Hutchison "Improperly Obtained Consensus" in D Hutchison & C Pretorius (eds) *The Law of Contract in South Africa* 3 ed (2017) 117 118. There are exceptions to the rule that benefits obtained under a rescinded contract must be returned; see *Extel Industrial (Pty) Ltd v Crown Mills (Pty) Ltd* 1999 2 SA 719 (SCA) 731.

[15] T Floyd "Legality" in D Hutchison & C Pretorius (eds) *The Law of Contract in South Africa* 3 ed (2017) *The Law of Contract* 181 201.

[16] Van der Merwe & Van Huyssteen (1995) *THRHR* 559; Du Plessis (2021) *Acta Juridica* 179; D Visser *Unjustified Enrichment* (2008) 242.

[17] *National Credit Regulator v Opperman* 2013 2 SA 1 (CC) para 14; Du Plessis (2021) *Acta Juridica* 179-180; JC de Wet & AH van Wyk *Kontraktereg en Handelsreg* 5 ed (1992) 89-90.

[18] Early support for the wide approach is found in Aquilius "Immorality and Illegality in Contract" (1941) 58 *SALJ* 337 344. See also Van Huyssteen et al *Contract* 209; MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems in Comparative Perspective* 143.

[19] 1905 TS 439.

[20] 442. See also *Gibson v Van der Walt* 1952 1 SA 262 (A).

in mind when analysing the authorities.[21] A convenient way to avoid confusion is to define the term without reference to particular legal consequences. In other words, the term "illegal contract" may be used to refer generally to any contract which infringes some legal rule.

2 3 Void or valid but unenforceable?

Having considered some basic features of illegality, we are now in a position to explore a particular kind of illegal contract in more detail, namely contracts that are valid but unenforceable. Wagers, such as the transaction in *Dodd v Hadley*, are typical cases that the courts traditionally treat in this way, but they are by no means the only examples.[22] For instance, in *Magna Alloys and Research (SA) (Pty) Ltd v Ellis* ("*Magna Alloys"*), Rabie CJ said the following about the status of certain agreements in restraint of trade:

> "An agreement which places a restraint on a party's freedom to trade is *not a void agreement*, but one that *is unenforceable when it is in conflict with the public interest*. The important question is therefore not whether an agreement of this nature is void *ab initio,* but whether it is an agreement which the court, measured against the requirements of the public interest, should not enforce." [emphasis added][23]

Thus, a restraint of trade agreement found to be unreasonable is still valid but cannot be enforced.

Contracts concluded by unassisted minors may generate similar consequences. A minor is not bound to such a contract unless it has been ratified by the minor's parent or legal guardian or by the minor upon attaining the age of majority.[24] However, a minor who is willing to perform his or her side of the bargain can enforce the contract against the other party.[25] The other party may also have an enrichment claim against the minor.[26] These cases are traditionally not regarded as instances of illegality, even though this peculiar legal position arises from non-compliance with a common-law rule. Instead, these cases are considered to fall under the element of contractual capacity.

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21 Du Plessis (2021) *Acta Juridica* 181.

22 The National Gambling Act 7 of 2004 now regulates wagers and reserves a less prominent role for the common law. However, s 16(1) provides that the common law still applies to debts arising from unlicensed gambling activities. See GB Bradfield & RH Christie *Christie's Law of Contract in South Africa* (2016) 7 ed 439-444.

23 1984 (4) SA 874 (A) 895C-E (own translation).

24 *Edelstein v Edelstein NO* 1952 3 SA 1 (A) 11.

25 B Kuschke "Contractual Capacity" in D Hutchison & C Pretorius (eds) *The Law of Contract in South Africa* 3 ed (2017) 153 157.

26 J du Plessis *The South African Law of Unjustified Enrichment* (2012) 81.

The phenomenon of valid but unenforceable contracts is also not limited to the common law. Courts have found certain illegal contracts to be valid but unenforceable in cases where the contract in question infringed a statutory provision. Litigation on this point typically arises in the context of statutory provisions that prohibit someone in a regulated profession from receiving consideration if they have not complied with certain requirements imposed by the legislation. Thus, in *Cool Ideas 1186 CC v Hubbard* ("*Cool Ideas"*) the court had to consider the impact of a home builder's failure to register with the National Home Builders Registration Council on its ability to enforce an arbitration award granted in its favour.[27] The court held that the purpose of the legislation in question, the Housing Consumers Protection Measures Act 95 of 1998 ("Housing Protection Act"), was to protect consumers. It found that the best way to achieve this purpose would be for the building contract between the parties to remain valid, but that the home builder's claim could nevertheless not be sustained. In other words, the contract was valid, but could not be enforced by the home builder. This case raises complex issues to which we shall return.[28] At this stage the point is only that the differentiation between voidness and unenforceability occurs both in the context of statutory and common-law illegality.[29]

There is considerable uncertainty in South African law around this issue. It is hard to find any thorough justification for why contracts that infringe legal rules are void in some cases but merely unenforceable in others. The finding in *Cool Ideas* was not unanimous and resulted from a particular interpretation of the relevant statute.[30] The passage in *Magna Alloys* cited above does not provide a clear justification either.

Sutherland suggests that the justification in restraint of trade cases can be traced back to a remark by Aquilius.[31] The argument is that a contract which is contrary to public policy may be valid but unenforceable because to enforce it would be detrimental to the interests of the community, despite the fact that the performance

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27 2014 4 SA 474 (CC). See also *Taljaard v Botha Properties* 2008 6 SA 207 (SCA).

28 See 2 6 below.

29 It is therefore strange that the chapter by Floyd "Legality" in *The Law of Contract* 187-189 deals with statutory illegality under the heading of illegal contracts that are void.

30 See 2 6 below; M Wallis "The Common Law's *Cool Ideas* for Dealing with Ms Hubbard" (2015) 132 *SALJ* 940 961; Du Plessis (2021) *Acta Juridica* 197; JC Sonnekus *Unjustified Enrichment in South African Law* 2 ed (2017) 261.

31 PJ Sutherland *The Restraint of Trade Doctrine in England, Scotland and South Africa* PhD thesis, University of Edinburgh (1997) 268-269, citing *National Chemsearch SA (Pty) Ltd v Borrowman* 1979 3 SA 1092 (T) 1107 and *Allied Electric (Pty) Ltd v Meyer* 1979 4 SA 325 (W) 330.

itself is not *per se* illegal or immoral.[32] However, as Sutherland argues, Aquilius was not purporting to state a general theory, and his use of the term unenforceable was insignificant in the context.[33]

A potentially more promising explanation may be that it does not necessarily follow from a failure to enforce the restraint in one context that it could not be enforced in another.[34] For example, if a restraint is placed on a former employee, it could be that the agreement is unenforceable if the former employee starts a business that does not seriously threaten the covenantee. However, if at a later stage the former employee joins a major competitor of the covenantee, it may be appropriate for the restraint to be enforced in that context. If the contract is declared void this would not be possible.

On the other hand, if the agreement is unenforceable as opposed to void, it might suggest that the covenantee cannot recover any money it paid in return for the restraint with an enrichment claim because there is technically still a legal basis for the transfer.[35] This kind of result might be justified on the basis that the restraint could still be enforced at a later stage, so the money continues to serve as a counter performance for the covenantor to undertake that risk. However, if the restraint is so oppressive that it will clearly never be enforceable, it is less clear why the covenantor should be able to retain the payment. It might in fact be more appropriate to declare the restraint void in these circumstances. It is not clear whether the court in *Magna Alloys* had any of these permutations in mind when it held that the restraints are unenforceable rather than void. Ultimately a more flexible approach to determining the consequences restraint of trade agreements might be necessary to take account of these variables.[36]

Sometimes rule-infringing contracts held to be valid but unenforceable are categorised as natural obligations.[37] Natural obligations are generally understood to be unenforceable but still capable of being performed.[38] They form a valid legal basis

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32 Aquilius (1941) *SALJ* 346.
33 Sutherland *The Restraint of Trade Doctrine* 269.
34 Visser *Unjustified Enrichment* 433; Van Huyssteen et al *Contract* 252.
35 Visser suggests that an enrichment claim should be principle be available in this kind of scenario, but that the appropriate action is not the *condictio ob turpem vel iniustam causam*; Visser *Unjustified Enrichment* 433. See further *Council for Medical Schemes v Liberty Medical Scheme* [2013] 3 All SA 508 (GNP) para 46.
36 See 5 3 below.
37 See generally P van Warmelo "Naturalis Obligatio" in Q de Wet (ed) *Huldigingsbundel aangebied aan Professor Daniel Pont op sy vyf-en-sewentigste verjaarsdag* 410; K Willems *De Natuurlijke Verbintenis* PhD thesis, KU Leuven (2011).
38 Zimmermann *Obligations* 7.

that excludes the possibility of an enrichment claim.[39] Natural obligations also display certain other features that are similar to civil obligations. Thus, a natural obligation is said to be capable of being set-off against another debt, novated or secured by a pledge or suretyship.[40]

Some authors such as Voet also distinguish between different kinds of natural obligations.[41] If the obligation displays all the features described above, it is a so-called *obligatio naturalis plena*, in other words a natural obligation in the complete sense.[42] By contrast, an *obligatio minus plena* is based merely on a party's sense of honour and has only some or even none of the above-mentioned features, depending on the scenario. This distinction is largely of historical interest, but it did assume some importance in litigation on the status of gambling debts in the common law.[43]

The concept of a natural obligation must, however, be treated with caution. Van Warmelo, after examining the Roman and Roman-Dutch authorities on the point, argues that the concept no longer serves any useful function in South African law and that the time has come for it to be discarded.[44] This is because the concept is not clearly demarcated and has in any event been relegated to the fringes of South African law by the courts.[45] Applying it to legal arrangements that display only some of the features of a civil obligation serves only to cause confusion.[46]

This conclusion also holds in the context of illegality. It would be fallacious to determine the consequences that should follow from contracts that are valid but unenforceable due to illegality by asking whether they can be classified as natural obligations.[47] Such an approach loses sight of the relevant normative considerations for determining whether such a classification is at all desirable.

The standard textbooks on contract law do not give clear answers either. The authors of the newest edition of *Contract - General Principles* lament the fact that no clear explanation for this differentiation has been provided by the courts, but go no further than suggesting that a greater degree of illegality is required for a contract to

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39 7.
40 Van Huyssteen et al *Contract* 6; Voet 44 7 3. See also Van Warmelo "Naturalis Obligatio" in *Huldigingsbundel Pont* 410.
41 Voet 44 7 3.
42 Van Warmelo "Naturalis Obligatio" in *Huldigingsbundel Pont* 426.
43 *Gibson v Van der Walt* 1952 (1) SA 262 (A) 268; see 2 7 and 2 8 below.
44 Van Warmelo "Naturalis Obligatio" in *Huldigingsbundel Pont* 432.
45 432.
46 432.
47 Van Huyssteen et al *Contract* 233. See 2 8 2 below.

be void than for a contract that is merely unenforceable.[48] Bradfield and Christie largely avoid the issue by describing the general consequence of illegality only as unenforceability.[49]

The explanation which appears to enjoy the most support is a paper by Van der Merwe and Van Huyssteen.[50] Their argument goes as follows. The basis of illegality lies in the idea that a legal order aims to protect and balance certain interests. These interests can be divided into individual and social interests. That is, interests of people in their personal capacity versus the interests which concern society as a whole or at least certain sectors of society.

Why there is a differentiation in the juristic force of agreements can then be explained with reference to this distinction. An agreement is void if it primarily conflicts with social interests. For example, a contract to commit a serious crime is void. So too is a contract which undermines the administration of justice. The authors acknowledge that in these and many other instances there may be some overlap between social and individual interests, but they maintain that in these instances the impact on individual interests is on a secondary level. In other words, the impact is *primarily* on social interests when a contract is void due to illegality. However, when a contract is valid but merely unenforceable as a result of illegality, it is because individual interests are the primary concern. Again, such agreements may also affect social interests, but it does so on a secondary level that does not justify voidness as the consequence.
While this position appears to be attractive at first glance, a deeper reflection reveals that the distinction between individual and social interests is not clear enough to serve a meaningful purpose. The overlap between the two categories seems to be greater than the authors are willing to admit. As we shall see presently, just about any interest may be classified as either individual or social, depending on which option is more convenient in the circumstances. The point can be illustrated with reference to three types of contracts: restraint of trade agreements, wagers and contracts that implicate considerations of fairness.

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48 224.

49 Bradfield & Christie *Christie's Law of Contract* 454.

50 Van der Merwe & Van Huyssteen (1995) *THRHR* 548, cited with apparent approval in *Reeves v Marfield Insurance Brokers (Pty) Ltd* 1996 3 SA 766 (SCA) 775F; see also Floyd "Legality" in *The Law of Contract in South Africa* 202; Van Huyssteen et al *Contract* 226. MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems in Comparative Perspective* n 111 describe the article as "an attempt to impose some rationality in this area of the law."

Van der Merwe and Van Huyssteen correctly identify sanctity of contract and the freedom to be economically active as the two main interests at stake in the adjudication of a restraint of trade agreement.[51] Freedom and sanctity of contract must be weighed against the freedom to be economically active. Both of these, they argue, are generally considered social interests. However, in a case where a restraint of trade agreement is held to be unenforceable "the individual interests which are taken into account in terms of public policy are *obviously* placed in the foreground and given greater weight than the social interests involved" [emphasis added].[52] Then immediately after this passage, they describe freedom and sanctity of contract as "first and foremost an expression of principal individual interests regarding contracts."[53] Even if we accept that the two interests at stake in this context may be either individual or social depending on the context, it adds nothing to the analysis to simply assert them as one or the other without providing reasons. To say that it is obviously the case is no justification at all.

The legal position on wagers and gambling agreements also offers little support. As we have seen above, some debts arising from gambling are neither immoral nor illegal, but nevertheless objectionable to such an extent that they will not be enforced by a court.[54] The authors assert that gambling debts are objectionable from the perspective of individual interests, which in turn explains why they are unenforceable. However, they do not identify what these individual interests are. The claim therefore amounts to nothing more than an assertion, lacking proper justification.

The final category concerns contracts that are challenged on the basis that they are so unfair that they violate public policy. A good example of this is *Sasfin (Pty) Ltd v Beukes*.[55] The court invalidated certain deeds of cession on the basis that they were so oppressive as to be contrary to public policy and were therefore void. The effect of the cluster of contracts was effectively to reduce the respondent to a financial slave of the appellant with no means of bringing an end to the arrangement. As Van der Merwe and Van Huyssteen acknowledge, the court focused almost exclusively on the effect

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51 562. For an authoritative exposition of the test for adjudicating the reasonableness of a restraint of trade agreement, see *Basson v Chilwan* 1993 3 SA 742 (A) 767.

52 Van der Merwe & Van Huyssteen (1995) *THRHR* 562.

53 562.

54 *Gibson v Van der Walt* 1952 1 SA 262 (A); *Rademeyer v Evenwel* 1971 3 SA 339 (T). The classic justification for why a court would not enforce gambling debts is because society considers gambling a wasteful activity that encourages prodigality; Van Huyssteen *Contract* et al 233.

55 1989 1 SA 1 (A).

the contracts would have on the respondent, in other words on the individual interests at stake. Yet the court held that the terms were completely void, not merely unenforceable.[56] This sits uncomfortably with the proposition that illegal contracts impacting individual interests are merely unenforceable. The authors can do no more than suggest that the court could have justifiably found that the terms were merely unenforceable and not void.

All things considered, the distinction between individual and social interests therefore fails to adequately explain why some illegal contracts are void while others are valid but unenforceable. The differentiation is not merely an academic issue. Indeed, the distinction becomes crucial in the context of partially performed illegal contracts where the need for restitution may arise.[57] But first it is necessary to understand the various consequences that could follow from illegality, prior to investigating the determinants of those consequences.

2 4 The general consequences of illegality

There are typically three issues of concern when dealing with the consequences of an illegal contract namely enforceability, restitution, and severability. Severability deals with the question of whether a partially illegal contract can be preserved by removing only the terms affected by the illegality. This issue need not be considered here since we are mainly concerned with the consequences of illegality that relate to enforceability and restitution.[58]

Generally, a court will not enforce an illegal contract, irrespective of whether it adopts the wide or narrow definition of illegality.[59] In this context courts typically cite the maxim *ex turpi causa non oritur actio*, which means that no action arises from a cause tainted by turpitude. In other words, one cannot base a claim for a remedy such as specific performance or damages on an illegal cause of action.[60]

If one party has transferred money or goods under an illegal contract which is subsequently found to be void, the question arises whether the transferor can obtain

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56 Van der Merwe & Van Huyssteen (1995) *THRHR* 563.

57 See 2 6 below.

58 For the general approach to severing illegal terms see *Sasfin (Pty) Ltd v Beukes* 1989 1 SA 1 (A) 15; *Senwes Ltd v Muller* 2002 4 SA 134 (T) 143.

59 *National Credit Regulator v Opperman* 2013 2 SA 1 (CC) para 14; *Jajbhay v Cassim* 1939 AD 537 540; *Schierhout v Minister of Justice* 1926 AD 99 109.

60 This principle extends beyond the law of contract, but it is not clear how far. See for example *Kylie v CCMA* 2010 4 SA 383 (LAC); *Minister of Police v Underwriters of Lloyds of London* 2021 ZASCA 72 para 14.

restitution. This brings us into the realm of unjustified enrichment. Although the courts have indicated a willingness to recognise a general enrichment action, it remains the practice to rely on one of the specific *condictiones* when instituting an enrichment claim.[61] In addition to satisfying the general requirements of enrichment liability,[62] a plaintiff may therefore also have to establish the elements that are peculiar to the particular enrichment action they are relying on.

The relevant action for reclaiming a transfer made under an illegal agreement is the *condictio ob turpem vel iniustam causam*.[63] The most notable feature of this action is that it is qualified by the *par delictum* rule, which provides that a plaintiff who is tainted with wrongdoing or turpitude resulting from the contract, may not claim under it.[64] It has been suggested that the justification for this rule is that it deters illegal contracts.[65] However, as will be indicated in more detail below, the court has an equitable discretion to relax the *par delictum* rule in order to do "simple justice between man and man".[66]

The purpose of the following sections is to investigate the implications of the *ex turpi* and *par delictum* rules in greater detail. It is said that the *ex turpi* rule is subject to no exception, meaning that once a contract is found to be illegal, the court has no equitable discretion to relax the rule.[67] However, it will be shown below that this proposition is not entirely correct. There are several ways in which the maxim might be subverted or avoided, which in turn generates a result akin to enforcement of the illegal contract.

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61 *McCarthy Retail Ltd v Shortdistance Carriers CC* 2001 3 SA 482 (SCA) para 9; Du Plessis *Unjustified Enrichment* 4-6.

62 The general requirements for enrichment liability are a) the plaintiff must be impoverished b) the defendant must be enriched c) at the expense of the plaintiff d) the enrichment must be without legal ground. See *Kudu Granite Operations (Pty) Ltd v Caterna Ltd* 2003 5 SA 193 (SCA) para 17; *McCarthy Retail Ltd v Shortdistance Carriers CC* 2001 3 SA 482 (SCA) para 15.

63 *National Credit Regulator v Opperman* 2013 2 SA 1 (CC) para 15. The court stated the other requirements of this *condictio* as follows: "ownership must have passed with the transfer; the transfer must have taken place in terms of an unlawful agreement; and the claimant must tender the return of what he or she received."

64 *Absa Bank Ltd v Moore* 2017 1 SA 255 (CC) para 47. The full maxim is *in pari delicto potior conditio possidentis vel defendentis.* It is not to be conflated or confused with the *ex turpi* rule as the court did in *Stols v Garlicke and Bousfield (PKF) (Durban) Incorporated* 2020 4 All SA 850 (KZP) para 227. The *ex turpi* rule excludes a claim in contract, whereas the *par delictum* rule operates to defeat a claim in unjustified enrichment. See further JS McLennan "Distinguishing the *turpis causa* and *par delictum* rules" (1996) 113 *SALJ* 214-215.

65 *Klokow v Sullivan* 2006 1 SA 259 (SCA) para 18; Visser *Unjustified Enrichment* 443-444.

66 *Jajbhay v Cassim* 1939 AD 537 544.

67 *Brits v Van Heerden* 2001 3 SA 257 (C) 270H-I; *Essop v Abdullah* 1986 4 SA 11 (C) 17.

2 5 Avoiding the *ex turpi* rule through statutory interpretation

A statute that explicitly specifies the status of a contract which infringes its provisions presents little difficulty.[68] But in cases where the statute is silent on the consequences, it is a question of interpretation to determine the consequences intended by the legislature. In such cases the courts have held that although a contract prohibited by implication is generally void and unenforceable, it will not always be so.[69]

Various factors may guide the court in determining the appropriate consequence of the illegality in a given case.[70] Commentators and courts compile this list differently, but there appears to be agreement that the following factors form the core of the inquiry. The most important consideration is the purpose of both the statute and more specifically, the purpose of the particular prohibition.[71] A second factor is whether a finding of validity would amount to the court sanctioning the very situation which the legislature wished to prevent.[72] If that is the case, the legislature could only have intended for the contract to be void. Another factor is whether a statute contains a penalty for infringements. The presence of a penalty provision typically, but not necessarily, indicates that the legislature desired a consequence of voidness. However, an illegal contract may nevertheless remain valid if the legislature regards the imposition of the penalty a sufficient punishment for the legal infringement.[73] A final and related consideration is proportionality. A court will not find a contract invalid if undoing the transaction would result in "greater inconveniences and impropriety" than if the contract remained valid in spite of the illegality.[74] To put it simply, the court will not find the contract invalid if doing so would amount to overkill.[75]

These principles are hard to reconcile with the proposition that the *ex turpi* rule is inflexible and subject to no exceptions. In the context of statutory illegality at least, the

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68 See for example s 51(3) of the Consumer Protection Act 68 of 2008 and s 90(3) of the National Credit Act 34 of 2005. Both these sections specify that transactions which contravene certain provisions of the respective pieces of legislation are void.

69 *Wierda Road West Properties (Pty) Ltd v Sizwe Ntsaluba Gbodo Inc* 2018 3 SA 95 (SCA); *Metro Western Cape (Pty) Ltd v Ross* 1986 3 SA 181 (A) 188; *Provincial Government of the Eastern Cape v Contractprops 25 (Pty) Ltd* 2001 4 SA 142 (SCA) para 4-9.

70 See generally Van Huyssteen et al *Contract* 225; Floyd "Legality" in *The Law of Contract* 188; *Swart v Smuts* 1971 1 SA 819 (A) 829; Bradfield & Christie *Christie's Law of Contract* 392-400.

71 *Absa Insurance Brokers (Pty) Ltd v Luttig NNO* 1997 4 SA 229 (SCA) 239; *Wierda Road West Properties (Pt) Ltd v Sizwe Ntsaluba Gbodo Inc* 2018 3 SA 95 (SCA) para 17.

72 *Pottie v Kotze* 1954 3 SA 719 (A) 726.

73 *Wierda Road West Properties (Pt) Ltd v Sizwe Ntsaluba Gbodo Inc* 2018 3 SA 95 (SCA) para 20; *Swart v Smuts* 1971 1 SA 819 (A) 829; *Pottie v Kotze* 1954 3 SA 719 (A) 727.

74 *Standard Bank v Estate van Rhyn* 1925 AD 266 274 quoting Voet 1 3 16.

75 *Oilwell (Pty) Ltd v Protec International Ltd* 2011 4 SA 394 (SCA) para 24.

intention of the legislature may be harnessed to sweep aside the *ex turpi* rule when the occasion demands it.

2 6 Subverting the *ex turpi* rule through an enrichment claim

As we have seen above, claims for restitution based on unjustified enrichment may arise from an illegal contract, although these claims are typically defeated by the *par delictum* rule if the plaintiff is also tainted by illegality. In Roman-Dutch law the *par delictum* rule was strictly applied.[76] However, in the first half of the 20th century it became increasingly apparent that this practice can generate unfair and unsatisfactory results.

The facts of *Friedman v Harris* provide a poignant illustration of the point.[77] A married man, the defendant, seduced a young girl, the plaintiff, and settled the seduction claim instituted against him afterward. He subsequently asked the plaintiff to repay the money on the promise that he would divorce his wife and marry the plaintiff or if he does not marry her, that he would repay her the money. The defendant did not divorce his wife and kept the money, after which the plaintiff sued to recover the sum. The defendant raised an exception that the claim was bad in law since it was based on an illegal contract to which the plaintiff was an equally guilty party. With great reluctance, the court held that it had no choice but to find for the defendant.

Eventually in *Jajbhay v Cassim* ("*Jajbhay*"), the court afforded itself an equitable discretion to relax the rule in order to do justice between the parties.[78] No fixed list of criteria has been laid down for when a court will exercise its discretion to relax the *par delictum* rule, although there appears to be consensus about at least some core factors a court should consider.[79] Relevant factors include the purpose of the provision that was contravened, what class of persons the provision is intended to benefit or protect;[80] the state of mind of the parties,[81] such as whether they were aware of the illegality, and the extent to which performance has already taken place.[82] Thus, if both

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76 Visser *Unjustified Enrichment* 447.
77 1928 CPD 43. See also *Brandt v Bergstedt* 1917 CPD 344; *Silke v Goode* 1911 TPD 989.
78 1939 AD 537 544.
79 See generally Du Plessis *Unjustified Enrichment* 206-208; Visser *Unjustified Enrichment* 447-451.
80 *Mamojee v Akoo* 1947 4 SA 733 (N) 738; *Wolmarans v Tuckers Land & Development Corporation (Pty) Ltd* 1979 1 SA 663 (T) 676; *Afrisure v Watson NO* 2009 2 SA 127 (SCA) para 47. Related to this is the question whether there is a need to protect vulnerable persons, see *Jordan v Penmill Investments CC* 1991 2 SA 430 (E) 440.
81 *Van Staden v Prinsloo* 1947 4 SA 842 (T) 848.
82 *Osman v Reis* 1976 3 SA 710 (C) 712; *Padayachey v Lebese* 1942 TPD 10; *Albertyn v Kumalo* 1946 WLD 529.

parties have fully performed under an illegal contract a court will be more reluctant to relax the *par delictum* rule.[83] Conversely, where there has only been partial performance, the need to award restitution may become more acute if it would prevent a situation where the defendant gets to retain an unwarranted windfall at the expense of the plaintiff.

Continued reference to the *par delictum* rule by the courts may be somewhat anachronistic in this context. It is not clear why the default should be that the position of the recipient is stronger than that of the transferor.[84] Instead of asking whether the *par delictum* rule should be relaxed, the court could just inquire from the outset whether the relevant policy considerations support granting or refusing restitution.[85]

Enrichment claims under partially performed illegal contracts can present fiendishly difficult problems. This is because the equities in a case might favour awarding restitution but doing so would amount to indirectly enforcing an illegal contract. A case in point is *Maseko v Maseko* ("*Maseko*").[86] The plaintiff owned a right to occupy a certain property. She became aware that the right might be attached by a creditor to satisfy a debt she had stood surety for, since the principal debtors had defaulted. Acting on dubious legal advice she, together with the defendant, with whom she was in a relationship at the time, put into motion a scheme designed to protect the asset. They would get married and then divorce shortly after. The crux of the scheme was that the settlement agreement for the divorce, which was made an order of the court, provided that the right to occupy the property would go to the estate of the defendant. Meanwhile the parties had informally agreed that the defendant would retransfer the right to occupy the property once the problem with the creditor had been resolved. After the divorce, the defendant deceived the plaintiff into moving out and subsequently refused to retransfer the occupation right to her. The plaintiff then approached the court in order to recover the right.

The contract between the parties was illegal and void because it was aimed at defrauding a creditor, it undermined the institution of marriage, and it abused the

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83 *Jajbhay v Cassim* 1939 AD 537 544; *Afrisure v Watson NO* 2009 2 SA 127 (SCA) para 46. Compare *Legator McKenna Inc v Shea* 2010 1 SA 35 (SCA).

84 Du Plessis (2021) *Acta Juridica* 189.

85 189.

86 1992 (3) SA 190 (W). In England this kind of case would be treated as a fraudulent resulting trust. See *Tinsley v Milligan* [1994] A.C. 340, discussed below at 3 3 3; *Tribe v Tribe* [1996] Ch. 107. One possible justification for assisting the claimant in such a situation despite the illegality is that it amounts to choosing the lesser of two evils; P Birks "Recovering Value Transferred under an Illegal Contract" (2000) 1 *Theoretical Inq L* 155 175-176.

judicial process. However, it was also clear from the evidence that there was a significant power imbalance between the parties.[87] Lazarus AJ summed up the problem as follows:

> "I have found the weighing of the equities in this case particularly difficult because if I do not make an order the defendant will have been substantially enriched at the plaintiff's expense whereas, if I do make an order, I will be indirectly enforcing an illegal contract. This is because an order that the defendant restore the property is exactly what the illegal agreement provided he should do."[88]

Despite concluding that the circumstances of the case warranted a relaxation of the *par delictum* rule even if it would amount to indirect enforcement of an illegal contract, the court ultimately dismissed the plaintiff's claim. The reason was that the settlement agreement of the divorce, even though it was based on an illegal contract, remained a valid court order until set aside. Since the issue of setting aside the order had not been properly canvassed, the court could not come to the aid of the plaintiff.

Maseko's case illustrates the advantages of a flexible approach to restitution under illegal contracts. Were it not for the procedural obstacle of the existing court order, the court would have correctly found for the plaintiff. The equities of the case clearly favoured her rather than the unscrupulous defendant, who sought to escape the consequences of his dishonourable conduct by relying on the illegality of the arrangement.

The flexible approach to the *par delictum* rule therefore allows the court to make a nuanced assessment of the merits in each individual case. Although it introduces some uncertainty into the law, the price is worth paying for the advantages gained.[89] Certain areas of the law are just so complex that they defy attempts to generate firm rules that will yield satisfactory results in every case.[90] The best option in these situations is to give judges a discretion they can exercise with reference to well-defined criteria.

The point of this discussion is that the *ex turpi* and *par delictum* rules are connected and can interact in complicated ways. A crucial feature of this interaction is that the assessment whether restitution should be awarded can only take place once the court

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87 For example, the defendant had severely assaulted the plaintiff on a previous occasion; 1992 3 SA 190 (W) 192.

88 1992 3 SA 190 (W) 200.

89 See the dramatic criticism of *Jajbhay v Cassim* 1939 AD 537 by De Wet & Van Wyk *Kontraktereg* 91-92 that the decision "plunges the law into a boundless morass of uncertainty and does so on unconvincing grounds."

90 J du Plessis "Equity, Fairness and Unjustified Enrichment: A Civil-Law Perspective" 2020 (83) *THRHR* 1 15.

has found that the illegality renders the underlying contract void. No enrichment claim can arise if the contract is merely unenforceable because the valid contract provides the defendant with a legal basis for retaining the transfer. A finding of validity therefore deprives the court of the opportunity to determine whether awarding restitution may have been appropriate in a particular case. This in turn may lead to the kind of harsh outcomes that characterised some of the cases decided before *Jajbhay*.

It is in this context that *Cool Ideas* merits closer attention. The appellant ("Cool Ideas") entered into a contract with the respondent ("Ms Hubbard") to construct a house for her. Cool Ideas was not registered as a home builder with the National Home Builders Registration Council ("the Council") at the time, since it had been advised by the Council that it was not necessary to do so. Cool Ideas had also employed a subcontractor who was duly registered to perform the actual construction of the house. When the construction was almost completed a dispute arose. Ms Hubbard was dissatisfied with the quality of the work and claimed compensation equivalent to the cost of remedying the defects. Cool Ideas in turn counterclaimed the outstanding portion of the contract price. In the subsequent arbitration proceedings, the arbitrator upheld some claims on both sides with the result that, on balance, Ms Hubbard owed Cool Ideas approximately R550 000. However, Ms Hubbard refused to pay on the basis that Cool Ideas was not registered as a home builder. Cool Ideas then approached the court in order to have the arbitration award enforced. Standing in its way was section 10 of the Housing Protection Act. The relevant part of the provision reads as follows:

> "10(1) No person shall—
> (a) carry on the business of a home builder; or
> (b) receive any consideration in terms of any agreement with a housing consumer in respect of the sale or construction of a home, unless that person is a registered home builder.
> 10(2) No home builder shall construct a home unless that home builder is a registered home builder."

The legislature also declared it an offence to contravene section 10.[91] Cool Ideas had clearly not complied with these provisions. The issue was therefore what impact its non-compliance had on the status of the arbitration award. Majorities in the Supreme Court of Appeal[92] and the Constitutional Court refused to enforce the arbitration award. Both courts found that the purpose of the Housing Protection Act was to protect

[91] S 21(1)(b).
[92] *Hubbard v Cool Ideas 1186* CC 2013 5 SA 112 (SCA).

consumers and that this purpose would be undermined if the award were enforced. A key feature of the outcome, especially in the reasoning of the Constitutional Court, was the finding that the contract between Cool Ideas and Ms Hubbard had to remain valid, but that the arbitration award which emanated from it could nevertheless not be enforced.[93]

It has been argued that the matter could have been resolved without making a finding on the validity of the contract.[94] However, assuming that it was necessary to pronounce on the contract's validity, it is submitted that the finding of the court that the contract remained valid is open to considerable doubt. To see why, we must examine the two reasons given by the court more closely.

The first reason was that the legislative aim of protecting consumers would be best served by a finding of validity. To hold otherwise, so the argument went, would render certain warranties incorporated into the contract by the Housing Protection Act redundant.[95] However, as Wallis shows, the illegality in the contract necessarily renders these implied terms ineffective, regardless of whether the contract remained valid or not.[96] The implied terms would only serve to protect the consumer if they were capable of being enforced.[97] In other words, Ms Hubbard would have to be able to enforce the contract against Cool Ideas. The problem is that any attempt by Ms Hubbard to enforce these terms would require Cool Ideas to perform – something it is not allowed to do.[98] Section 10 of the Housing Protection Act explicitly prohibits an unregistered home builder from performing.[99] The provision contains three prohibitions aimed at unregistered homebuilders. They may not carry on the business of a homebuilder, they may not receive any consideration in terms of any agreement with a housing consumer in respect of the sale or construction of a home and finally, they may not construct a home. To do any of these three things constitutes a criminal offence. Since a court cannot order a person do something illegal, the implied terms offer no practical assistance to consumers in this context. Accordingly, the continued validity of the building contract does not translate into the consumer protection

93 But see the minority judgment of Jafta J at para 47-51 who found that the contract was void.
94 See Wallis (2015) *SALJ* 949 where it is suggested that the case actually turned on the effect of an arbitration award on an obligation.
95 2014 4 SA 474 (CC) para 48.
96 Wallis (2015) *SALJ* 962.
97 962.
98 962.
99 962.

contemplated by the court.

The second reason in the majority judgment is that a finding of validity in this context would offer greater protection to both parties, because it allows them to keep any performances already received under the contract.[100] This might be true if both parties rendered performances of approximately equal value. However, if the performances are disproportionate, as it was in *Cool Ideas,* then the consequences could be quite harsh on the party who rendered the greater performance.

The court was aware that the finding of validity excluded any possible enrichment claim that Cool Ideas might have had. For this reason, it embarked on an analysis of whether its interpretation that the Housing Protection Act required the contract to remain valid amounted to an arbitrary deprivation of property under section 25 of the Constitution of the Republic of South Africa 1996, ("the Constitution").[101] But this was a red herring, because Cool Ideas could only have had an enrichment claim if the contract was void in the first place. It is logically impossible to be deprived of something one never had. The finding that the contract was valid meant that the claim never came into being in the first place, because the contract remained a valid basis for the transfer.[102]

One cannot help but feel some sympathy for the plight of Cool Ideas. It received bad advice from the Council, performed work to an adequate standard, but was left empty-handed because its client managed to hide behind a technical rule that Cool Ideas had in any event in substance complied with, albeit not in form.[103] Ms Hubbard was left with a significant windfall at the expense of *Cool Ideas*. However, in spite of the strained reasoning, the result reached by the court was ultimately the correct answer to the way in which Cool Ideas had framed its case. It had conceded that if it had sued on the contract itself, its claim would have been excipiable as a result of the illegality.[104] The existence of an arbitration award could not materially alter that state of affairs – the *ex turpi* rule remained in the way.

What Cool Ideas did not argue, and the court did not consider, was the merits of

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[100] 2014 4 SA 474 (CC) para 47.
[101] Para 38-44.
[102] JC Sonnekus *Unjustified Enrichment in South African Law* 2 ed (2017) 263; Wallis (2015) *SALJ* 963.
[103] See *Hubbard v Cool Ideas 1186* CC 2013 5 SA 112 (SCA) para 8. Considerations of fairness invited dissenting judgments from Willis JA in the Supreme Court of Appeal and Froneman J in the Constitutional Court.
[104] *Hubbard v Cool Ideas 1186* CC 2013 5 SA 112 (SCA) para 12.

awarding an enrichment claim instead.[105] Since an enrichment claim is said to be an equitable remedy, it would have addressed the dissentient judges' concerns about fairness.[106] The court would have been able to make a nuanced assessment of the relevant policy considerations at stake in its determination whether it should relax the *par delictum* rule or not. For example, the need to prevent legislation from being subverted could have been balanced with the need to prevent a disproportionate gain to Ms Hubbard.[107]

Another significant feature of this solution is that the quantum of the claim might have differed. Unlike claims in contract, enrichment claims are quantified according to the so-called double ceiling rule: the quantum is the lesser amount between the value of the plaintiff's impoverishment and the defendant's enrichment.[108] This could be equal to the contract price, in which case it would create a result akin to enforcing an illegal contract. However, it could also have been less, since a plaintiff may not include any profit it stood to gain when calculating its impoverishment.[109] This means that Cool Ideas could at least have been compensated for the expenses it incurred, say for paying the subcontractor. The purpose of the Housing Protection Act would still be given some effect since Cool Ideas would be deprived of any profit it stood to gain, but at the same time Ms Hubbard would not be left be with a significant and undeserved windfall.

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[105] Cool Ideas might also have explored a claim in delict against the Council for negligently giving the wrong advice.

[106] Wallis (2015) *SALJ* 964. On the role of fairness in the law of unjustified enrichment, see Du Plessis (2020) *THRHR* 1.

[107] Du Plessis (2021) *Acta Juridica* 198.

[108] *Kudu Granite Operations (Pty) Ltd v Caterna Ltd* 2003 5 SA 193 (SCA) para 17.

[109] The South African authorities on the proposition that a plaintiff may not include profit in the calculation of its impoverishment are tenuous. In *Skyword (Pvt) Ltd v Peter Scales (Pvt) Ltd* 1979 1 SA 570 (R) 573, a Rhodesian court applied the proposition but quoted only *Gorfinkel v Miller* 1931 CPD 251 in support. *Gorfinkel's* case is not strong authority for the point, since it was held there that profit would be recoverable if the parties concluded a tacit mandate to that effect. The crucial difference is that the basis for such a claim would be in contract, not unjustified enrichment. In *Absa Bank Ltd t/a Bankfin v Stander t/a CAW Paneelkloppers* 1998 1 SA 939 (C) 942 the plaintiff made repairs to a car and claimed an amount greater than the actual value by which the car had increased. The court did not consider whether the plaintiff had included profit in its calculation of the quantum. Instead, it followed a line of cases which provide that judges have a discretion to determine the quantum of useful expenditure incurred by the plaintiff in a manner that is fair in the circumstances (1998 1 SA 939 (C) 942 957; *Wynland Construction (Pty) Ltd v Ashley-Smith* 1985 1 SA 534 (C) 538 and the cases cited there). The idea of excluding profits in enrichment claims where the contract is illegal may be an attractive middle way solution to cases where full enforcement of the contract and full denial of the enrichment claim are both unpalatable; see further 5 2 3 5 below.

2 7 Subverting the *ex turpi* rule: connected and collateral contracts

So far, we have seen how statutory interpretation and enrichment claims may be used to subvert the *ex turpi* rule. A relevant consideration in both scenarios is the need to avoid bringing about the very illegal situation that the statute or common-law rule in question intended to prevent. This raises the question to what extent a court may give effect to a contract which is in some way connected or collateral to a separate, illegal contract. A typical category of cases dealing with this problem concerns contracts related to gambling debts governed by the common law.

Gibson v Van der Walt ("*Gibson"*) remains the authoritative case on this issue.[110] The case established two principles. The first is that a relevant consideration in this context is the "nature and degree of reprobation" which attaches to the impugned act or contract.[111] In other words, a contract which is illegal or immoral is void since a high degree of reprobation attaches to it.

However, a different approach is needed where the original contract is merely rendered unenforceable and not void, since these contracts are not *per se* regarded as illegal. The court in *Gibson* faced exactly this problem since the debt at stake arose from wagering. The appellant was a bookmaker who had concluded various betting transactions with the respondent. The respondent had subsequently given an undertaking that he would pay the bookmaker the money that was owed. When he failed to do so, the bookmaker approached the court for assistance. For this kind of situation Fagan JA set out a different approach:

> "The test in such a case, to my mind, should be whether the Court is asked, in effect, to enforce the unenforceable claim; in other words, is the later transaction on which the plaintiff relies merely a device for enforcing his original claim, is it merely his original claim clothed in another form or with some term or condition added to it, or a ratification or even novation of the original claim which leaves its essential character unchanged; if so, the plaintiff must fail."[112]

In the end the appeal failed since the undertaking by the respondent was essentially the same wagering agreement but with a time stipulation added to it. Even though the wagering contract was not illegal, the court characterised it as *improbata*, meaning

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[110] 1952 1 SA 262 (A).

[111] 269G.

[112] 270A-B; The courts also tend to apply this test where the illegality rendered the original contract void and not merely unenforceable, see *Shabangu v Land and Agricultural Development Bank of South Africa* 2020 1 SA 305 (CC) para 22; *Valor IT v Premier, North West Province* 2021 1 SA 42 (SCA) para 49-50.

that the debt is objectionable to the extent that a court should not enforce it.[113]

The first principle from *Gibson* also requires some elaboration. Although it is true that one cannot always meaningfully rank degrees of illegality, the general idea seems to be that a contract or act which facilitates or encourages an illegal contract will also be void due to the illegality and that this must be determined on a case-by-case basis.[114]

The decision in *Courtney-Clarke v Bassingthwaighte* illustrates how this principle works in practice.[115] The case concerned the relationship between two agreements. The first was an illegal credit agreement between the plaintiff and a bank. The second one was an oral agreement between the plaintiff and the defendant. In terms of the oral agreement the defendant undertook to pay monthly instalments to the plaintiff that corresponded to the instalments that the plaintiff owed to the bank. When the defendant defaulted on the payments, the plaintiff sought to enforce the oral agreement. The court refused to enforce the oral agreement because it found that there was an express interlocking of the two contracts.[116] This was not so much a case of an illegal credit agreement being indirectly enforced since that would have to be motivated by the bank and not the plaintiff. The finding may rather be explained as an application of the first principle in *Gibson*, namely that the illegality attaching to the credit agreement was objectionable enough to taint the verbal agreement and render it void too. This is because it ultimately facilitated the performance of the illegal contract between the plaintiff and the bank.

Therefore, in the context of connected contracts there appears to be less latitude for a plaintiff who wants to circumvent the *ex turpi* rule than in the cases of statutory interpretation or enrichment claims.

2 8 The impact of illegality on the termination of obligations

2 8 1 Novation and compromise

There is one mystery which *Gibson* did not conclusively solve. While there is no doubt that some gambling debts, and presumably other illegal obligations which are valid but

[113] 1952 1 SA 262 (A) 268C.
[114] *Richards v Guardian Assurance Co.*1907 TH 24 28; Bradfield & Christie *Christie's Law of Contract* 459.
[115] 1991 1 SA 684 (Nm).
[116] 1991 1 SA 684 (Nm) 691.

unenforceable, cannot be enforced by dressing them in different clothing, it remains uncertain whether other methods of extinguishing obligations such as novation, compromise or set-off are permitted.

Novation is an agreement which extinguishes an obligation and replaces it with a new obligation.[117] A crucial feature of a novation is that the original obligation must be valid for the novation to be valid.[118] In other words, if an original obligation is tainted by illegality, it cannot be resuscitated through a novation.[119]

A compromise, on the other hand, is an agreement in terms of which the parties settle a disputed or uncertain level of indebtedness.[120] This is different to a novation because the validity of a compromise is said to be independent from its original cause.[121] This means that the compromise can be valid even if the original obligation is not.

It is worth emphasising that for the transaction to constitute a compromise, there must be some uncertainty surrounding the status of the original debt. If both parties were without a doubt aware at the outset that the original debt is invalid, then they cannot compromise on it. This principle emerges from *Shabangu v Land and Agricultural Development Bank of South Africa.*[122] The applicants had stood surety to loans unlawfully extended to a property developer by the respondent bank. The bank calculated that the developer owed it some R 95 million. The developer disputed this amount but signed an acknowledgement of debt in which it accepted liability for R 82 million in full and final settlement of its indebtedness. When the developer was liquidated, the bank sought to recover the money from the sureties, not based on their liability for the original loans, but rather their alleged liability for the acknowledgement of debt entered into by the developer. The bank argued that the acknowledgement of debt constituted a valid compromise and that it was therefore not tainted by the illegality of the original loan agreement. The Constitutional Court disagreed. It applied

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[117] Van Huyssteen et al *Contract* 581.
[118] The other elements of a novation, such as an *animus novandi,* must also be complied with; Van Huyssteen et al *Contract* 582-584.
[119] *Shabangu v Land and Agricultural Development Bank of South Africa* 2020 1 SA 305 (CC) para 20.
[120] There is some debate about whether compromise is a subspecies of novation or not. The better view seems to be that they are distinct; Van Huyssteen *Contract* et al 588-589; Floyd "Legality" in *The Law of Contract* 392.
[121] *Benefeld v West* 2011 2 SA 379 (GSJ) para 14. The court qualified the statement by adding that the terms of the compromise itself must still be legal. See also *Investec Bank Limited v Pillay* 2021 ZAKZPHC 25; *Dennis Peters Investments (Pty) Ltd v Ollerenshaw* 1977 1 SA 197 (W) 202G-203A.
[122] 2020 1 SA 305 (CC).

the second principle in *Gibson* and found that the acknowledgement of debt did not change the illegal nature of the bank's claim. The acknowledgement of debt actually amounted to a novation rather than a compromise, since the parties were at the time already aware that the original loan agreement was illegal.[123]

In principle, it therefore appears to be possible to circumvent the *ex turpi* rule by entering into a compromise. A creditor might manage to recover a debt in this manner and thereby indirectly enforce the illegal contract, even though their claim would have failed before a court. However, this is a justifiable exception. A debtor may legitimately elect to compromise in order to avoid costly litigation even if they are of the view that they are not indebted at all or to the extent alleged by the creditor.

2 8 2 Set-off

If two persons are mutually indebted to each other through two or more distinct obligations, they may extinguish these obligations without exchanging performances. If the parties are equally indebted, the obligations on both sides are terminated. If not, the smaller debt extinguishes the larger one *pro tanto*. This process is called set-off.[124] The question that arises is to what extent set-off may be relied on when one of the obligations is valid but unenforceable due to illegality. This was the problem that confronted the court in *Nichol v Burger* ("*Nichol*").[125] The appellant sued the respondent for about R1500, to which the respondent pleaded that the appellant owed him about R14 000 in gambling debts against which the claim could be set-off.

The authorities on this point are not harmonious. In *Fensham v Jacobson*[126] and *Rosen v Wassermann,*[127] debts arising from gambling were allowed to be set-off. On the other hand, the attitude of the Appellate Division in *Gibson* seemed to suggest that gambling debts are not capable of set-off. In the course of his judgment, Fagan JA noted that Voet did not regard debts arising from wagers as natural obligations.[128] However, Tebbutt J in *Nichol* held that the comment by Fagan JA was *obiter* and that the Roman-Dutch authors in any event held conflicting views on the matter.[129] Thus it

[123] Para 31-32. The sureties could only have been liable if the acknowledgement of debt was in respect of an enrichment claim of the bank and the terms of the suretyships were wide enough to cover that.
[124] Van Huyssteen et al *Contract* 599.
[125] 1990 1 SA 231 (C).
[126] 1951 2 SA 136 (T).
[127] 1984 1 SA 808 (W).
[128] *Gibson v Van der Walt* 1952 1 SA 262 (A) 268A referring to Voet 11 5 7.
[129] *Nichol v Burger* 1990 1 SA 231 (C) 235.

was not necessary to follow Voet. The court in *Nichol* therefore felt competent to hold that set-off was permitted.

This decision leaves one with the impression that set-off may be used to indirectly enforce a debt that is illegal in the wide sense. Is this not exactly the situation the court in *Gibson* wished to prevent? To this argument Tebbutt J replied that there is a difference between enforcement and performance of a debt.[130] *Gibson* only blocks the indirect enforcement of an illegal debt. The respondent in *Gibson* could still have validly paid the debt even though he was not required to. Set-off has the same effect as payment and is therefore a manner of performance. Since natural obligations can be performed, *Gibson* does not bar set-off.

The problem with *Nichol* is the way in which the court framed the issue:

> "Is a gambling debt a natural obligation and therefore capable of set-off?"[131]

To describe the obligation arising from gambling as a natural obligation and then infer from this description that the obligation therefore has to display certain characteristics is to commit a logical fallacy.[132] As Hume famously argued, one cannot derive an *ought* from an *is*.[133] Were this question to come before a court today, the proper approach would be to ask whether a gambling debt *ought* to be capable of set off, by having regard to the relevant considerations of public policy. In this regard it may be putting form over substance to hold that set-off does not operate akin to indirect enforcement here, but that it is merely a method of payment. However, as Tebbutt J noted, it may also be necessary for the court to reconsider the legal status of a gambling debt governed by the common law in light of the changes to public policy in the past few decades.[134] It may follow from such a reconsideration that set-off would also be permitted.

2 9 Illegality and estoppel

Another mechanism whereby a party may attempt to circumvent the *ex turpi* rule is estoppel. Estoppel is traditionally thought of as a defence that may be raised where a person X made a blameworthy representation to another person Y and Y, relying on the truth of the representation, acted accordingly and suffered prejudice as a result.

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[130] 237.
[131] 1990 1 SA 231 (C) 233, quoted in Van Huyssteen et al *Contract* 233 n 172.
[132] Van Huyssteen et al *Contract* 233.
[133] D Hume *Treatise on Human Nature* (EC Mossner ed) (1985) book III part I section I.
[134] *Nichol v Burger* 1990 1 SA 231 (C) 236F.

Estoppel operates to preclude X from denying the truth of the representation.[135] In other words, X is held to the representation upon which Y acted.

To see how estoppel and illegality can interact we may consider the following example. Suppose a plaintiff's contractual claim is met with a plea that the contract is illegal. Suppose further that the defendant had represented to the plaintiff that the contract was lawful. The question is whether the plaintiff should be able to rely on estoppel to preclude the defendant from denying the truth of their representation that the contract was valid.

The *locus classicus* on estoppel and illegality is *Trust Bank van Afrika Bpk v Eksteen* ("*Eksteen*").[136] The court reiterated the general principle that an act which is contrary to a legal rule is void and cannot be made valid through indirect means if doing so would undermine the purpose of the prohibition.[137] However, it left open the question of whether a party to an illegal agreement may raise estoppel. The judgment only established that the illegality of an agreement between two parties does not preclude a third party from invoking estoppel against one of them.[138] It nevertheless appears to have been largely settled in the wake of *Eksteen* that estoppel may not be raised if it would have the effect of rendering an illegal contract enforceable.[139]

That is, however, not the end of the matter. In *Eksteen* Hoexter AJA wrote a separate, concurring judgment in which he said:

> "[W]henever a representor relies on a statutory illegality it is the duty of the Court to determine whether it is in the public interest that the representee should be allowed to plead estoppel. The Court will have regard to the mischief of the statute on the one hand and the conduct of the parties and their relationship on the other hand."[140]

This seems to open a back-door, although the scope is quite limited. The representee would have to establish that raising estoppel would not subvert the statute or policy considerations which caused the contract to be void. This is a very high bar and most

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[135] JC Sonnekus *The Law of Estoppel in South Africa* 3 ed (2012) 48. But see also *Makate v Vodacom (Pty) Ltd* 2016 4 SA 121 (CC) para 120-123 where the court held that estoppel can be used both as a "sword" and a "shield."

[136] 1964 3 SA 402 (A).

[137] 411H. A similar position prevails in English law. As Wilken & Ghaly write: "A party cannot be estopped from denying that which it could not lawfully have agreed"; S Wilken & K Ghaly *The Law of Waiver, Variation and Estoppel* 3 ed (2012) 9.132.

[138] 1964 3 SA 402 (A) 412.

[139] *Provincial Government of the Eastern Cape v Contractprops 25 (Pty) Ltd* 2001 4 SA 142 (SCA) para 11; *Mgoqi v City of Cape Town; In Re: City of Cape Town v Mgoqi* 2006 4 SA 355 (C) para 145.

[140] 1964 3 SA 402 (A) 415-416; see also GF Lubbe & CM Murray *Farlam and Hathaway Contract: Cases, Materials and Commentary* 3 ed (1988) 286.

attempts to vault over it have thus far been met with failure.[141]

2 10 Illegal contracts in administrative law

Contracts concluded with the State are subject to the rules of administrative law and therefore behave somewhat differently from illegal contracts where the rules of the common law apply. If a contract concluded with the State is unlawful because it contravened the rules of administrative law, the position is normally that the contract must be declared invalid as a first step.[142] The court has no discretion not to invalidate the contract. The court must then determine the appropriate remedy. In terms of this second step, the court is given a wide discretion to grant any order that is 'just and equitable.'[143] Due to this rule, it may occur that a legally flawed contract is nevertheless fully or partially enforced in substance because the court considers it just and equitable to do so.

The typical scenario where this kind of indirect enforcement might happen is the following. A state entity awards a tender to a contractor. The contractor performs fully or to a significant extent and then demands payment for its services. The state entity responds that the contract is invalid because it failed to adhere to its own procurement procedures when it awarded the tender. The state entity subsequently takes its own decision to award the tender on review. The court is obliged to declare that the contract is invalid. The question then arises what a just and equitable order would be in the circumstances.

The Constitutional Court has dealt with this problem in two recent cases. In *State Information Technology Agency SOC Limited v Gijima Holdings (Pty) Ltd,* the State Information Technology Agency ("SITA") instituted a review of its own decision to

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[141] The appellant in *Credit Corporation of SA Ltd v Botha* 1968 4 SA 837 (N) 851-852 succeeded with this argument but it was a third party, so it fell clearly within the ambit of *Eksteen.* The argument failed in *Strydom v Die Land – en Landboubank van Suid-Afrika* 1972 1 SA 801 (A) and *Oceanair (Natal) (Pty) Ltd v Sher* 1980 1 SA 317 (D) 326. See also *Merifon (Pty) Ltd v Greater Letaba Municipality* 2021 ZASCA 50 para 26-27; *City of Tshwane Metropolitan Municipality v RPM Bricks (Pty) Ltd* 2008 3 SA 1 (SCA) para 13; *Syfrets Mortgage Nominees Ltd v Cape St Francis Hotels (Pty) Ltd* 1991 3 SA 276 (SE) 289. Unusually, the court was prepared to allow estoppel to enforce an illegal agreement in *Stols v Garlicke and Bousfield (PKF (Durban) Incorporated* 2020 4 All SA 850 (KZP) para 224, but the comment by the court was clearly *obiter*.

[142] S 172(1)(a) of the Constitution; s 8 of the Promotion of Administrative Justice Act 3 of 2000 ("PAJA"); *Allpay Consolidated Investment Holdings (Pty) Ltd v Chief Executive Officer of the South African Social Security Agency* 2014 1 SA 604 (CC) para 56.

[143] S 172(1)(b) of the Constitution; s 8 PAJA; *Allpay Consolidated Investment Holdings (Pty) Ltd v Chief Executive Officer of the South African Social Security Agency* 2014 1 SA 604 (CC) para 25.

award a tender.[144] SITA had given the contractor false assurances that all the necessary procedures had been followed and only raised the question of invalidity after a lengthy delay. The court found that SITA should not be allowed to benefit from its conduct, so along with a declaration that the contract was invalid, the court ordered that the declaration of invalidity did not have the effect of divesting the contractor of any rights it would have been entitled to under the contract but for the declaration of invalidity.

The same happened in *Buffalo City Metropolitan Municipality v Asla Construction (Pty) Ltd* ("*Asla*").[145] The applicant municipality had awarded a tender to the respondent, but the tender turned out to be defective because the municipality's procurement procedures had not been followed. The municipality only took its decision on review after the respondent had almost fully performed in terms of the contract and sued for payment. Again, the court found that the contract was invalid, but held that the municipality should not benefit from its dilatory conduct. Accordingly, the contract was not set aside so as to preserve the rights that the respondent would have been entitled to under the contract. However, the court also stressed that the order preserved only the rights that had already accrued to the respondent under the contract. The order does not permit the respondent to obtain any future rights under the contract.

Most recently, the Supreme Court of Appeal ("SCA") had occasion to consider the impact of these two decisions in *BW Brightwater Way Props (Pty) Ltd v Eastern Cape Development Corporation.*[146] The contract in this case was not a tender, but a long-term lease. Again, it transpired that the respondent state entity did not follow the required procedures when it concluded the lease with the appellant. When the validity of the lease was challenged in the High Court, it issued an order that the lease was indeed invalid. However, in terms of section 172(1)(b) of the Constitution, the court considered it just and equitable to order additionally that the invalidity did not divest the appellant of any rights it held under the lease. The difference between this case and *Gijima* and *Asla* is that it concerned a lease rather than a tender. In *Gijima* and *Asla* the rights that were preserved were to demand payment for services that had been rendered. By contrast, enforcing the lease agreement could only mean that the

[144] 2018 2 SA 23 (CC).
[145] 2019 4 SA 331 (CC).
[146] 2021 6 SA 321 (SCA).

appellant was entitled to continue occupying the property. Accordingly, the High Court's order actually had the effect of enforcing an unlawful contract. It was on the basis of this distinction that the SCA overturned the High Court's decision. It held that the effect of the High Court order was to preserve future rights of the appellant. *Gijima* and *Asla* was only authority for the proposition that rights that had already accrued under an unlawful contract may be preserved in terms of section 172(1)(b) of the Constitution if it is just and equitable to do so.[147]

Much more could be said about this issue and the differences and similarities between illegality in administrative law and the law of contract. A deeper analysis is unfortunately beyond the scope of this thesis. The point emphasised here is simply that there is a line of cases in administrative law where contracts are effectively enforced notwithstanding their illegality.

2 11 Conclusion

Depending on the circumstances, a contract which infringes a legal rule will be either void, or valid but unenforceable. This area of the law is beset with difficulty, not least because the language used in this context is inconsistent. The reason for the difficulty lies in the fact that courts and commentators tend to differ on the ambit of what constitutes an illegal contract. Some regard voidness as a necessary condition for a transaction to be considered an illegal contract. Others use the term more generously to also include contracts which are not considered illegal *per se but* will nevertheless not be enforced by the court for reasons of public policy.

It has been argued in this chapter that the decisions of the courts and academic writing in South Africa do not provide convincing answers for why this distinction is drawn. Characterising valid but unenforceable contracts as natural obligations takes the matter no further, nor does an inquiry into whether the contract in question primarily impacts on social or individual interests.

A common theme in the explanations considered is that the greater the degree of illegality, the harsher the sanction of the law should be. A serious infringement of the

[147] Rather cryptically towards the end of its judgment, at para 29, the SCA seemed to suggest that the appellant may have an enrichment claim against the respondent. But how an enrichment claim fits in with the notion of preserving 'accrued rights' in these kinds of cases is unclear. On the application of the principles of unjustified enrichment to provide compensation in terms of PAJA or s 172(1)(b) of the Constitution, see further G Quinot, A Anthony, J Bleazard, S Budlender, R Cachalia, H Corder, M Finn, M Kidd, T Madonsela, P Maree, M Murcott, M Salukazana & E Webber *Administrative Justice in South Africa: An Introduction* 2 ed (2020) 330-332.

law thus warrants voidness as a consequence, whereas the law is content with mere unenforceability as the consequence of a less serious infringement. It has been argued that this is unconvincing because it fails to appreciate the full scope of consequences that may flow from illegality. In cases where there has been a partial and unequal performance between the parties, a finding of voidness may well yield the less harsh result. This is because a finding of validity prevents the court from making a nuanced assessment of whether an enrichment claim should be awarded.

In this context it is crucial to distinguish carefully between the operation of the *ex turpi* and *par delictum* rules. The *ex turpi* rule prevents a plaintiff from suing on an illegal contract, whereas the *par delictum* rule prevents the enrichment claim of a plaintiff who is also tainted by illegality.

Despite statements to the contrary, the *ex turpi* rule has been shown to not be inflexible. There are many ways in which it may be circumvented or subverted. One way is when the court decides to award an enrichment claim. This is a justifiable exception, since in practice the determination of whether the enrichment claim should be awarded, requires a careful balancing of the relevant policy factors. It has been argued that in cases such as *Maseko* and *Cool Ideas* the policy factors in favour of awarding the enrichment claim outweighed the need to prevent indirect enforcement of the respective illegal contracts.

There are also other situations in which a plaintiff might circumvent the *ex turpi* rule. A court can soften the impact of illegality on a contracting party, where appropriate, by interpreting a statute accordingly. A creditor might also achieve a compromise on or set off the illegal debt, though the scope here is more limited than in the cases of enrichment claims or statutory interpretation. A party who attempts to indirectly enforce an illegal contract by suing on a connected contract or raising estoppel is also likely to fail.

Finally, there is a series of cases in administrative law where tenders that are invalid due to illegality are nevertheless enforced because the court considers it just and equitable to do so in the circumstances. It is worth noting that the factors which the court considers when adjudicating any of the issues that arise from illegal contracts are remarkably similar. Of these factors, the purpose of the relevant legal rule and the need to avoid undermining it will almost always be decisive. On the other hand, however, a court may also, in appropriate circumstances, take into account the need to avoid a result that is disproportionately harsh on the losing party when compared to

the severity of the legal infringement. Where an illegal contract is found to be valid but unenforceable instead of void, the court risks losing sight of these policy considerations, since it then becomes unable to determine whether awarding restitution would be appropriate. Considering the uncertainty surrounding this area of the law, it is therefore worth investigating how other prominent jurisdictions deal with illegal contracts. That is the task of the following chapter.

CHAPTER 3: ILLEGALITY IN FOREIGN JURISDICTIONS

3 1 Introduction

The previous chapter considered the consequences of illegality from a South African perspective. This chapter investigates how selected foreign jurisdictions approach the problems caused by illegal contracts. The aim is to set the stage for a critical analysis of difficult fact patterns that every legal system must confront, and potentially draw some conclusions as to appropriate responses to these problems.

3 2 German law

3 2 1 Terminological orientation

The term 'illegal contract' does not translate neatly into German. This is because the rules concerning illegality in Germany are largely contained in the general section of the German Civil Code ("BGB") rather than in the section dealing specifically with contracts. Thus, the legal rules governing illegality speak of legal transactions (*Rechtsgeschäfte*), which include not only contracts but also other juristic acts such as the making of a will or entering into a marriage.

A second important distinction drawn in German law is between legal transactions that conflict with statutory prohibitions and those that are contrary to good morals (*die gute Sitten*). This thinking is reflected in the two most prominent provisions that deal with illegality, namely § 134 BGB and § 138 BGB.[1] In view of this structure, it is therefore sensible to consider each provision separately.

3 2 2 Transactions contrary to statutory prohibitions.

The rule on statutory prohibitions is contained in § 134 BGB:

> "Ein Rechtsgeschäft, das gegen ein gesetzliches Verbot verstößt, ist nichtig, wenn sich nicht aus dem Gesetz ein anderes ergibt."
>
> "A legal transaction that violates a statutory prohibition is void, unless the statute leads to a different conclusion."

When applying this provision, the first step is to determine whether the statute that has been infringed by the transaction is a so-called prohibition statute (*Verbotsgesetz*) or

[1] In references to the BGB, § means "paragraph"; where there are sub-paragraphs, (I) means "first subparagraph"; (1) means "first sentence"; R Zimmermann & JE du Plessis "Basic Features of the German Law of Unjustified Enrichment" (1994) 2 *RLR* 14 n 1.

merely a regulatory prescription (*Ordnungsvorschrift*).[2] A *Verbotsgesetz* directly prohibits the content of a certain transaction. An *Ordnungsvorschrift,* on the other hand, disapproves of the circumstances under which a certain transaction is concluded rather than its content.

This difference may be illustrated with reference to the scenario of a retailer trading outside prescribed hours. Although the Shop Closing Act[3] only allows trading during prescribed hours, contracts concluded with the retailer outside these hours are nevertheless regarded as valid. The Shop Closing Act is considered an *Ordnungsvorschrift,* since it disapproves only of the circumstances of contract conclusion, rather than the content of the contract.[4] In such cases, the imposition of an administrative penalty is regarded as a sufficient sanction for the breach – requiring the contract to be void would be overkill.[5] In addition, if a statute specifies a particular consequence for the infringing contract, effect will be given to that consequence.[6] § 134 BGB therefore only comes into play when the statute that has been infringed is a *Verbotsgesetz* and does not specify what consequence should follow.[7]

The meaning of § 134 BGB is controversial because there is some debate about how the qualification in the latter part of the provision should be interpreted.[8] One view is that it creates a presumption of invalidity.[9] In other words a transaction is void as a result of § 134 BGB unless the statute allows it to remain valid, either by expressly stating or implying it. Another approach is to regard § 134 BGB as a so-called empty norm which only refers to whichever statute has been infringed.[10] The statute thus becomes wholly determinative of the result.[11] Against this suggestion, however, it has been questioned what should happen if the interpretation of the statute yields no clear result.[12] For jurists from other jurisdictions this debate may seem somewhat esoteric.

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2 J Gleim "*Patel v Mirza* und die Illegality-Doktrin im Vergleich zum deutschen Recht" (2018) 2 *ERPL* 227 234.

3 *Gesetz über den Ladenschluss* 28 11 1965.

4 C Armbrüster "§ 134" in FJ Säcker, R Rixecker, H Oetker & B Limperg (eds) *Münchener Kommentar zum Bürgerlichen Gesetzbuch* 8 ed (2018) para 62 ("*MüKo*").

5 B Häcker "Illegality and Immorality from a Civilian Angle" in S Green & A Bogg (eds) *Illegality after* Patel v Mirza (2018) 331 345.

6 *MüKo* § 134 para 3.

7 Para 3.

8 Häcker "Illegality and Immorality" in *Illegality after* Patel v Mirza 344.

9 R Zimmermann *The Law of Obligations: Roman Foundations of the Civilian Tradition* (1996) 701; CW Canaris *Gesetzliches Verbot und Rechtsgeschäft* (1983) 19.

10 *HKK* §§ 134-137 para 2.

11 Häcker "Illegality and Immorality" in *Illegality after* Patel v Mirza 344 citing W Flume *Allgemeiner Teil des Bürgerlichen Gesetzbuchs Band 2: Das Rechtsgeschäft* 4 ed (1992) 341.

12 Häcker "Illegality and Immorality" in *Illegality after* Patel v Mirza 344.

If the interpretation of a statue yields no clear intent about the status of the infringing transaction, then one cannot help but wonder whether the statute was indeed properly interpreted in the first place. Fortunately, there is no need to take a firm position in this debate for present purposes. From a practical perspective it is at the very least clear that an application of § 134 BGB requires an inquiry into the spirit and purpose (*Sinn und Zweck*) of the relevant statute to determine its impact on the infringing contract.[13]

The approach to interpretation that German courts use to determine these questions consist of four steps. First, the court will consider the language used in the statute, in what is called semantic interpretation. Thus, certain phrases such as "must not" (*darf nicht*) or "is not allowed" (*ist unzulässig*) are typically indications that the legislature requires the transaction in question to be void.[14] Conversely, use of the term "should not" (*soll nicht*) is more likely to mean that the transaction was not intended to be void.[15] It is important to stress that the use of these phrases is not decisive and that a statute using one of them could also be interpreted to have intended a different result for the transaction in question.[16]

Second, the court will consider the position of the norm vis-à-vis the rest of the legal framework. Then follows a consideration of the historical intention of the legislature, which is typically revealed in the preparatory works of the statute. Finally, the court will consider the purpose of the relevant provision.[17] Generally there is no fixed hierarchy among these criteria and a court will give each factor different weight depending on the circumstances of the case.[18] However, in this context the teleological approach in step four is arguably the most important, given the emphasis on the spirit and purpose of the statute.

To sum up, the application of § 134 BGB is said to entail two steps. The first is to determine the character of the infringed statute, that is, whether it is a *Verbotsgesetz* or an *Ordnungsvorschrift*. This is followed by an interpretation of the statute in order to determine the status of the infringing transaction. The criteria for determining both steps are essentially the same, although it is important that the two be treated

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13 Zimmermann *Obligations* 701; F Dorn "§§ 134-137: Nichtigkeit I" in M Schmoeckel, J Rückert & R Zimmermann (eds) *Historisch-kritischer Kommentar zum BGB, Band I, Allgemeiner Teil: §§ 1-240* (2003) para 17 ("*HKK*"); *MüKo* § 134 para 119.

14 *HKK* §§ 134-137 para 13.

15 Para 18.

16 *MüKo* § 134 para 43-45.

17 BS Markesinis, H Unberath & A Johnston *The German Law of Contract: A Comparative Treatise* 2 ed (2006) 243.

18 243.

separately. This is because a *Verbotsgesetz* may nevertheless require a result other than voidness.[19]

3 2 3 Transactions contrary to public morals

Most legal rules in Germany derive from legislation. However, a transaction may also be invalidated if it conflicts with certain norms of society that are not contained in a specific legislative provision. Thus, § 138 I BGB provides that a contract that violates good morals (*gute Sitten*) is void.[20]

The difficulty with this provision is how to determine the content of the term good morals. The BGH's definition of "the sense of decency of all fair and right-thinking persons" is typically quoted as a point of departure,[21] although it is also admitted that this formulation is quite unhelpful.[22] Commentators instead take the view that *gute Sitten* refer to a set of core values that underlie the legal order.[23] These values include notions like equality, autonomy in private dealings and the protection of public institutions.[24]

One of § 138 I BGB's most important functions is to provide a doorway for importing policy considerations into private law. A particularly important aspect of this function is that the provision facilitates the indirect horizontal application of constitutional rights or values in private-law disputes (*mittelbare Drittwirkung*).[25] Thus, according to the German Constitutional Court, when determining whether a transaction violates good morals, the courts must have regard to values enshrined in the Basic Law ("GG").[26] These values may then in turn protect private interests.

A more controversial application of § 138 I BGB's is to invalidate transactions that are regarded as immoral by society, although this function nowadays bears a close resemblance to the previous category. The views of society have of course significantly changed over time, so many of the older cases in this category are only

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19 *MüKo* § 134 para 119.
20 For an account of how the concept of good morals or *boni mores* developed from Roman law, see Zimmermann *Obligations* 706-713.
21 BGHZ 10, 232. The German formulation reads: "Anstandsgefuhl aller billig und gerecht Denkenden." See also BGH NJW 2009, 1346 para 10.
22 C Armbrüster "§ 138" in FJ Säcker, R Rixecker, H Oetker, & B Limperg (eds) *Münchener Kommentar zum Bürgerlichen Gesetzbuch* (2018) para 14 n 85.
23 H Mansel "§ 138" in R Stürner (ed) *Jauernig - Bürgerliches Gesetzbuch Kommentar* 16 ed (2015) para 8*; MüKo* § 138 para 11.
24 *MüKo* § 138 para 11.
25 Markesinis et al *Law of Contract* 37-40; *MüKo* 138 para 20.
26 BVerfG NJW 1958, 257; BVerfG NJW 1994, 38.

of historical interest.[27] The most prominent area of application today relates to transactions that harm the institutions of family life (*Familienordnung*), such as the institution of marriage.[28]

A final important field in which § 138 I BGB may apply is where one party has unjustifiably exploited another's weakness to gain an advantage. Originally, the intention of the BGB's drafters was for § 138 II BGB to fulfil this function.[29] However, the requirements of § 138 II have been interpreted so narrowly by the courts that it became very difficult to invalidate a contract under this provision.[30] As an alternative, the courts have increasingly applied § 138 I BGB with requirements that have been watered down in these cases.[31]

3 2 4 Duties of restitution arising from illegal transactions

Thus far the focus has been on the enforceability of contracts that infringe legal rules. We have seen that these contracts are typically void, but that in some cases a statute may be interpreted as not requiring voidness. However, where a contract is found to be contrary to public policy, voidness follows as a necessary result. The next question to consider is whether a party to such an illegal contract may obtain restitution for any transfers they have made.

It has been noted above that South African law notionally recognises a general enrichment action, but that the practice is still to sue under one of the specific Roman *condictiones* when instituting an enrichment claim.[32] In the case of a transfer with an illegal foundation, the appropriate action is the *condictio ob turpem vel iniustam*

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[27] H Kötz "Die Ungültigkeit von Verträgen wegen Gesetz- und Sittenwidrigkeit: Eine rechtsvergleichende Skizze" (1994) 58 *RabelsZ* 209 211.

[28] For example, an engagement entered into by someone who is already engaged to someone else is void (RGZ 105, 245).

[29] § 138 II BGB provides: "In particular, voidness attaches to a legal transaction, whereby one person through exploitation of the distressed situation (*Zwangslage*), inexperience (*Unerfahrenheit*), lack of the ability to form a sound judgment (*Mangel an Urteilsvermögen*) or grave weakness of will (*erhebliche Willensschwäche*) of another, causes economic advantages to be promised or granted to himself or to a third party in exchange for a performance, and these advantages exceed the value of the performance to such an extent that, under the circumstances, there is a striking disproportion between them." Translation from JE du Plessis "Threats and Excessive Benefits or Unfair Advantage" in HL MacQueen & R Zimmermann (eds) *European Contract Law — Scots and South African Perspectives* (2006) 161.

[30] J Gordley "Equality in Exchange" (1981) *California LR* 1587 1630; Markesinis et al *Law of Contract* 251.

[31] A party wishing to escape liability now only has to show that the advantaged party displayed a reprehensible attitude by exploiting the "precarious situation" of the disadvantaged party; RGZ 150, 1; Gordley (1981) *California LR* 1630.

[32] See 2 4 above.

causam. German law on the other hand contains a fully-fledged general enrichment action. § 812 I(1) BGB reads:

> "Wer durch die Leistung eines anderen oder in sonstiger Weise aufdessen Kosten etwas ohne rechtlichen Grund erlangt, ist ihm zur Herausgabe verpflichtet."
>
> "A person who through an act performed by another or in any other way, acquires something at the expense of that other person without legal ground, is bound to render restitution."[33]

But despite the adoption of this general clause, the Roman *condictiones* have not become irrelevant. This is because some of the other provisions in the BGB cannot be meaningfully understood without reference to the system of the *condictiones*.[34] § 812 I(1) BGB is essentially a conflation of the *condictio indebiti* and *condictio sine causa.* In addition, other actions such as the *condictio ob turpem vel iniustam causam* were codified separately.[35] However, in practice § 817(1) BGB is hardly, if ever, applied because every case where it may have been applicable is also covered by § 812 BGB.[36]

A further difficulty arises if one considers § 817(2) BGB:

> "Die Rückforderung ist ausgeschlossen, wenn dem Leistenden gleichfalls ein solcher Verstoß zur Last fällt, es sei denn, dass die Leistung in der Eingehung einer Verbindlichkeit bestand; das zur Erfüllung einer solchen Verbindlichkeit Geleistete kann nicht zurückgefordert werden."
>
> "The claim for restitution is barred if the person performing has committed a similar infringement unless the performance consisted in entering into an obligation; what has been given for the performance of such an obligation may not be demanded back."[37]

This is essentially a codification of the *par delictum* rule, which bars restitution if the claimant is also tainted by illegality.[38] The problem with this provision is determining to which *condictio* it refers. Its location in the BGB would suggest that it refers to the *condictio ob turpem vel iniustam causam* contained in the same paragraph. However, if this were true then it would lead to an absurd situation. A claimant tainted by illegality

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33 Translation from Zimmermann & Du Plessis (1994) *RLR* 14.

34 20.

35 18-19. For example § 817(1) BGB provides: "[T]he recipient is liable to render restitution if the purpose of the transfer was of such a nature that its acceptance constitutes an infringement of a statutory prohibition or is contrary to *boni mores*" (Translation from Zimmermann & Du Plessis (1994) *RLR* 19).

36 S Lorenz in N Horn (ed) *J von Staudingers Kommentar zum Bürgerlichen Gesetzbuch mit Einführungsgesetz und Nebengesetzen, Buch 2, Recht der Schuldverhältnisse §812-822 (Ungerechtfertigte Bereicherung)* § 817 para 6 ("*Staudinger*"); Häcker "Illegality and Immorality" in *Illegality after* Patel v Mirza 355.

37 Translation from Zimmermann & Du Plessis (1994) *RLR* 22.

38 See 2 4 above. In Germany the rule is known as the *in pari turpitudine* rule; G Dannemann *The German Law of Unjustified Enrichment and Restitution: A Comparative Introduction* (2009) 80.

could sidestep the rule by simply suing under § 812 BGB because that provision also covers transfers flowing from illegal contracts.[39] The German courts have therefore held that § 817(2) BGB covers all the *condictiones* contained in the other provisions of the BGB.[40]

A further textual difficulty with § 817(2) BGB is the fact that it refers to a state of affairs where the claimant has committed a *similar infringement* to that of the recipient. The problem with this formulation is best explained with an example. Suppose A, the claimant, has made a transfer to B, the recipient. If both parties acted illegally, A's claim would be barred by § 817(2) BGB. However, if only A acted illegally, the claim would succeed since the infringement cannot be 'similarly' illegal when compared to the conduct of B. This leads to the anomalous result that an innocent recipient must return what they received but one who acted illegally need not do so.[41] The courts have therefore also applied § 817(2) BGB to cases where only the claimant had acted illegally, despite the fact that this goes directly against the wording of the provision.[42] Sensible as this solution may appear, it has also created further problems.

A particularly challenging scenario concerns the extension of a usurious loan. Depending on the circumstances, it may be quite unpalatable to allow the recipient of the loan to retain the capital without having to repay it.[43] The German courts have managed to exclude the operation of § 817(2) BGB in this particular scenario by holding that the performance (*Leistung*) contemplated by § 817(2) is not the transfer of money itself, but rather the granting of the ability to use the money for a certain period of time.[44] This means that an enrichment claim would still be allowed after the stipulated timeframe for the loan has expired.[45]

The scenario of the usurious loan also illustrates a broader point. The categorical exclusion of enrichment claims that involve illegality on the part of the claimant may at times yield harsh and unsatisfactory results.[46] German law therefore recognises limited exceptions where the operation of § 817(2) BGB is excluded.

The primary mechanism for circumventing § 817(2) BGB is the doctrine of

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39 *Staudinger* § 817 para 10.
40 See the authorities cited in M Schwab "§ 817" in M Habersack (ed) *Münchener Kommentar zum Bürgerlichen Gesetzbuch* 8 ed (2020) para 11 n 34.
41 Zimmermann *Obligations* 863; Zimmermann & Du Plessis (1994) *RLR* 23.
42 Zimmermann & Du Plessis (1994) *RLR* 23; *MüKo* § 817 para 48.
43 Zimmermann *Obligations* 863.
44 *Staudinger* § 817 para 12; *MüKo* § 817 para 49.
45 Dannemann *Unjustified Enrichment* 83.
46 83.

teleologische Reduktion.[47] The idea of this doctrine is that § 817(2) BGB should not be applied if doing so would undermine the purpose of the prohibition even more than if the enrichment claim were allowed.[48] A case of the BGH dealing with a gift circle (*Schenkkreis*) provides a good illustration.[49] The scheme was that new donors to the circle would pay a fee that was then distributed among existing members. In turn, these new donors would receive the fees from the next round of donors and so forth. As with all schemes of this nature, everything eventually collapses once new members can no longer be found. The BGH held that the entry payments were void in terms of § 138 BGB. However, despite finding that both the old and new participants to the scheme knowingly acted illegally, the court nevertheless allowed the enrichment claims of the new donors. The reasoning was that if the claims were barred, the illegal state of affairs would be perpetuated since the recipients would profit from their unlawful conduct.

A second exception to the application of § 817(2) BGB concerns the requirement of knowledge on the part of the claimant. Where a claimant unknowingly transgressed the law, the claim will still be allowed.[50] The justification for this rule is that the purpose of precluding claims tainted by illegality, namely, to deter wrongdoing, is only meaningfully served where a claimant has knowingly stepped outside the bounds of the law.[51]

Finally, in some exceptional instances a claimant might be able to avoid the operation of § 817(2) BGB by relying on the general duty of good faith contained in § 242 BGB.[52] The provision broadly requires debtors to perform in the manner required by good faith. Its scope is, however, considerably wider than the wording suggests.[53] In some earlier cases dealing with clandestine labour (*Schwarzarbeit*), the BGH

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47 *MüKo* § 817 para 22.

48 Gleim (2018) *ERPL* 236; L Klöhn "Die Kondiktionssperre gem. § 817 S. 2 BGB beim beidseitigen Gesetzes- und Sittenverstoß: Ein Beitrag zur Steuerungsfunktion des Privatrechts" (2010) 210 *AcP* 804 813-815.

49 BGH NJW 2006, 45. See also *MüKo* § 817 para 24.

50 *Staudinger* § 817 para 21; Klöhn (2010) *AcP* 810.

51 *MüKo* § 817 para 85. This idea is known as the *Rechtschutzverweigerungstheorie*; see HJ van Kooten "Illegality and Restitution as a Matter of Policy Considerations: A Comparative Analysis of Dutch, English and German Law" (2001) 9 *RLR* 67 68-69.

52 A Stadler "§ 812" in R Stürner (ed) *Jauernig - Bürgerliches Gesetzbuch Kommentar* 16 ed (2015) para 14. One could also consider the reliance on § 242 BGB as another instance of *teleologische Reduktion.*

53 See generally JP Schmidt "Art 1:201: Good Faith and Fair Dealing" in N Jansen & R Zimmermann (eds) *Commentaries on European Contract Laws* (2018) 100; J du Plessis "Giving Practical Effect to Good Faith in the Law of Contract" (2018) 3 *Stell LR* 379.

allowed a builder's claim for services rendered despite the fact that the builder had knowingly concluded a contract that was illegal.[54] Although the court accepted that the claim should in principle be defeated by § 817(2) BGB, it was held that the provision should not apply on the basis of good faith. These decisions have been heavily criticised[55] and the courts now unequivocally refuse restitution in *Schwarzarbeit* cases.[56]

Accordingly, while German law does recognise some cases where the operation of the *in pari turpitudine* rule is relaxed, the scope is considerably more modest than in South African law.[57]

3 3 English law

3 3 1 Introduction

Illegality has historically been one of the most complicated and confusing areas of English private law. There are at least three reasons for this. The first is that courts and commentators have tended to use confusing language when discussing issues surrounding illegality. Terms like 'void,' 'voidable,' 'unenforceable' and 'illegal' have not been rigorously distinguished and tend to be used interchangeably.[58] A further problem is the impact of the so-called reliance rule, which provides that an action must fail if the plaintiff is required to rely on its own illegality to assert the claim.[59] The strictness of this rule has compelled courts to contort facts and create complicated exceptions in an effort to avoid patently unjust results. That is the second reason. Flowing from the first two is the final reason. The case law on illegality has been described as very unclear and even arbitrary.[60] Fortunately matters have been simplified to some extent by the UK Supreme Court in the leading case of *Patel v Mirza* ("*Patel*").[61] The focus of this section will therefore be on the impact of *Patel*.

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54 The classic example is BGHZ 111, 308. See also BGHZ 176, 198; in this *Schwarzarbeit* case, the BGH managed to award damages to an employer, despite the illegality of the contract. In its reasoning the court also relied on heavily on § 242 BGB.

55 *Staudinger* § 817 para 10.

56 BGHZ 198, 141. See 4 4 5 below.

57 See 2 6 above.

58 A Burrows "A New Dawn for the Law of Illegality" in S Green & A Bogg (eds) *Illegality after Patel v Mirza* (2018) 23 25. For the purposes of this section only, "void" and "unenforceable" are treated as synonyms.

59 *Bowmakers Ltd v Barnet Instruments Ltd* [1945] 1 KB 65 71

60 Law Commission of England and Wales *The Illegality Defence* Consultation Paper No 189 (2009) 35-36.

61 [2016] UKSC 42.

Two further points should be made by way of introduction. The current approach to illegality is not limited to the law of contract but applies to the whole of English private law.[62] As we shall see, many of the cases relevant to contract law actually dealt with torts, trusts or unjust enrichment. Secondly, for the sake of brevity it is not possible to consider the question of how to determine whether a contract is illegal here.[63] That is on its own a topic of considerable complexity and lies beyond the scope of what this section seeks to achieve.

3 3 2 Statutory illegality

English textbooks typically distinguish between statutory illegality and illegality at common law.[64] In the South African context this distinction refers to the source of the illegality. However, English commentators are careful to point out that in English law the distinction instead refers to the effect of the illegality on the contract and not its source.[65] It is said that the question of whether the statute requires the contract to be unenforceable is a separate inquiry from whether the contract is unenforceable at common law.[66] This distinction does little to illuminate matters.[67] The reason is that when courts find a contract unenforceable due to illegality and a statutory offence is involved, they make little effort to specify whether the voidness results from the statute itself or from the common law doctrine of illegality.[68] And so, despite drawing the distinction, it is also admitted that there is a considerable degree of convergence between the considerations taken into account in both situations.[69] To the extent that one may discern a meaningful difference between the categories two cases are frequently cited as examples of statutory illegality.

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62 Burrows "A New Dawn" in *Illegality after* Patel v Mirza 33-34.

63 See generally E Peel *Treitel on the Law of Contract* 14 ed (2015) ch 11 2; MP Furmston "The Analysis of Illegal Contracts" (1965) 16 *Toronto LJ* 267. Most English textbooks divide illegal contracts into three categories: contracts with an illegal subject matter, contracts with an illegal purpose and contracts performed in an unlawful manner.

64 *Okedina v Chikale* [2019] I.C.R. 1635 para 12-14; RA Buckley *Illegality and Public Policy* (2002) 10; Burrows *Restatement* 235; Law Commission *Illegality Defence* 18.

65 J Beatson, A Burrows & J Cartwright *Anson's Law of Contract* (2020) 410.

66 Law Commission *Illegality Defence* 18.

67 See for example *Ochroid Trading Ltd v Chua Siok Lui* [2018] SGCA 5 para 114-115, where the Singapore Court of Appeal described the distinction between statutory illegality and illegality at common law in England as "unprincipled."

68 Buckley *Illegality and Public Policy* 11.

69 Burrows *Restatement* 235. In *Okedina v Chikale* [2019] I.C.R. 1635 para 58 the Court of Appeal remarked that "[T]he distinction is in truth largely at the level of theory, since the same underlying principles are involved."

The first is *Re Mahmoud and Ispahani*.[70] Legislation at the time prohibited the sale and purchase of linseed oil without the necessary licence. The defendant sought to purchase linseed oil without the licence, although he had represented to the claimant that he did have one. The defendant then refused to accept delivery of the oil. The court dismissed the claimant's action for damages as a result of the non-acceptance, since the legislation prohibited the transaction. Allowing the claim to succeed would have undermined the purpose of the statute.

The second example is *St John Shipping Corporation v Joseph Rank Ltd*.[71] Here the claimant was contracted to carry grain for the defendants. The vessel carrying the goods was overloaded, which amounted to a statutory offence. However, as a result of the overloading, the claimant stood to earn extra freight. The defendants refused to pay the extra freight on the basis that the contract was performed in an illegal manner. However, the court awarded the claim because it found that Parliament could not have intended for the contract to be unenforceable, since that would mean that the claimants were not entitled to any freight at all. Such a result would impose a further penalty in addition to the criminal sanction already prescribed. Devlin J held that, as a general principle, courts should be hesitant to find that a statute intends to interfere with ordinary rights and remedies in a contract in the absence of a clear implication, since a great number of statutes which govern economic activity may be infringed without malicious intent.[72]

Not much more needs to be said here about statutory illegality. Ultimately the impact of a statute will depend on how the court construes it. As the two examples illustrate, consequences may range from complete unenforceability to no impact at all on the tainted contract.[73] Far more instructive for comparative purposes is the development of the illegality doctrine in the common law.

Before turning to the common law, there is one further point that is worth noting. *St John Shipping* is considered one of the leading judgments on the doctrine of illegality in the English law. However, in South Africa and many civilian jurisdictions the facts of *St John Shipping* would probably not be considered a case of an illegal contract. In these systems, the general view is that an illegal manner of performance does not

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70 [1921] 2 KB 716.
71 [1957] 1 QB 267. Confusingly, Buckley argues that this was in fact a case of common-law illegality; Buckley *Illegality and Public Policy* 11.
72 [1957] 1 QB 267 288.
73 For a comprehensive treatment of statutory illegality, see Buckley *Illegality and Public Policy* 10-32.

typically affect the enforceability of the contract itself. It only impacts on the rights of the parties where it amounted to a breach of the contract.[74]

By contrast, English law recognises a specific doctrine of performance illegality. Under this doctrine, it would appear that performing a contract in an illegal manner, whether in violation of a statute or the common law, may sometimes render the contract itself unenforceable, but it is not entirely clear when and why.[75] The cases in this area are difficult to reconcile and as a result, the operation of this doctrine remains quite uncertain.[76] The important point for present purposes is simply that jurisdictions do not necessarily agree on the classes of fact patterns that should be included under the notion of an 'illegal contract.'

3 3 3 The reliance rule

The classic statement of the reliance rule is credited to Lord Mansfield in *Holman v Johnson* ("*Holman*"):

> ''The principle of public policy is this: ex dolo malo non oritur actio. No court will lend its aid to a man who founds his cause of action upon an immoral or an illegal act. If from the plaintiff's own stating or otherwise, the cause of action appears to arise ex turpi causa, or the transgression of a positive law of this country, there the court says he has no right to be assisted. It is upon that ground the court goes; not for the sake of the defendant, but because they will not lend their aid to such a plaintiff. So, if the plaintiff and defendant were to change sides, and the defendant was to bring his action against the plaintiff, the latter would not then have the advantage of it; for where both are equally in fault, potior est conditio defendentis.''[77]

Although there is no mention of the word 'reliance' in the passage quoted from *Holman*, the idea expressed by Lord Mansfield became known over time as the reliance rule. As an abstract proposition it means that a claim cannot be enforced if a claimant has to rely on their own illegal conduct in order to establish their cause of action.[78] Suppose A and B agree to work together in order to steal some diamonds and divide the spoils equally among themselves. B then decides to flee with all the stolen diamonds once the theft has been performed. If A were to sue B for his share of the loot, the reliance

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74 See LF van Huyssteen, GF Lubbe, MFB Reinecke & JE du Plessis *Contract - General Principles* 6 ed (2020) 219-220; S Meier "Illegality" in N Jansen & R Zimmermann (eds) *Commentaries on European Contract Laws* (2018) 1905.

75 Law Commission *Illegality Defence* 26. See also *Hall v Woolston Hall Leisure Ltd* [2001] 1 WLR 225 246.

76 Compare *Anderson Ltd v Daniel* [1924] 1 KB 138; *Archbolds (Freightage) Ltd v S Spanglett Ltd* [1961] 1 QB 374; *Ashmore, Benson, Pease and Co Ltd v Dawson* [1973] 1 WLR 828. See also Buckley *Illegality and Public Policy* 33-41.

77 (1775) 1 Cowp. 341 343.

78 A Burrows *Restatement of the English Law of Contract* (2016) 224.

rule would prevent him from enforcing his contract with B. The reason is that A would be *relying* on an illegal contract since it is an agreement to commit the crime of theft.

A further point illustrated by the passage in *Holman* is that English law recognises functional equivalents of the *ex turpi* and *par delictum* maxims. However, unlike South Africa, the two do not seem to be rigorously distinguished.[79] Since *Holman,* both maxims have been frequently quoted in the context of contractual claims as well as in cases dealing with unjust enrichment, trusts, torts, and proprietary interests.[80] However, as we have seen above, these sayings have a tendency to cause confusion and should be handled with caution.[81]

The most prominent modern treatment of the reliance rule is the decision of the House of Lords in *Tinsley v Milligan* ("*Tinsley*").[82] The facts were as follows. The parties jointly contributed to the purchase of a home, but the property was registered in Tinsley's name only. They shared a mutual understanding that they were the joint beneficial owners. The reason for this was so that Milligan could make false benefit claims from the Department of Social Security. The parties used a small portion of the money obtained in this way to pay for the property while the rest was used to pay their bills. The scheme continued for several years until one day, when Milligan confessed her fraud to the Department. The relationship between the parties soured and Tinsley moved out of the house. She then instituted eviction proceedings against Milligan, who in turn sought a declaration that Tinsley held the property on trust for the two of them in equal shares.[83] Tinsley argued that Milligan's claim was barred due to the illegality.

The court found in favour of Milligan. Lord Browne-Wilkinson, writing for the majority, accepted that the Milligan's claim would fail if she were required to rely on evidence of her illegal behaviour. However, he found that she did not need to do so. It was sufficient for her to prove that she had contributed to the purchase of the house, received nothing in exchange from Tinsley and that legal title to the house had vested in Tinsley's name only. In other words, the court was able to 'ignore' the reason why the house had been put in Tinsley's name in the first place.

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79 Burrows *Restatement* 221; *Lissenden v C A V Bosch Ltd* [1940] AC 412 435.
80 See for example *Hardy v Motor Insurers' Bureau* [1964] 2 QB 745 767.
81 2 4 above.
82 [1993] 3 All ER 65.
83 This was said to be a resulting trust, which arises when a settlor makes a voluntary purchase of property in the name of a trustee or in both their names. In such a scenario the beneficial interest is presumed to remain vested in the settlor; *Gissing v Gissing* [1971] AC 886 905; PH Pettit *Equity and the Law of Trusts* 12 ed (2012) 68-70.

This case has been heavily criticised for its reasoning over the years.[84] A central theme is the point that the reliance rule operated as a procedural rather than a substantive defence for the party resisting the claim. In other words, the outcome of a case was determined with reference to the technicalities of pleading rather than the underlying policy considerations at stake. This meant that the rule had a propensity to generate unduly harsh and even arbitrary results.[85] In an attempt to avoid unjust results the courts created numerous complicated exceptions[86] or massaged the facts of difficult cases to reach the desired outcome.[87]

And so matters continued until the uncertainty reached its apex in a trio of cases where members of the Supreme Court split on the proper approach to illegality.[88] The tension was finally resolved in *Patel,* to which we now turn.

3 3 4 *Patel v Mirza*

The facts were quite simple. Patel transferred about £620 000 to Mirza under an agreement that Mirza would use the money to bet on the price movement of shares by illegally relying on inside information. However, the information anticipated by Mirza never materialised, which meant that the scheme could not be carried out. Mirza subsequently failed to pay Patel back despite promises to do so. Patel then sued Mirza for the return of the money. It was common cause that the agreement between the parties amounted to a conspiracy to commit the offence of insider dealing.[89] The obstacle for Patel was therefore that he had to explain the nature of his agreement with Mirza. This is because the category of unjust enrichment his claim was based on, namely failure of consideration, required a claimant to show in the first place what the consideration in question was.[90]

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84 See Burrows *Restatement* 225-229 for a summary of the main criticisms.

85 In *Tinsley* itself for example Lord Goff, in a dissenting judgment, said: "I recognise, of course, the hardship which the application of the present law imposes upon the respondent in his case; and I do not disguise my own unhappiness at the result"; [1993] 3 All ER 65 80.

86 See G Virgo *The Principles of the Law of Restitution* 3 ed (2015) 717-724; C Mitchell, P Mitchell & S Watterson *Goff and Jones on the Law of Unjust Enrichment* 9 ed (2016) 889.

87 Law Commission *Illegality Defence* 34-35.

88 *Hounga v Allen* [2014] UKSC 47; *Les Laboratoires Servier v Apotex Inc* [2014] UKSC 55; *Bilta (UK) Ltd v Nazir (No 2)* [2015] UKSC 23.

89 In terms of section 52 of the Criminal Justice Act 1993.

90 *Patel* [2016] UKSC 42 para 13. The term of 'failure of consideration' in the context of unjust enrichment is no longer accepted as correct by authors because of its tendency to be confused with the technical meaning of consideration in the law of contract. The term now preferred is 'failure of basis.' See Virgo *Restitution* 308; P Birks "Recovering Value Transferred under an Illegal Contract" (2000) 1 *Theoretical Inq L* 155 161.

Much of the argument in the courts below turned not on whether the claim was barred by illegality, but on whether the claim could be located within an exception to the reliance rule known as the doctrine of *locus poenitentiae* – that restitution could be allowed if the claimant had withdrawn timeously from the illegal scheme.[91] However, the majority of the Supreme Court considered this focus to be incorrect.

Lord Toulson, writing for the majority, rejected the rule-based approach in *Tinsley* and endorsed the 'range of factors' approach proposed by the Law Commission[92] instead. He distilled from the case law a trio of relevant considerations that a court must consider:

> "[O]ne cannot judge whether allowing a claim which is in some way tainted by illegality would be contrary to the public interest, because it would be harmful to the integrity of the legal system, without a) considering the underlying purpose of the prohibition which has been transgressed, b) considering conversely any other relevant public policies which may be rendered ineffective or less effective by denial of the claim, and c) keeping in mind the possibility of overkill unless the law is applied with a due sense of proportionality."[93]

The first two factors are quite straight-forward. However, explicitly recognising proportionality as a relevant consideration has been regarded as an innovation for private law and garnered considerable academic attention recently.[94] Since the concept is somewhat open-ended, some uncertainty remains as to what is meant by applying the law "with a due sense of proportionality". Lord Toulson did not lay down a conclusive list of factors which must be considered here but regarded the following as potentially relevant: the seriousness of the conduct, its centrality to the transaction, whether the transgression was intentional and whether there is a marked disparity in the respective culpability of the parties.[95]

It is clear from the majority in *Patel* that this 'range of factors' approach is meant to apply to all areas of private law and that the impact of illegality will depend on the context.[96] However, at least in the law of unjust enrichment, Lord Toulson clarified that if a claimant would ordinarily be entitled to restitution in the absence of illegality, its

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91 [2013] EWHC 1892 (Ch); [2014] EWCA Civ 1047. On the relevance of *locus poenitentiae* after *Patel*, see G Virgo "Illegality and Unjust Enrichment" in Green & Bogg (eds) *Illegality after* Patel v Mirza (2018) 213 229.

92 Law Commission *Illegality Defence* 147.

93 *Patel* [2016] UKSC 42 para 101.

94 E Lim & FJ Urbina "Understanding Proportionality in the Illegality Defence" (2020) 136 *LQR* 575; ZX Tan "The Proportionality Puzzle in Contract Law: A Challenge for Private Law Theory?" *Can J Law Jurisprud* 33 (2020) 215.

95 *Patel* [2016] UKSC 42 para 107.

96 This point has been confirmed by the Supreme Court in *Henderson v Dorset Healthcare University NHS Foundation Trust* [2020] UKSC 43 para 76.

presence should rarely defeat the claim, although there may be exceptional cases involving serious crimes such as murder or drug trafficking.[97] The implicit reason is that the claimant is trying to unwind the illegality rather than enforce it.[98]

On the facts it was held that Patel had satisfied the ordinary requirements for a claim in unjust enrichment. He was therefore entitled to restitution since the result would not undermine the purpose of the prohibition on insider dealing.

In the wake of *Patel,* there was some uncertainty as to whether the old cases on illegality were still of any relevance.[99] It is now settled that the approach in *Patel* should be used as a lens through which to read older cases.[100] In other words, where courts rely on authorities predating *Patel*, the outcomes of those cases must be justified in terms of the underlying policies. The older cases therefore retain their precedential value unless it can be shown that they are incompatible with *Patel*.[101]

To sum up, in English law policy considerations will rarely require that illegality defeats an enrichment claim that is otherwise good in law. That concludes the exposition on restitution, but what does *Patel* mean for the enforceability of a contract tainted by illegality? That is the next question to be considered.

3 3 5 Enforceability after *Patel*

The question of enforceability in the present context relates to whether illegality excludes contractual remedies for breach of contract, such as damages or specific performance. This question was not directly addressed in *Patel* and remains quite uncertain.[102] As we have seen, the 'range of factors' approach was clearly intended to also apply to contractual enforceability, but how exactly it works in practice has not been spelled out.[103]

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97 *Patel* [2016] UKSC 42 para 116.

98 Burrows "A New Dawn" in *Illegality after* Patel v Mirza 27.

99 A good example is *Parkinson v College of Ambulance Ltd* [1925] 2 KB 1. A donation made in return for a knighthood could not be recovered when the honour failed to materialise. Lord Toulson discussed this case but left open its correctness in *Patel* [2016] UKSC 42 para 118. In Germany, a payment to secure some title or honours that failed to materialise cannot be recovered with an enrichment claim; BGH NJW 1994 187.

100 *Okedina v Chikale* [2019] IRLR 905 para 62; Burrows "A New Dawn" in *Illegality after* Patel v Mirza 37-38.

101 *Henderson v Dorset Healthcare University NHS Foundation Trust* [2020] UKSC 43 para 77.

102 In *Ronelp Marine Ltd v STX Offshore & Shipbuilding Co Ltd* 106 EWHC 2228 (Ch) para 37 Norris J said that the question of how the approach in *Patel* applies to illegality in the context of contractual enforcement remains "uncertain to an exceptional degree."

103 See J O'Sullivan "Illegality and Contractual Enforcement*"* in Green & Bogg (eds) *Illegality after* Patel v Mirza (2018) 165.

It would appear that little has changed from the old position in this context, since the underlying policy considerations operate differently here than in the case of unjust enrichment. At least where statutes have been contravened, the courts have always managed to enforce tainted contracts under the mantle of statutory interpretation where it was deemed appropriate, such as in *St John Shipping*. Moreover, it has also always been clear that the courts will not enforce a contract that is clearly prohibited. The reason, which was made explicit in *Patel,* is that refusing to enforce a prohibited contract is necessary to preserve the integrity of the legal system.[104] Enforcing an illegal contract means carrying out the illegal scheme of the parties, whereas restitution unwinds the illegality instead. Therefore, just as illegality will not *prima facie* defeat a claim for restitution, it will *prima facie* bar the enforcement of a contract. The impact of *Patel* on future cases will therefore probably not be to give rise to significantly different results than under the previous position. Instead, it will only make the reasoning used to arrive at those results more transparent.

Nevertheless, it is worth stressing that although illegality will generally bar contractual enforcement, the 'range of factors' approach may in some cases also yield a different result. The case of *ParkingEye Ltd v Somerfield Stores Ltd* ("*ParkingEye*") illustrates the point.[105] Although decided before *Patel*, the Court of Appeal in this matter applied a range of factors approach very similar to the method laid down in *Patel* in the context of contractual enforcement.

The case concerned a contract in terms of which ParkingEye undertook to manage several supermarket car parks owned by Somerfield. ParkingEye's main obligation was to collect fines from those who overstayed the free parking time allowed. Its method was to send a series of aggressive letters to fine recipients. Some of these letters also deliberately contained information that was false. In addition, the evidence showed that ParkingEye had intended to use these misleading letters from the time they had concluded the contract. Somerfield repudiated the contract, which would ordinarily entitle ParkingEye to contractual damages. However, Somerfield raised illegality as a defence, arguing that ParkingEye had illegally performed its obligation under the contract. That is because sending out the letters which contained the false

[104] *Patel* [2016] UKSC 42 para 115.
[105] [2012] EWCA Civ 1338.

information gave rise to the tort of deceit if it induced the recipient to pay a debt that was not owed.

The court upheld the claim for damages. It considered that ParkingEye did not fully appreciate that aspects of its performance were unlawful and so did not have a "fixed intention" to act unlawfully, that the illegality was relatively trivial and not central to the contract between the parties and, most importantly, that denying ParkingEye's claim for damages would be a disproportionate response to the illegal conduct. This is for the time being the best illustration of how the range of factors approach applies in the context of contractual enforcement.[106] While it has been argued here that illegality will still generally bar a claim for contractual enforcement, a case such as *ParkingEye* shows that the issue ultimately depends on the relevant policies and facts of each case.[107]

3 3 6 Illegal contracts and the claim for quantum meruit

After *Patel* it seems clear that the English courts have little appetite left for allowing illegality to defeat an enrichment claim. An issue that remains to be considered is the extent to which the law can be stultified, as Birks put it, by awarding a different remedy when the claim for enforcement of the contract is unavailable as a result of illegality.[108] To stultify means to make a fool of something. Birks used the concept to capture the idea that "the law as stated in one area should not make nonsense of the law is it is stated in another."[109]

Where the enforcement of a contract is denied due to illegality, awarding a different remedy carries this risk. Although it is beyond the scope of this chapter to engage with Birks's thesis, it is worthwhile from a comparative perspective to discuss one particular

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[106] It is worth noting that this was also a case of so-called performance illegality; see 3 3 2 above.

[107] The two most recent cases in which the Supreme Court applied *Patel* dealt with claims in tort. See *Stoffel & Co v Grondona* [2020] UKSC 42 (where the illegality defence failed) and *Henderson v Dorset Healthcare University NHS Foundation Trust* [2020] UKSC 43 (where it succeeded). Illegality is not recognised as a defence to a delictual claim in South African law; *Minister of Police v Underwriters at Lloyds of London* 2021 ZASCA 72 para 14.

[108] Birks (2000) *Theoretical Inq L* 155. See also *Boissevain v Weil* [1950] AC 327 341 and the famous Canadian case *Hall v Hebert* [1993] 2 SCR 159.

[109] Birks (2000) *Theoretical Inq L* 160. The thrust of his argument is that almost all the cases where illegality was said to defeat a claim for restitution, the actual underlying reason for denying the claim was to avoid stultifying the law and conversely, that the cases where restitution was allowed were correct to the extent that they did not cause stultification. Birks's analysis has been particularly influential in Australia (*Equuscorp Pty Ltd v Haxton* [2012] HCA 7 para 45) and Singapore (*Ochroid Trading Ltd v Chua Siok Lui* [2018] SGCA 5 para 139-159).

remedy which could in principle lead to stultification, namely awarding a claim for quantum meruit under an illegal contract.

The claim for quantum meruit is a restitutionary remedy awarded for the reasonable value of services rendered under a failed contract.[110] Arguably the most prominent case illustrating how this remedy may operate in the context of illegality is *Mohamed v Alaga & Co*.[111] The claimant was a Somali translator who had an arrangement with a solicitors' firm that he would introduce Somali clients to the firm and provide translation services. In return he would receive a share of the solicitors' fees generated from these clients. This kind of arrangement was prohibited by rules promulgated under the Solicitors Act 1974. When the solicitors failed to pay, the claimant sought to recover the fees. Although the translator's claim to enforce the contract was struck out as bad in law, the Court of Appeal found that he was nevertheless entitled to pursue a claim for quantum meruit. Lord Bingham, on behalf of the court, distinguished claims for breach of contract and quantum meruit. The purpose of prohibiting fee-sharing arrangements of this nature, he said, was to protect the public. That purpose would be undermined if the non-solicitor party to the agreement were allowed to enforce it in a court. The claim for quantum meruit on the other hand should not be regarded as recovering a portion of the consideration under the unenforceable contract, but rather as a reasonable reward for services rendered. A crucial feature of the case was that the parties were regarded as not equally culpable. The solicitors could reasonably be assumed to have known that the arrangement was illegal. However, the same could not be said for the claimant.

This case generated some controversy[112] but was ultimately approved in *Patel.*[113] It is easy to see why, since Lord Bingham explicitly considered the factors emphasised by Lord Toulson, in particular the purpose of the prohibition and proportionality in the sense of the relative culpability of the parties.

3 3 7 Conclusion

The approach to illegality in English law has long been regarded as unsatisfactory, confusing, and difficult to state with accuracy. The ground-breaking judgment in *Patel*

[110] Virgo *Restitution* 19. In South Africa the terminology of quantum meruit is disapproved of; see *BK Tooling (Edms) Bpk v Scope Precision Engineering (Edms) Bpk* 1979 1 SA 391 (A) 422H.
[111] [2000] 1 WLR 1815; but contrast *Awwad v Geraghty* [2001] QB 570.
[112] See Law Commission *Illegality Defence* 72-74 for a summary.
[113] [2016] UKSC 42 para 119.

has improved matters considerably. Rather than mechanically applying a strict rule or trying to fit a case into the myriad of difficult exceptions which have developed over time, courts may now exercise a discretion in order to reach the result that best gives effect to the policies underlying the illegality defence. Perhaps the most outstanding feature of the judgment is the emphasis on transparency. When deciding whether illegality ought to defeat a claim in a particular case, a court is now required to identify the policies underpinning its decision explicitly instead of applying a formal rule which had the tendency to obfuscate the underlying reasons for a particular result. And although a degree of uncertainty still lingers in some areas of application such as contract enforceability, it is likely that over time clearer guidelines will be carved out by the courts.[114]

[114] Beatson et al *Anson's Law of Contract* 421.

3 4 Illegal contracts in Scotland

3 4 1 Introduction

The law on illegal contracts in Scotland is uncertain and regarded as unsatisfactory.[115] At least part of the reason for this is that the authorities on illegality are sparse and difficult to reconcile.[116] As with other jurisdictions, it is necessary at the outset to clear some of the semantic weeds that have grown in this area of the law.

Scots law tends to use a variety of terms to describe defective contracts.[117] This includes void, voidable, null, unenforceable, and illegal.[118] The terms 'void' and 'voidable' are typically reserved for contracts dealing with a defect in consent or capacity and need not be considered here.[119]

The usage of the other terms has not been consistent over time. In early sources and the works of the Institutional writers, so-called *pacta illicita* were described as void, as is done in jurisdictions from the civilian tradition.[120] However, in modern Scots law, the main effect of illegality on a contract is described as rendering the contract unenforceable.[121] This is presumably due to the influence of English law.[122]

Scots law also recognises comparable principles to those contained in the *ex turpi* and *par delictum* maxims of South African law.[123] A court will generally not award specific implement and damages in a case where a pursuer sues on an illegal contract. Moreover, where both parties are equally at fault and there has been partial performance of the contract, the court will generally allow losses to lie where they have fallen.[124]

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[115] HL MacQueen *MacQueen and Thomson on Contract Law in Scotland* 5 ed (2020); LJ Macgregor "Illegal Contracts and Unjustified Enrichment" (2000) 4 *Edin LR* 19 45. For a historical overview see LJ Macgregor "*Pacta Illicita*" in K Reid & R Zimmermann (eds) *A History of Private Law in Scotland* (2000) 129.

[116] J Thomson "Illegal contracts in Scots law" (2002) 18 *SLT* 153.

[117] For a detailed explanation, see WW McBryde *Void, Voidable, Illegal and Unenforceable Contracts in Scots Law* PhD Thesis, University of Glasgow (1976) 165-185.

[118] WM Gloag *The Law of Contract: A Treatise on the Principles of Contract in the Law of Scotland* 2 ed (1929); WW McBryde *The Law of Contract in Scotland* 3 ed (2007) 350.

[119] MacQueen *Contract Law* 333; McBryde *Contract in Scotland* 350.

[120] Macgregor "*Pacta Illicita*" in *A History of Private Law in Scotland* 129-131, 149.

[121] 194; See also *Malik v Ali* 2004 SLT 1280 para 11. McBryde *Contract in Scotland* 357-359 distinguishes between contracts that are illegal and those that are unenforceable. He suggests that the latter developed as a distinct category from a series of eighteenth century cases before the Court of Session which dealt with smuggling contracts and gambling. This division is not followed by other authors, see Macgregor (2000) *Edin LR* n 21.

[122] Macgregor "*Pacta Illicita*" in *A History of Private Law in Scotland* 149,

[123] *Barr v Crawford* 1983 SLT 481.

[124] MacQueen *Contract Law* 341.

As for the anterior question of when a contract is illegal in the first place, it is difficult to give a clear answer. This is in part because the courts have tended to conflate the question of whether a contract is illegal with the question of whether any restitution of benefits conferred, is available.[125] At a basic level, however, there is considerable convergence between South Africa and Scotland on the categories of contracts regarded as illegal.[126] Given the conflation of the two questions, an easier method of presentation is to survey the cases on illegality first and draw conclusions from them afterwards.

3 4 2 Two conflicting cases

The *locus classicus* on illegality in Scotland is *Cuthbertson v Lowes* ("*Cuthbertson*").[127] Legislation at the time declared contracts for the sale of produce where the price was determined with reference to the Scots acre (as opposed to the Imperial acre) to be null and void. The pursuer had sold and delivered potatoes to the defender with reference to the Scots acre. The defender refused to pay, citing the illegal nature of the contract. The court held that it could not enforce the contract, but that the pursuer was entitled to recover the market value of the potatoes. In his judgment the Lord President (Inglis) stressed that the illegal contract was not the basis for awarding the market value of the potatoes to the pursuer. Although not specified, he presumably had in mind a remedy that Scots law would nowadays regard as being based on unjustified enrichment.[128]

Two factors weighed particularly heavily with the court. The first was the finding that there was no turpitude or immorality involved in the selling of potatoes by the Scots acre. In addition, the court considered that it would be inequitable for the defender to retain the potatoes without accounting for their value.[129]

The second famous case on illegality is *Jamieson v Watt's Trustees* ("*Jamieson*").[130] Wartime legislation required that licences be obtained to perform

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[125] Thomson (2002) *SLT* 153.

[126] See MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems* 148-150. Both systems recognise illegality caused by legislation as a specific category and illegality resulting from the common law or public policy as another.

[127] (1870) 8 M 1073. This case was referred to by Centlivres JA in *Jajbhay v Cassim* 1939 AD 537 558-559. See also the similar facts in *Alexander v M'Gregor* (1845) 7 D 915.

[128] The technical term is a claim for recompense. Nowadays, there is support for the notion that the basis of a duty of recompense is unjustified enrichment; Macgregor "*Pacta Illicita*" in *A History of Private Law in Scotland* 154.

[129] (1870) 8 M 1073 1075.

[130] 1950 SC 265. For a discussion, see Thomson (2002) *SLT* 153.

certain building works. The pursuer worked as a joiner and had a licence to perform work to the value of £40. However, in violation of the regulations, he performed work for the defender to the value of £114. After the defender refused to pay the balance of the unauthorised work, the pursuer sought to claim the money by relying on *Cuthbertson*. The court dismissed the claim by holding that *Cuthbertson* was a unique case which should be confined to its particular circumstances. The reasoning was that the effect of the statute in *Cuthbertson* was to render the contract void whereas the statute in *Jamieson* rendered the contract illegal. The court cited with approval a rather strained distinction drawn by Gloag between contracts which the law will not allow to operate versus contracts which are contrary to law.[131] *Cuthbertson* fell under the first category whereas *Jamieson* fell under the second.

3 4 3 Steps towards a synthesis

If these two cases appear to be contradictory, it is perhaps because they simply are. However, there have been attempts at reconciliation over the years.[132] A common theme is the idea that the degree of illegality differed in the two cases. In *Cuthbertson* it was stressed that there was little to no turpitude in the transaction whereas in *Jamieson* the contract was considered a serious contravention of the law.[133] This may suggest that Scots law, like many other systems, regards the seriousness of the illegality as an important consideration.

A final important case to consider *Dowling & Rutter v Abacus Frozen Foods Ltd* ("*Dowling*").[134] Although the court did not discuss *Cuthbertson* and *Jamieson* in much detail, it is one of the more recent cases in Scotland dealing with illegality. The matter concerned a contract in terms of which the pursuers supplied workers to be employed at the defenders' fish processing factory. It transpired, unbeknownst to the pursuers, that these workers were foreigners who did not have the necessary work permits required by immigration law. The defenders refused to pay for the labour on the basis that the pursuers performed their side of the contract unlawfully by supplying the unauthorised labourers.

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[131] 1950 SC 265 272; Gloag *The Law of Contract* 550.
[132] See O Ezike & J Macleod "Restitution Under an Illegal Contract: A Scots Law Perspective on *Patel v. Mirza*" (2018) 2 *ERPL* 273 279-280; Macgregor (2000) *Edin LR* 27.
[133] This is perhaps because *Jamieson* was decided in the context of post-war Britain when resources were quite scarce; Macgregor (2000) *Edin LR* 27.
[134] 2002 SLT 491.

Lord Johnston, relying heavily on *St John Shipping,* upheld the claim of the pursuers. He said:

> "[T]he issue is essentially one of equitable remedy in the sense that a person who is seeking to rely knowingly on his own illegal act cannot gain by it but equally should not lose by it if the illegal act is committed by somebody else completely outwith his own knowledge, actual or constructive"[135]

Since the pursuers were unaware of the workers' immigration status, it was held that it would have been inequitable to deny them the right to sue upon an otherwise perfectly legal bargain.

One interpretation of *Dowling* is that Scottish courts may hold an equitable discretion whether to apply the *ex turpi* rule in a particular case, at least if the parties were not *in pari delicto*.[136] Whether this is correct ultimately turns on how a particular system defines the *ex turpi* maxim. For example, we have seen in South African cases that a court may, in appropriate circumstances, enforce a contract which has infringed on legislation.[137] However, the South African courts do so despite claiming that the *ex turpi* rule operates inflexibly. Accordingly, at least on the South African understanding of the *ex turpi* maxim, this interpretation of *Dowling* would not be accurate. It is not clear whether Scotland indeed defines the *ex turpi* maxim differently. The only point that clearly emerges here is that the use of this maxim is quite unhelpful when describing the impact of illegality on a contract.[138]

A better explanation of *Dowling* may be that considerations of policy did not require the contract to be unenforceable. The crucial factor was the fact that the pursuers were unaware of the illegality. A further feature that distinguishes *Dowling* from *Jamieson* is, as Lord Wheatley recognised in his opinion, that the content of the contract itself was not prohibited, it was only performed in an illegal manner.[139] In that sense *Dowling* is more apposite to the reasoning and result in *St John Shipping*.[140]

A final question to consider is the impact of *Patel* on Scots law. Although the court in *Patel* did not consider any Scottish authorities, the case is likely to be very influential in any future Scottish case involving illegality.[141] This is because in the past the

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[135] 2002 SLT 491 para 20.
[136] See MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems* 163.
[137] 2 5 above.
[138] J du Plessis "Some Thoughts on the Consequences of Illegal Contracts" (2021) *Acta Juridica* 177 190-191.
[139] 2002 SLT 491 494.
[140] But see 3 3 2 above on the notion of performance illegality.
[141] Ezike & Macleod (2018) *ERPL* 281. To date, the only Scottish case that has referred to *Patel* is *D Geddes (Contractors) Ltd v Neil Johnson Health & Safety Services Ltd* [2017] CSOH 42 para 16.

Scottish courts have often taken English case law into account when deciding disputes pertaining to illegal contracts.[142] MacQueen has also argued that the approach in *Patel* is consistent with the way in which Scots law, in his view, approaches illegal contracts.[143] In other words, the outcomes of *Cuthbertson*, *Jamieson* and *Dowling* would not have differed if the method in *Patel* had been applied.

3 4 4 Conclusion

Although there is evidence that earlier Scottish sources described illegal contracts as void, the term that is now preferred is 'unenforceable.' In the context of South African law, it has been argued that an important difference exists between the terms 'void' and 'unenforceable' because it is only when a contract is void that an enrichment claim can arise.[144] This distinction does not appear to hold the same value in Scotland, because illegal contracts are said to have their own unique rules which govern the question of restitution.[145] It follows from the somewhat unhappy distinction in *Jamieson* between contracts that are void and contracts that are illegal.[146] Where contracts categorised as illegal are described as being unenforceable, it relates only to the question of whether a contractual action such as a claim for specific implement may succeed. It says nothing about the availability of a claim in unjustified enrichment.[147]

For the time being it remains a difficult task to describe the consequences of illegal contracts in Scotland with accuracy. As in other systems, references to the *ex turpi* and *par delictum* maxims have not been particularly helpful. *Cuthbertson* and *Jamieson* are difficult to reconcile, and *Dowling* potentially confused matters more by framing the whole question as "a matter of equitable remedy." Indeed, there is not one question but two, which the court in *Dowling* conflated into one.[148] It must first be

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[142] For example, *Jamieson v Watt's Trustees* 1950 SC 265 271.
[143] MacQueen *Contract Law* 344-345.
[144] 2 6 above.
[145] Macgregor "*Pacta Illicita*" in *A History of Private Law in Scotland* 151. In *Patel* the court seemed to regard void and unenforceable as interchangeable terms; see Häcker "Illegality and Immorality" in *Illegality after* Patel v Mirza 336.
[146] McBryde *Contract in Scotland* 359-360.
[147] The bigger problem caused by the distinction between illegal and void contracts in *Jamieson* concerns the question whether title to goods may transfer under an illegal contract or not. It is a matter of debate whether Scotland follows an abstract or causal system for transfer of title. In an abstract system the validity of the underlying contract has no bearing on the validity of the transfer of title, whereas in a causal system the transfer of title is dependent on the validity of the underlying contract. In so far as Scotland may follow a causal system, the status of the contract becomes critically important. See Macgregor (2000) *Edin LR* 29-33; MacQueen *Contract Law* 346.
[148] Thomson (2002) *SLT* 154.

determined whether the contract is unenforceable due to the illegality. It is only if the contract is found to be unenforceable that the second question arises, namely whether a claim in unjustified enrichment ought to be awarded to the pursuer. There has not recently been a case on illegal contracts in Scotland, but when the next one arises, it is likely that the court will closely consider the approach in *Patel*.[149] For now, one can only speculate whether such a case will illuminate matters.

3 5 The law of New Zealand

Thus far the focus has been on countries whose approach to illegality was strongly influenced by the *ex turpi* and *par delictum* maxims received from Roman law. Some jurisdictions have opted for a more radical reform by passing legislation that gives courts a broad discretion to determine the consequences of illegality. Although the possibility for statutory reform in this area of the law is probably remote in South Africa and many other countries, the experience of a comprehensive statutory regime may nevertheless provide valuable insights. Arguably the most prominent example of such a reform is New Zealand's Illegal Contracts Act 129 of 1970 ("ICA").[150] The ICA was recently consolidated into the Contract and Commercial Law Act 5 of 2017 ("CCLA").[151] Although the CCLA made some minor structural changes, the substance of the ICA has remained the same.[152]

The first problem confronting any statutory reform is the definition of an illegal contract. Rather than reinvent the wheel, section 71 of the CCLA preserved the common-law approach.[153] It defines an illegal contract as "a contract that is illegal at law or in equity, whether the illegality arises from the creation or performance of the contract." The scope of the word "performance" is constrained by section 72, which states that a contract lawfully entered into does not become illegal where its

[149] However, the approach in *Patel* has not found traction in all jurisdictions where English law is influential. For example, the Singapore Court of Appeal has expressly declined to follow *Patel,* see *Ochroid Trading Ltd v Chua Siok Lui* [2018] SGCA 5 para 113.

[150] The other notable example is Israel. Section 31 of the Israeli Contract Law (General Part) 1973 provides for restitution of benefits conferred under an illegal contract by default, subject to a judicial discretion to refuse restitution. In addition, the provision empowers a court to compel performance by a party to an illegal contract, in whole or part, where the counterparty has already performed. See D Friedmann "Consequences of Illegality under the Israeli Contract Law (General Part) 1973" (1984) 33 *ICLQ* 81.

[151] See *Xiao v Sun* [2018] NZHC 536 n 25.

[152] New Zealand's statute has for example influenced proposals for reform in the states of British Columbia, Ontario, and South Australia. See Buckley *Illegality and Public Policy* 289-294 for an overview.

[153] Compare s 2 ICA.

performance is in breach of a statutory provision, unless that provision expressly provides so or its purpose clearly requires it.

The definition in section 71 provision has been criticised on the basis that the common law is itself not entirely clear on when a contract is illegal.[154] While it may be true that determining illegality under the common law is difficult, it is perhaps even more difficult to draft a statutory provision that would not be either over- or under-inclusive. To leave that determination to the courts appears to have been a sensible move.[155]

The innovation of this statutory regime is its approach to the consequences that follow once a contract is brought within its ambit. As a point of departure, section 73(1) of the CCLA declares every illegal contract to be of no effect.[156] However, section 76(1) provides that:

> "(1) The court may grant to a person referred to in section 75 any relief that the court thinks just, including (without limitation)—
> (a) restitution; or
> (b) compensation; or
> (c) variation of the contract; or
> (d) validation of the contract in whole or in part or for any particular purpose."

The court therefore has wide powers to order what it considers would be a just result in a particular case. A striking feature of section 76(1) is that it empowers the court to validate a contract that has been deemed undesirable by the common law or prohibited by the legislature.[157] In other words, the court may override the prior reasons for why the law disallowed the contract in question to be enforced.

That does not mean that the judicial discretion is unrestrained. In exercising its discretion to grant relief under section 76, section 78 requires the court to consider the conduct of the parties, the purpose of the statute and gravity of the penalty prescribed for the breach if applicable, as well as any other matter the court deems relevant. In addition, section 79 provides that the court must not grant relief if doing so would be contrary to the public interest.

While it is not possible to conduct a comprehensive survey of the cases which have

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[154] MP Furmston "The Illegal Contracts Act 1970 - An English view" (1972) 5 *NZULR* 151 155.

[155] The Law Commission of New Zealand considered the provision defining an illegal contract to be satisfactory in its review of the ICA in 1993. See Law Commission of New Zealand *Contract Statutes Review* (1993) no 25 174.

[156] Compare s 6(1) ICA.

[157] Buckley *Illegality and Public Policy* 283. However, the court has made it clear that that the purpose of the ICA is not to subvert the social or economic policies of other statutes; *Harding v Coburn* [1976] 2 NZLR 577 584-585. For criticism of how the courts have used their power to validate illegal contracts, see B Coote "Validation under the Illegal Contracts Act" (1992) 15 *NZULR* 80.

been decided under this statutory regime, we may get a good sense of how the legislation operates from *Duncan v McDonald*.[158]

Duncan worked as a solicitor and in that capacity served as the trustee of an estate. A group of New Zealanders, who were participants in a Nigerian fraud scheme, approached Duncan to persuade him to advance a loan from the funds of the estate. The group had been tricked into believing that by paying about NZ $285 000 as bribes to Nigerian government officials, they would receive kickbacks amounting to US $2 million. Duncan knew that the money was intended for an illegal purpose and was promised a fee for arranging the financing. In order to secure the loan, he persuaded the McDonalds to mortgage their property in favour of the estate, by representing to them that they would also benefit from the proceeds of the scheme. The McDonalds duly did so. Unsurprisingly, the NZ $285 000 was lost. The consequent litigation generated a vast procedural labyrinth not worth navigating here. Reduced to its essence, the ultimate issue before the court was whether the estate could recover the lost NZ $285 000 from the McDonalds' property and/or Duncan in his personal capacity, since he had breached his duties as a trustee. The McDonalds for their part resisted the claim by arguing that the mortgage was invalid due to the illegality.

The court found that both the loan agreement and the mortgage securing it were indeed illegal, since their aim was to defraud a foreign government allied to New Zealand. Accordingly, the contracts were *prima facie* of no effect. However, the court exercised its discretion in terms of the ICA and allowed the estate to recover the money. It did so by validating the mortgage to the extent of NZ $75 000. The rest of the NZ $285 000 was to be paid to the estate by Duncan. The court considered this to be a just solution, since it found that Duncan's conduct was more blameworthy than that of the McDonalds'. Although it was held that the McDonalds should have reasonably been aware that they were participating in an illegal scheme, they were ultimately induced into joining it by Duncan's false assurances. For this reason, they were less blameworthy and therefore liable for a lesser share of the lost money.

This case illustrates the flexibility afforded to courts in New Zealand when dealing with an illegal contract. They can distribute liability according to the degree of each party's illegal conduct and so reach a just result. A side-effect of this flexibility is that the courts have on occasion reached opposing outcomes in cases concerned with the

[158] [1997] 3 NZLR 669.

same statutory provision. For example, in some cases dealing with prohibited financial assistance granted by companies, relief akin to enforcement of the contract was granted in some cases[159] but refused in others.[160] However, these results were reached with reference to the relevant policies considerations at stake.[161]

The enactment of the ICA was met with the predictable objection that it would generate an intolerable amount of uncertainty.[162] However, this concern appears to have been unfounded. The ICA seems to have been quite successful instead.[163] The statutory regime has now been in force for about half a century, with only minor amendments. If anything, the experience of New Zealand illustrates that a discretionary approach to illegality can work rather well.

3 6 Supranational model instruments

Over the past few decades various working groups, mostly based in Europe, have endeavoured to develop model rules for contract law.[164] One of the motivations for these projects was to lay the foundation for a European civil code in the future. In the area of illegal contracts, the most notable instruments are the Principles of European Contract Law[165] ("PECL"), the UNIDROIT Principles of International Commercial Contracts[166] ("PICC") and the Draft Common Frame of Reference[167] ("DCFR"). Political enthusiasm for the development of a European civil code has faded and none of these instruments are legally binding today.[168] Nevertheless, these model rules are the result of considerable comparative research, which makes them worthy of brief

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159 *Catley v Herbert* [1988] 1 NZLR 606; *Colemand v Myers* [1977] 2 NZLR 225.

160 *NZI Bank Ltd v Euro-National Corp Ltd* [1992] 3 NZLR 528; *Hoverd Industries Ltd v Supercool Refrigeration & Air Conditioning Ltd* [1994] 3 NZLR 300; Buckley *Illegality and Public Policy* 287.

161 The conclusive factor leading to the different outcomes in the financial assistance cases was whether a particular arrangement undermined the purpose of the infringed legislation, namely, to protect shareholders and creditors; Law Commission of New Zealand *Contract Statutes Review* 17-19; Buckley *Illegality and Public Policy* 287-288.

162 See generally the analysis of Furmston (1972) *NZULR* 151.

163 A Beck "Illegality and the Court's Discretion: The New Zealand Illegal Contracts Act in action" (1989) 13 *NZULR* 389 418-419; Buckley *Illegality and Public Policy* 284.

164 For an account of the various projects, see R Zimmermann "The Textual Layers of European Contract Law" in A Fagan & H Scott (eds) *Private Law in a Changing World - Essays for Danie Visser* (2019) 165.

165 O Lando, E Clive, A Prüm & R Zimmermann (eds) *Principles of European Contract Law* Part III (2003).

166 UNIDROIT (ed) *Principles of International Commercial Contracts* (2010). For analysis see M J Bonell "The New Provisions on Illegality in the UNIDROIT Principles 2010" (2011) 16 *Rev dr unif* 517.

167 C von Bar & E Clive (eds) *Principles, Definitions and Model Rules of European Private Law: Draft Common Frame of Reference (DCFR)* Full Edition vol 1-4 (2009). On the provisions dealing with illegality, see Häcker "Illegality and Immorality" in *Illegality after* Patel v Mirza 365- 370.

168 Parties may elect for their contract be governed by one of these instruments.

consideration here. This section focuses on the approach in the PECL, partially for the sake of brevity and partially because the PECL is the most appropriate reference text of what can be considered traditional European contract law.[169] There is also considerable overlap between this instrument and the DCFR and PICC.

The PECL distinguishes between contracts infringing legal principles regarded as fundamental by the laws of members of the European Union[170] and contracts infringing mandatory rules.[171] These fundamental principles refer to extra-legal standards regarded as important by member states. In other words, they encapsulate in neutral terms what is described in national systems by terms such as *boni mores,* public policy or immorality.[172] Mandatory rules on the other hand, are more akin to what is known in national systems as statutory illegality. This would for example include infringements on legislation in common-law systems and legal codes in civilian systems. In the PECL itself, the mandatory rules may refer to rules in a national system, a supranational body of law, such as EU competition law, or the contents of international conventions.[173]

Article 15:101 declares contracts contrary to fundamental principles to be of no effect, meaning quite plainly that they cannot be enforced. This provision gives the judge or arbitrator no discretion to enforce the contract.

The provision dealing with mandatory rules is more flexible.[174] Article 15:102 provides that the effect on the contract is that which is expressly prescribed by the relevant mandatory rule. Where there is no prescription, the judge or arbitrator has a discretion to declare the contract to have full effect, some effect or no effect at all.[175] Article 15:102(3) requires that this discretion must be a proportional response to the infringement and the following factors must be taken into account: the purpose of the infringed rule, the category of persons for whose protection the rule exists, any sanction that may be imposed under the infringed rule, the seriousness of the infringement, whether the infringement was intentional and the closeness of the relationship between the infringement and the contract.

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[169] Zimmermann "The textual layers of European Contract Law" in *Private Law in a Changing World* 177-178.
[170] Art 15:101.
[171] Art 15:102.
[172] MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems* 168.
[173] Meier "Illegality" in *Commentaries* 1902.
[174] This provision includes contracts with illegal content, contracts performed in an illegal manner or contracts concluded for an illegal purpose; Meier "Illegality" in *Commentaries* 1906-1907.
[175] A separate provision, Art 15:103, deals with the extent to which a contract that is only partially illegal may be upheld by severing the illegal part; Meier "Illegality" in *Commentaries* 1914-1920.

Where a contract is rendered ineffective due to illegality, Article 15:104 provides for the possibility of restitution.[176] In deciding whether to award restitution, a judge or adjudicator must again consider the factors in Article 15:102(3). However, since enforceability and restitution are different issues, an analysis in terms of the same factors may lead to different results.[177]

Two more features of Article 15:104 are worth noting. The first is that restitution may be refused in terms of Article 15:104(3) where a party knew or ought to have known about the illegality. Second, if restitution cannot be made, Article 15:104(4) allows for a reasonable sum to be awarded instead. This would presumably cover situations where the performance took the form of a service.

The approaches adopted in the PECL and the other model instruments are very similar to New Zealand's statutory regime and *Patel.* All of them recognise the need for a flexible approach to illegality and the need to explicitly consider policy considerations.

3 7 Conclusion

The purpose of this chapter was to investigate how foreign jurisdictions approach illegal contracts. To this end, four legal regimes and some supranational model rules were considered. It is difficult to draw general conclusions from this overview about how rules on illegal contracts operate. In many respects the rules in the various jurisdictions are similar, but often with significant qualifications and peculiarities. Nevertheless, some clear trends and features do emerge.

The first is that describing the consequences of illegality with clarity remains difficult. The *ex turpi* and *par delictum* maxims and their functional equivalents have long obscured matters in jurisdictions where rules on illegality have been influenced by Roman law. It led to the development of the much-maligned reliance rule in England which was only discarded relatively recently. In Germany, § 817(2) BGB is regarded as unsatisfactory and in Scotland the case law on illegality is difficult to reconcile.

In addition, terms such as void, illegal and unenforceable tend to cause confusion unless they are used with care. In South African law, a contract described as void is

[176] An alternative remedy that may be available in terms of Art 15:105 is damages, but only to the value of a claimant's reliance interest. See MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems* 168-169.

[177] Meier "Illegality" in *Commentaries* 1926.

associated with the idea that an enrichment claim is available in principle, as long as the other requirements for enrichment liability are met. The same is true in German law. However, when a contract is described as 'unenforceable' in South African law, it follows that an enrichment claim can never arise, because the *sine causa* requirement has not been met. In English law on the other hand, the terms 'void' and 'unenforceable' have not been clearly distinguished and are sometimes even used interchangeably by the courts. In other words, an English court may well describe a contract as unenforceable but then proceed to award restitution. The same is true in Scotland. The point is that these terms have varying meanings in different jurisdictions and these meanings may even change over time. In this regard the approach of New Zealand and the PECL to describe an illegal contract as being without legal effect as a point of departure is more sensible. Doing so avoids the assumptions about the availability of restitution associated with the concepts of voidness and unenforceability.

Secondly, the policy considerations regarded as important when dealing with illegal contracts are very similar in all the legal systems considered. Although they may have been made more explicit in some countries like England and New Zealand than say in Germany or even South Africa, clear agreement exists about their core content. Factors like the purpose of the rule which has been infringed, the state of mind of the parties and the seriousness of the illegality, to name a few, will almost invariably play a crucial role. On a more fundamental level, whether stated or implicitly assumed, the notion of proportionality is also important.

The most conspicuous difference between the various systems is therefore not which policies are important. Rather, it is about how they should best be given effect. At the one end of the spectrum is a far-reaching discretion for a judge to arrive at a just result, although that discretion is always tempered by a list of relevant factors which must be considered. This approach is best exemplified by New Zealand, the PECL and to a lesser extent England after *Patel*. At the other end of the spectrum is a rule-based approach with relatively well-defined exceptions. Examples of this approach is Germany and England before *Patel*.

The essence of the difficulty posed by illegal contracts is that the relevant policy considerations at stake are often in conflict and must therefore be weighed against each other. This means that reasonable people may disagree on the outcome of a particular case. However, because such a weighing of policies is inevitably required, a rule-based approach, which attempts to state the consequences of illegality *a priori*,

will often have difficulty in reaching satisfactory results consistently while also remaining true to the rules themselves. This is evident, for example, in how German courts have been forced to contort § 817(2) BGB.

Critics of a discretionary approach often point out that rules generate more certainty, so long as the rules and their exceptions are clearly stated. A discretionary approach, on the other hand, is inherently uncertain. The experiences of New Zealand and England dispel this objection. The discretionary approach in New Zealand has not generated an intolerable amount of uncertainty whereas the rule-based approach in England has been rejected in favour of a discretionary one, among other reasons that there was much uncertainty surrounding the reliance rule too.

We have now seen how various systems approach illegality in broad terms. While most agree about the policies that are important, their application in particular factual scenarios may well differ. The next chapter therefore investigates illegality on a more granular level by analysing how various jurisdictions respond to particular problem areas.

CHAPTER 4: SPECIFIC PROBLEMS OF ILLEGALITY: ILLEGAL CONSUMER LOANS, EMPLOYMENT AND CONSTRUCTION CONTRACTS

4 1 Introduction

Thus far two themes have been covered in this thesis. The first was concerned with what determines the consequences of illegality in the South African law of contract. In this regard it was demonstrated that much uncertainty underlies this area of the law. One peculiarity is that there is no clear justification for why some illegal contracts are classified as void while others are merely unenforceable. The second theme, addressed in Chapter 3, investigated how selected foreign jurisdictions determine what the consequences of an illegal contract should be. Here it was shown that foreign systems have struggled with this problem and that more flexible or discretionary approaches seem to be growing in popularity.

This chapter develops these two themes by considering three particularly difficult fact-patterns from a comparative perspective. The aim is to investigate what policy factors determine the consequences of the illegality in each fact-pattern and to compare how different jurisdictions navigate the tension between them.

The first scenario relates to the consequences of a consumer loan that infringed credit legislation. May the lender recover any money from the borrower? The second scenario deals with the position of an employment contract that has been tainted with illegality. What remedies, if any, are available to an employee in such as case? Finally, the scenario of a contractor who performed work contrary to the applicable laws or regulations is considered. Does illegality in this scenario exclude the contractual claim of an employee or contractor? And may they alternatively recover the value they transferred with an enrichment claim?

4 2 Loans contrary to credit law

4 2 1 South Africa

In an effort to broaden access to credit and improve consumer protection, the legislature completely overhauled the consumer credit regime in South Africa in 2005 by enacting the National Credit Act 34 of 2005 ("NCA").[1] Unfortunately, the attempt to address an issue of great importance to society has proven controversial. The NCA

[1] For a historical overview of credit regulation in South Africa see J Otto "The History of Consumer Credit Legislation in South Africa" (2010) 16 *Fundamina* 257.

has been plagued by constitutionality challenges and adverse commentary.[2] Some important provisions have also been amended over time. Nevertheless, the development of the NCA is instructive. This is particularly so because one of the most controversial provisions of the NCA is concerned with the consequences of an unlawful credit agreement.[3]

For a credit agreement to be unlawful, it must fall within the catalogue of circumstances provided for in section 89(2). For example, section 89(2)(d) renders a credit agreement unlawful if the lender was required to register as a credit provider under the NCA at the time when the loan was extended and failed to do so. The question of when a credit provider must register has been subject to a great deal of uncertainty. Indeed, some of the most important litigation on the NCA was triggered by transactions where the lenders failed to register, often without realising that it was necessary.

The issue has now been clarified, but the certainty comes at a price. In terms of section 40, a person must register as a credit provider if the total principal debt owed to that person under all outstanding credit agreements exceeds the prescribed threshold. The threshold used to be R500 000 but was reduced to zero in 2016,[4] meaning that registration is now always required for all transactions governed by the NCA.[5] In other words, registration is a requirement not only for regular participants in the credit market, but also for anyone who extends a loan, even if it is only once off. This much was confirmed in *Du Bruyn v Karsten* although Nicholls AJA expressed some dissatisfaction at the state of affairs.[6]

If a credit provider failed to register or the agreement is unlawful for some other reason specified by the NCA, the consequences that follow are set out in section 89(5). In its original form, the provision read:

> "If a credit agreement is unlawful in terms of this section, despite any provision of common law, any other legislation or any provision of an agreement to the contrary, a court must order that –
>
> (a) the credit agreement is void as from the date the agreement was entered into;

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2 For an appraisal, see JM Otto "National Credit Act. Vanwaar Gehási? Quo Vadit Lex? And Some Reflections on the National Credit Amendment Act 2014 (Part 1)" (2015) 3 *TSAR* 583; JM Otto "National Credit Act. Vanwaar Gehási? Quo Vadit Lex? And Some Reflections on the National Credit Amendment Act 2014 (Part 2) (2015) 3 *TSAR* 765. See also *Du Bruyn v Karsten* 2019 1 SA 403 (SCA) para 1.

3 S 89(5).

4 *Government Gazette* 39981 of 11 May 2016.

5 Not all credit agreements are governed by the NCA. Various exceptions are provided for in s 4.

6 2019 1 SA 403 (SCA) para 27-28 overturning *Friend v Sendal* 2015 1 SA 395 (GP).

> (b) the credit provider must refund to the consumer any money paid by the consumer under that agreement to the credit provider, with interest calculated
> (i) at the rate set out in that agreement; and
> (ii) for the period from the date on which the consumer paid the money to the credit provider, until the date the money is refunded to the consumer; and
> (c) all the purported rights of the credit provider under that credit agreement to recover any money paid or goods delivered to, or on behalf of, the consumer in terms of that agreement are either –
> (i) cancelled, unless the court concludes that doing so in the circumstances would unjustly enrich the consumer; or
> (ii) forfeit to the State, if the court concludes that cancelling those rights in the circumstances would unjustly enrich the consumer."

Under the common law, an illegal loan is generally void (as opposed to unenforceable).[7] If so, the credit provider would be able to recover the money transferred to the borrower with the *condictio ob turpem vel iniustam causam*, provided that the court exercises its discretion in terms of *Jajbhay v Cassim* ("*Jajbhay*") to relax the *par delictum* rule.[8] The wording "despite any provision of common law" read with section 89(5)(c) specifically appears to exclude this possibility. This part of the NCA has been heavily criticised and was even described as "Orwellian".[9]

A good example of just how harshly it operated is *Cherangani Trade and Invest 107 (Pty) Ltd v Mason* ("*Cherangani*").[10] The respondents had borrowed more than R 2 million from the applicant on onerous terms through a variety of agreements. Their intention was to use the loan to satisfy a judgment debt against them. When the respondents defaulted, the applicant approached the court to enforce the loan. Among other defects in the application, it transpired that the applicant was not registered as a credit provider despite being required to do so due to the value of the loan. The High Court considered section 89(5) to be peremptory and declared that the loan was void in terms of the NCA. It also declared any rights which the applicant may have had against the respondent in terms of the other agreements related to the loan forfeited to the State in terms of section 89(5)(c). Indeed, it is difficult to see how the court could make an order other than forfeiture to the State. In theory, the court could in terms of section 89(5)(c) allow the borrower to keep the money if it is 'justly' enriched, but when would this be the case?[11] In terms of section 89(5)(b), the credit provider must always

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7 *National Credit Regulator v Opperman* 2013 2 SA 1 (CC) para 43.
8 1939 AD 537.
9 JM Otto "Die *Par Delictum*-Reël en die National Credit Act" (2009) 3 *TSAR* 417 432.
10 2011 11 BCLR 1123 (CC). See also JM Otto "National Credit Act, Ongeoorloofde Ooreenkomste en Meevallertjies vir die *Fiscus*" (2010) 1 *TSAR* 161.
11 Although the NCA uses the term 'unjust' enrichment, the preferred term in South African law is 'unjustified' enrichment; *National Credit Regulator v Opperman* 2013 2 SA 1 (CC) para 23-24.

refund whatever the consumer paid, meaning that the consumer will always obtain some additional gain by retaining whatever the credit provider refunded. So the only remaining option is that a court must declare any 'purported rights' of the credit provider under the agreement forfeited to the State.

The applicant approached the Constitutional Court in an attempt to have section 89(5)(c) declared unconstitutional but leave to appeal was refused on procedural grounds. Although Yacoob J expressed some doubt about the correctness of High Court's order, he ultimately found that the circumstances were not right for the Constitutional Court to rule on the constitutionality of section 89(5)(c).[12]

A better opportunity itself in *National Credit Regulator v Opperman* ("*Opperman*)".[13] Once again the matter was triggered by the non-registration of a credit provider. The first respondent, Opperman, lent R 7 million to the second respondent, Boonzaaier for the purpose of property development. It was common cause that Opperman, a Namibian farmer, was not in the business of providing credit. He was not aware of the requirement to register and had no intention of violating the provisions of the NCA when he provided the loan. Boonzaaier defaulted on the loan and Opperman applied to have the debtor's estate sequestrated. The High Court raised concerns about the constitutionality of section 89(5)(c) and postponed the sequestration proceedings until the issue could be resolved. Subsequently the High Court found the provision to be unconstitutional, which resulted in the matter being referred to the Constitutional Court for a confirmation of invalidity.[14] The National Credit Regulator joined proceedings and argued that the order of invalidity should not be confirmed.

The issue to be determined was whether section 89(5)(c), on a proper interpretation, arbitrarily deprives the credit provider of property. If so, it would amount to a limitation of the right to property contained in section 25(1) of the Constitution. That in turn raises the question whether such a limitation is justified in terms of section 36 of the Constitution.

The majority of the Constitutional Court accepted the High Court's interpretation of section 89(5)(c) as the most plausible. That is, the contract is void and the court is obliged to order that all rights that may follow from the agreement are either cancelled

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12 2011 11 BCLR 1123 (CC) para 21-25.
13 2013 2 SA 1 (CC). See also R Brits "Arbitrary Deprivation of an Unregistered Credit Provider's Right to Claim Restitution of Performance Rendered" (2013) 16 *PELJ* 422.
14 *Opperman v Boonzaaier* 2012 ZAWCHC 27.

or forfeited to the state. The court also accepted that any purported right will in practice always be forfeited to the State for the same reason outlined above, namely that it is difficult to imagine how allowing the borrower to keep the loan would not result in unjustified enrichment.[15]

As for the constitutionality of the provision, Van der Westhuizen J found that it amounts to an unreasonable limitation of the right not to be arbitrarily deprived of property. The arbitrariness lies in the fact that the court has no discretion not to deprive the credit provider of its claim. Although the aim of protecting consumers from unregistered credit providers is laudable, the means employed to do so were disproportionate to the aim. This is because credit providers who unintentionally failed to register are treated just as harshly as those who wilfully ignored the requirements of the NCA.[16] In addition, Van der Westhuizen J suggested that the same degree of protection could be achieved in a less restrictive manner by requiring the credit provider to forgo any interest they stood to earn but allowing them to recover the capital.[17]

Opperman dealt only with section 89(5)(c), which concerned a credit provider's enrichment claim. An arguably even harsher provision was section 89(5)(b), which required a credit provider to refund any monies, with interest, that the consumer had already paid in terms of the loan agreement. Unsurprisingly, the Constitutional Court also declared this provision unconstitutional a few years later.[18] As in *Opperman*, the reason was that section 89(5)(b) amounted to an arbitrary deprivation of property that could not be justified in terms of section 36 of the Constitution. Around the same time, Parliament amended the NCA.[19] The amendment deleted section 89(5)(b) and (c), as well as the reference to the common law in the first sentence of section 89(5). The provision now reads as follows:

> (5) If a credit agreement is unlawful in terms of this section, despite any other legislation or any provision of an agreement to the contrary, a court must make a just and equitable order including but not limited to an order that —
> (a) the credit agreement is void as from the date the agreement was entered into."

In other words, the common law position appears to have been essentially restored. An unregistered credit provider cannot recover anything in terms of the credit

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15 2013 2 SA 1 (CC) para 55.
16 2013 2 SA 1 (CC) para 76.
17 2013 2 SA 1 (CC) para 78.
18 *Chevron SA (Pty) Limited v Wilson t/a Wilson's Transport* 2015 10 BCLR 1158 (CC).
19 National Credit Amendment Act 19 of 2014.

agreement itself, but is not entirely out of pocket, since the court may award such a party an enrichment claim if it is just and equitable to do so in the circumstances.[20] This development is to be welcomed, since it allows the court to balance various conflicting policy considerations in a manner that is sensitive to the context of each case.

4 2 2 England

4 2 2 1 The swaps litigation

Although this section is concerned with consumer credit agreements, brief reference should be made to the so-called swaps litigation in England because these transactions also raised the problem of indirect enforcement. In the latter part of the twentieth century, various local authorities concluded interest rate swap agreements with financial institutions.[21] It turned out that these transactions, which resembled loans, were beyond their statutory powers and that the contracts were thus void.[22] Various creditors to these transactions then sought to recover what they were owed by instituting claims for restitution based on unjust enrichment. The litigation culminated in the test case of *Westdeutsche Landesbank Girozentrale v Islington LBC,* where the House of Lords overturned existing authority and held that a claim for restitution was available in these circumstances.[23] The court argued that the transaction was not in fact a loan, but a futures contract which did not involve the lending of money. Accordingly, awarding the enrichment claim would not indirectly enforce the contract, it would only restore the parties to the position they had occupied before entering into the agreement.[24]

Although these cases display some similarities to the problem considered in this section, they are not strictly speaking cases about illegal loans. This is because the

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[20] *Fourie v Geyer* 2020 6 SA 569 (NWM) para 32-33.

[21] An interest rate swap agreement is in essence a bet between two parties about how an interest rate will change in the future with reference to a notional capital sum. Depending on the movement of the interest rate over a predetermined period of time, the one party will be indebted to the other by a certain amount. The utility of the transaction is that it allows an entity with a fixed interest rate over its debt to effectively swap it for a floating interest rate and vice versa. The transaction has various applications such as hedging against foreign exchange fluctuations or simplifying the financial planning of large institutions. For a summary and analysis of the swaps litigation, see G Virgo *The Principles of the Law of Restitution* 3 ed (2015) 372-377.

[22] *Hazell v Hammersmith and Fulham LBC* [1992] 2 AC 1.

[23] [1996] AC 669.

[24] It now seems that even if the contract had been a loan, an enrichment claim would have been available; *Haugesund Kommune v Depfa ACS Bank* [2012] QB 549.

swaps litigation dealt with the consequences of contracts that failed due to a lack of capacity and not due to illegality.[25]

4 2 2 2 Illegal consumer credit

More instructive for comparative purposes is the experiences of English courts when confronted with consumer loans that do not comply with credit legislation. A good starting point is *Orakpo v Manson Investments Ltd* ("*Orakpo*").[26] The respondent had borrowed money from the appellants to acquire several properties. The loans were advanced, and mortgages were registered over the properties in favour of the appellants. However, due to inadvertence, the written version of the contract left out a crucial term that was required to be in writing by the Moneylenders Act 1927. Although the respondent was aware of this term and had expressly agreed to it, the fact that it was not in writing meant that the loan agreements as well as the mortgages were unenforceable. When the respondent fell into arrears it applied to the court for an order that the agreements and securities over the property were unenforceable. The appellants attempted to recover their money in a counterclaim by relying on a complicated doctrine of equity that need not be untangled here. The important point is that the House of Lords dismissed the appeal, but expressed dissatisfaction at the result, since it left the respondent with a large windfall. At the heart of the court's reasoning is the proposition that it would be improper to apply an equitable doctrine to allow moneylenders to escape from the consequences occasioned by their non-compliance with the relevant statute. The fact that the non-compliance was not intentional made no difference.

Some years later, the House of Lords expressed the same attitude towards indirect enforcement in *Dimond v Lovell* ("*Dimond*").[27] Mr Lovell negligently crashed his car into the car of Mrs Dimond. She approached 1st Automotive to hire a replacement car to use while her car was being repaired. The attraction of 1st Automotive's offering is that they allow a customer to defer payment for the hire of the replacement vehicle until after the damages claim against the negligent driver, or rather the other driver's insurer, has been concluded. The agreement also entitles 1st Automotive to conduct

[25] It is admittedly not always easy to draw a hard border between capacity and legality as criteria for a valid contract. After all, a contract that fails due to a lack of capacity infringes the legal rules governing the matter of who may enter into contracts. However, in keeping with convention, this thesis treats such contracts as falling outside the ambit of illegal contracts; see 2 3 above.

[26] [1977] 3 All ER 1.

[27] [2002] 1 A.C. 384.

any litigation necessary to recover the damages on the customer's behalf. In other words, once the insurer had compensated Mrs Dimond, her bill to 1st Automotive for hiring the replacement vehicle would become due.

Although the Mr Lovell's insurer settled the bill for the repair costs, it refused to pay for the hiring of the replacement vehicle. The insurer argued that 1st Automotive was in fact in the business of providing credit and that its contract with Ms Lovell was an improperly executed agreement within the meaning of the Consumer Credit Act 1974 ("the CCA") since it did not contain certain prescribed terms.

In this kind of case, section 65(1) of the CCA provides that an improperly executed agreement shall only be enforceable by an order of the court. Such an application must be brought in terms of section 127(1), which directs the court to dismiss an application for an enforcement order but only if it considers it just to do so.[28] In addition, the provision requires the court to take into account "prejudice caused to any person by the contravention in question, and the degree of culpability for it" as well as the powers conferred on the court by section 127(2)[29] and sections 135-136.[30]

In short, if an agreement does not comply with the CCA, it is generally open to the court to do justice between the parties in terms of section 127(1). However, at the time of *Dimond,* section 127(3), a provision which has since been repealed, excluded the section 127(1) discretion in specific circumstances.[31] According to section 127(3), the court could not enforce a consumer agreement unless the debtor signed a document containing the necessary prescribed terms. Mrs Dimond never signed such a document, which meant that her agreement with 1st Automotive was irredeemably unenforceable.

Ultimately the problem before the court was whether Mrs Dimond was entitled to damages for the loss of use and enjoyment of her car caused by Mr Lovell's negligence.[32] Although the named parties in the case were the drivers, the true litigants were actually 1st Automotive and Mr Lovell's insurer, since it was their respective business interests that would be affected by the outcome of the case. The question of

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28 S 127(1).

29 S 137(2) allows the court to reduce or discharge any sum payable by the debtor if it considers it just to do so.

30 Ss 135-136 gives the court certain powers to impose conditions or suspend certain terms of the credit agreement.

31 Schedule 4 of the Consumer Credit Act 2006.

32 There was a separate issue before the court about the proper approach to quantifying damages that is not relevant here.

whether 1st Automotive had a claim for restitution based on unjust enrichment against Ms Dimond was therefore not directly before the court.

Lord Hoffmann nevertheless addressed the point. After acknowledging that Mrs Dimond had certainly been enriched at the expense of 1st Automotive, he said:

> "The real difficulty, as it seems to me, is that to treat Mrs Dimond as having been unjustly enriched would be inconsistent with the purpose of section 65(1). Parliament intended that if a consumer credit agreement was improperly executed, then subject to the enforcement powers of the court, the debtor should not have to pay. This meant that Parliament contemplated that he might be enriched and I do not see how it is open to the court to say that this consequence is unjust and should be reversed by a remedy at common law."[33]

The crisp question of whether a moneylender had an enrichment claim against a debtor if their credit agreement fell within the circumstances contemplated by sections 65(1) and 127(3) of the CCA reached the Court of Appeal in *Barons Finance Ltd v Ul-Haq*, but only in the form of an application for leave to appeal.[34] The court, in a rather cryptic dismissal of the application, repeated the dictum of Lord Hoffmann cited above and held that it was an insurmountable obstacle to the appellant's claim.

A few months later, the House of Lords again had occasion to consider the problem when it decided *Wilson v First County Trust Ltd* ("*Wilson*").[35] Mrs Wilson had borrowed money from a pawnbroker, First County Trust Ltd. The property pawned to secure the loan was her car. She did not repay the loan, which caused the pawnbroker to demand payment, failing which it would sell her car. Mrs Wilson then approached the court for an order that the agreement was unenforceable in terms of the CCA on the basis that it did not contain all the prescribed terms. In addition, she sought an order for the return of her car. It was common cause that section 127(3) of the CCA rendered the contract unenforceable because of the defects in the written document. As a result, Mrs Wilson would have been entitled get her car back and keep all the money she had borrowed. The Court of Appeal was troubled by this outcome. It therefore invited the litigants, the government and other interested parties to make submissions on whether section 127(3) of the CCA was compatible with article 6(1) of the European Convention on Human Rights[36] ("ECHR") and article 1 of the First Protocol to the ECHR.[37] The Court

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33 [2002] 1 A.C. 384 397; Lord Hoffmann cited *Orakpo* in support.
34 [2003] EWCA Civ 595.
35 [2004] 1 AC 816.
36 European Convention on Human Rights (adopted 4 November 1950, entered into force 3 September 1953) ETS 5.
37 Protocol 1 to the European Convention on Human Rights (adopted 20 March 1952, entered into force 18 May 1954) ETS 9.

of Appeal found that it was not[38] and issued a declaration of incompatibility in terms of section 4 of the Human Rights Act 1998 ("HRA").[39]

However, the House of Lords saw the matter differently. The main reason why it overturned the Court of Appeal was as a result of its finding that the HRA did not apply to the facts. This is because the legislation did not operate retroactively, and the parties had concluded their contract before the HRA came into force. However, Lord Nicholls, speaking for a unanimous court, nevertheless addressed the compatibility question since it would affect future credit agreements.

In essence, the two relevant provisions of the ECHR protect the right to a fair trial[40] (which implies the right of access to court) and the right to property respectively.[41] Lord Nicholls found the fair trial right of article 6(1) was not engaged by section 127(3) of the CCA. The right to a fair trial, he held, is a procedural right and not a substantive one. The effect of section 127(3) of the CCA was only to remove a court's discretion. It did not deny a creditor access to the court to decide, for example, whether section 127(3) applied to a particular set of facts.

On the other hand, article 1 of the First Protocol, being a substantive right, was indeed applicable. Lord Nicholls also accepted that section 127(3) amounted to a deprivation of the lender's property, in the sense that it extinguished the lender's contractual rights in favour of the borrower. However, this deprivation, he said, was justified. The purpose of the CCA was to protect borrowers, who were often vulnerable and prone to exploitation. Parliament had employed reasonably proportional means to achieve this aim. Lord Nicholls acknowledged the limitation inherent in section 127(3)'s inflexibility, namely that it could lead to unfair results in some cases. A borrower loses all their rights under these ineffective credit agreements along with any security they held. This result applies both to the lender who in good faith misinterprets the complex

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38 *Wilson v First County Trust Ltd* [2002] QB 74

39 The purpose of the HRA is to incorporate the rights contained in the ECHR into UK domestic law. Under the HRA an English court may declare legislation incompatible with the ECHR. The declaration has no binding effect. However, if such a declaration has been issued, section 10 of the HRA empowers the relevant minister to make a remedial order, which may include amending the impugned legislation, subject to approval by Parliament.

40 The relevant part of art 6(1) of the ECHR states: "In the determination of his civil rights and obligations or of any criminal charge against him, everyone is entitled to a fair and public hearing within a reasonable time by an independent and impartial tribunal established by law."

41 Art 1 of the First Protocol to the ECHR provides: "Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law."

statutory requirements of the CCA and the one who deliberately flouts them. The deprivation even follows where, as in the case of Mrs Wilson and the pawnbroker, the non-compliance caused no prejudice to the borrower. Nevertheless, Lord Nicholls held that it was open to Parliament to take the approach it did, even if that meant that some individual lenders would suffer from harsh outcomes. As for whether the lender had an enrichment claim against the borrower in this kind of situation, the court again swept aside the idea for the same reasons as in *Dimond*.

The clear trend in the cases considered here is that the English courts have consistently refused to come to the aid of lenders in the scenario under consideration. In the tension between giving effect to the policy envisioned by the legislature and the desirability of avoiding harsh results, the courts have favoured the former. One potential explanation is that the UK has a system of parliamentary sovereignty which means that English courts have much more limited powers than their South African counterparts when scrutinising legislation. It is an open question what precedential force *Orakpo*, *Dimond,* and *Wilson* would have today. Section 127(3) of the CCA has since been repealed, so the discretion from section 127 (1) now applies in all instances of non-compliance with the CCA. This means that the courts are now in principle better positioned to do justice between the parties in each individual case. An English court deciding this kind of case today would perhaps also be influenced by the reasoning of *Patel v Mirza* ("*Patel*"), where it was held that illegality is generally not a defence to a claim for restitution of an unjust enrichment and that the question must be decided with reference to a range of factors, including whether the response is proportional to the legal infringement.[42] These considerations may well justify awarding restitution rather than denying it in the case of a consumer loan that infringes the CCA.

4 2 3 German law

In contrast to South Africa and the UK, German has a more measured approach to illegal loans. As discussed in the previous chapter, the recovery of value transferred under a failed contract in German law is normally recoverable through the general enrichment action in § 812 BGB. However, where the parties are equally tainted by illegality, the claim will be barred by § 817(2) BGB. The courts have considered it undesirable for a borrower to retain all the money paid over under a usurious

[42] [2016] UKSC 42 para 116; see 3 3 4 above.

agreement.[43] This is even though these agreements are void in terms of § 138 BGB. They have therefore circumvented the operation of § 817(2) BGB by interpreting the notion of performance, or *Leistung,* in a different way.[44] The performance of the lender is not constituted by the provision of money itself, but rather by the act of making the capital available for the debtor's use for a prescribed period of time.[45] In other words, the borrower is not enriched by the money itself, but rather by the ability to use the money. The court suggested that the claim does not undermine the policy rationale of § 817(2) BGB, since the transaction principally involves the use of capital against interest. Returning the capital to the lender after the time period has elapsed is merely a so-called *Abwicklungsleistung* or "unwinding performance" and should be considered analogous to returning an item that has been pledged as a security after it has served its purpose.[46] This construction however appears to be somewhat artificial and has not garnered universal approval.[47]

As for the question of interest, the court was emphatic that the lender was not entitled to any.[48] There are conflicting views in the literature about whether this position is correct.[49] One argument is that depriving the lender of all interest amounts to a form of punishment, which is not the purpose of private law. However, there is a more compelling counterargument: if exploitative lenders were entitled to any interest, then they would essentially be allowed to operate illegally without taking any risk.[50] At best for these lenders, they get away with extracting excessive interest from borrowers. At worst they receive a market-related or statutory rate of interest. In either scenario they still profit from their wrongdoing.

It must be kept in mind that usurious loans are void because they are contrary to public policy in terms of § 138 BGB. That is what triggers the question of whether § 817(2) BGB applies. However, the BGB also contains specific rules relating to consumer loans that focus on formalities. Accordingly, in terms of § 492 BGB I the contract must be in writing while § 492 II BGB requires the agreement to contain

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43 *MüKo* § 817 para 49.
44 On the notion of performance in German and South African law, see F Botha "The Legal Nature of Performance Reconsidered" (2020) 137 *SALJ* 246.
45 RGZ 161, 52; *Staudinger* § 817 para 12.
46 RGZ 161, 52 (56).
47 MüKo § 817 para 50.
48 RGZ 161, 52 (57).
49 See *MüKo* § 817 para 49 for a summary of the debate.
50 U Loewenheim *Bereicherungsrecht* 3 ed (2007) 72-73.

certain prescribed information.[51]

The consequences of not meeting these requirements are set out in § 494 BGB. § 494 BGB I provides that a consumer credit agreement is void if it does not comply with the requirements of § 492 BGB. However, § 494 II BGB allows for the voidness to be cured under certain conditions. Specifically, it provides that the invalidity is cured to the extent that the borrower has "received the loan or drawn on it."[52] Some special conditions attach to such a curing of invalidity. First, the borrower still retains a right to withdraw from the contract.[53] Secondly, some content of the contract are modified to the detriment of the lender.[54] The most important modification is that the interest rate of the loan is reduced to the statutory rate, if the agreement contains deficient information about the rate agreed to between the parties.[55] In addition, § 494 IV BGB provides that any costs relating to the loan not stated in writing are not owed by the borrower, despite the curing of invalidity.

4 2 4 Comparison

The question of whether an illegal loan may be recovered with an enrichment claim engages conflicting policies. On the one hand, the risk exists that allowing recovery of the loan would undermine the integrity of the legal system because the infringed rule would effectively be circumvented.

However, there are also other considerations that pull in the opposite direction, such as the state of mind of the lender. Denying restitution may be quite harsh toward lenders who inadvertently failed to comply with statutory rules. For example, the sense of discomfort that one experiences about a case like *Orakpo* is at least partially rooted in the fact that the lender had no malicious intent.

Another important factor is the extent to which the parties have performed. The nature of a loan agreement is that a lender must perform first, meaning that there will always be an initial disparity between the parties. The problem with denying restitution to a lender is that the borrower could be left with a significant windfall at the expense

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51 The prescribed information is set out in art 247 §§ 6-13 of the *Einführungsgesetz zum Bürgerlichen Gesetzbuch* (Introductory Act to the Civil Code).

52 "… soweit der Darlehensnehmer das Darlehen empfängt oder in Anspruch nimmt."

53 J Schürnbrand & CA Weber "§ 494" in HP Westermann (ed) *Münchener Kommentar zum Bürgerlichen Gesetzbuch* 8 ed (2019) para 25.

54 In terms of §§ 494 II(2) and 494 III-VI BGB. If the agreed rate is already lower than the statutory rate, the agreed rate remains in force.

55 § 494 II(2) BGB.

of the lender.

Finally, there is the overarching concern of the need for the court to achieve a result that is proportional to the illegality. Proportionality is not necessarily a self-standing factor but may have considerable influence when considered together with the other factors.[56] For example, the court in *Opperman* regarded it disproportionate that the NCA did not allow for a differentiation between lenders who intentionally exploit consumers and those innocently failed to register as credit providers.[57]

The difficulty presented by illegal consumer loans is that both awarding and denying restitution has its downsides. Awarding restitution risks damaging the integrity of the legal system whereas denying restitution risks an outcome that is disproportionately harsh on the lender. The best solution to this conundrum may be to allow judges a discretion whether restitution should be available or not. The policies of preserving the integrity of the legal system and achieving outcomes that are generally considered proportionate and fair need not be mutually exclusive. Indeed, they can be achieved without resorting to harsh sanctions. A particularly attractive solution is to allow the lender to recover the capital but not interest.[58] Binns-Ward J, sitting in the court *a quo* in *Opperman,* said the following:

> "[T]he only reason any person would wish to do business in the field of providing credit … is to make a profit, which is achieved through the levying of interest, charges and fees of the sort comprehended in section 101 of the NCA. A credit provider who was party to an agreement that was void by reason of section 40(4) would not be able to legally recover or retain any interest, charges and fees contemplated in terms of the transaction."[59]

It is questionable whether additionally depriving the lender of their capital would be that much of a stronger incentive to comply with the law than the deprivation of profit. Nor is there a good justification for why the borrower should in such a case be entitled to a windfall. This approach also has the benefit that a lender, such as in *Opperman* or *Orakpo,* who unintentionally failed to comply with the law is not left completely out of pocket.

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56 See 5 2 3 7 below.

57 *National Credit Regulator v Opperman* 2013 3 SA 1 (CC) para 76.

58 See for example the Canadian case of *Tsoi v Lai* 2012 BCSC 1082. The plaintiff had lent money to the defendant knowing that it would be used to finance an illegal gambling operation. The court awarded the plaintiff an enrichment claim for the capital of the loan, but not the interest. The main reason was that the need to avoid the defendant being left with a windfall weighed more heavily than the court's concern about the illegality.

59 2012 ZAWCHC 27 para 40.

4 3 Illegal contracts of employment

4 3 1 Introduction

Illegal contracts of employment also raise an indirect enforcement problem. Consider the facts of *Nizamuddowlah v Bengal Cabaret Inc* ("*Nizamuddowlah"*), a case decided in the state of New York.[60] A restaurateur meets a man in Bangladesh and invites him to come and work at his restaurant in New York City. The restaurateur offers to arrange a visa for the man to enter the United States and promises to assist him eventually in obtaining permanent residency there. For twenty months the employee receives no remuneration for his services, nor any help with his residency application. After eventually obtaining residency through his own efforts, he sues the restaurant to recover his wages. The employer objects on the basis that the employment contract was illegal. Should such a claim succeed? On the one hand, there is the risk in such a case that the integrity of the legal system could be undermined if the claim is allowed. On the other hand, as Birks remarked, "to rule out the claim by the unpaid illegal immigrant would be to increase the possibility of grievous exploitation, approaching slavery."[61]

Interestingly, this issue does not appear to have troubled German courts. Arguably the reason is that § 98a of the Germany's Residence Act[62] explicitly requires an employer to pay for services rendered by an employee even if the employee was not allowed to work in Germany.[63] Sex work, another paradigm case in some jurisdictions, is legal in Germany, so the issue of illegal employment does not arise there either.[64] Accordingly, the focus of this section will be on South Africa and England where some instructive cases dealing with illegal employment have reached the courts in the past few years.

4 3 2 South Africa

As with the law of consumer credit, the development of the law on illegal employment in South Africa must be viewed in its historical context. During apartheid the labour

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60 (1977) 399 NYS 2d 854; but see also the judgment of the US Supreme Court in *Hoffman Plastics Inc v NLRA* 53545 137 (2002).

61 P Birks "Recovering Value Transferred under an Illegal Contract" (2000) 1 *Theoretical Inq L* 155 174.

62 *Aufenthaltsgesetz* 30 07 2004.

63 *MüKo* § 134 para 85.

64 § 1 *Prostitutionsgesetz* 20 12 2001.

rights of people of colour were severely restricted.[65] The courts would not assist employees who were party to prohibited contracts of employment, particularly where the legislation in question formed part of the apartheid statutory regime.

A case in point is *Lende v Goldberg* ("*Lende*").[66] The appellant was employed as a domestic worker but did not have a permit to work in the area where her employer lived.[67] After being dismissed, she sued her employer for wages. However, the High Court dismissed her claim in contract on the basis that the legislature intended for the contract to be void.[68] The court also considered whether the appellant was entitled to an enrichment claim, but ultimately dismissed the possibility on the basis that the claim had not been properly argued. The court further held that even if a case had been made out, it would not be appropriate to relax the *par delictum* rule in the circumstances.[69]

Litigants before industrial tribunals fared no better. These tribunals refused to assume jurisdiction over employees whose contracts of employment were illegal.[70] This meant, for example, that a Mozambican national who did not have a permit to work in South Africa could not claim compensation for allegedly unfair labour practices.[71]

In the constitutional era this area of the law has undergone significant development. Before considering these changes, it is necessary to revisit some basic principles of labour law. The labour law regime in South Africa consists mainly of a cluster of rights contained in various statutes, of which the most relevant for present purposes is the Labour Relations Act 66 of 1995 ("LRA"). If a labour dispute cannot be settled through mediation, it proceeds to arbitration before the Commission for Conciliation, Mediation and Arbitration ("CCMA"). A dissatisfied litigant may take an award from the CCMA on review to the Labour Court ("LC"). Finally, a decision of the LC may be appealed to the Labour Appeal Court ("LAC").

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65 C Garbers, PAK Le Roux, A Basson, M Christianson & W Germishuys-Burchell *The New Essential Labour Law Handbook* 7 ed (2019) 4-8.

66 1983 2 SA 284 (C).

67 As required by s 10bis of the Blacks (Urban Areas) Consolidation Act 25 of 1945.

68 The matter came before a civil court, because at the time domestic workers were excluded from the general labour legislation; Garbers et al *Labour Law* 64.

69 It is questionable whether the parties were truly *in pari delicto* since the criminal prohibition in the applicable legislation only targeted the employer and not the employee. An enrichment claim for the value of services already rendered should arguably have succeeded; A C Beck "Illegal Employment and the Par Delictum Rule" (1984) 101 *SALJ* 62 65-66.

70 *Norval v Vision Centre Optometrists* (1995) 16 ILJ 481 (IC).

71 *Dube v Classique Panelbeaters* [1997] 7 BLLR 868 (IC).

For workers to assert any rights under labour law legislation, they must fall within the definition of an employee as contemplated by the particular statute they intend to rely on.[72] If the worker cannot satisfy this definition, then none of the fora mentioned above are entitled to exercise jurisdiction over the dispute. Ordinarily an employment relationship may be established by showing that a valid contract of employment exists between the parties. However, since illegal contracts of employment are typically void, it is much harder for employees to bring themselves within the statutory definition required by the CCMA to assume jurisdiction. Furthermore, even if illegal employees can satisfy the definition, the question of what remedy is available, remains. These issues have been considered by two important judgments, to which we now turn.

4 3 2 1 Employment contrary to immigration law

Consistent with pre-constitutional labour law jurisprudence, the general approach of CCMA commissioners was typically to deny that they have jurisdiction over foreign employees without a permit since they were not thought to be employees in terms of the LRA. Against the tide, one commissioner took the opposite view. When this decision was taken on review in *Discovery Health Limited v CCMA* ("*Discovery*"), the LC had its first opportunity to rule on the issue.[73] The employee in *Discovery* was an Argentinean national lawfully resident in South Africa. A few months after starting work at the applicant, his work permit expired. Upon discovering this, his employer dismissed him without a hearing, prompting him to bring an unfair dismissal claim against his employer. The employer argued that the CCMA had no jurisdiction. The reason was that the contract of employment was void since it contravened section 38(1) of the Immigration Act 13 of 2002.[74] This in turn meant that the employee did not satisfy the definition in the LRA that is required for jurisdiction to be triggered.

The LC disagreed. It pointed out that the prohibition on section 38(1) says nothing about the validity of an employment contract. It only targets the conduct of employing a foreigner without permission to work. Although in *Lende* a similarly worded provision

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[72] S 213 of the LRA defines an employee as: "(a) any person, excluding an independent contractor, who works for another person or for the State and who receives, or is entitled to receive, any remuneration; and (b) any other person who in any manner assists in carrying on or conducting the business of an employer …" The same definition appears in s 1 of the Basic Conditions of Employment Act 75 of 1997 and a similar one in s 1 of the Employment Equity Act 55 of 1998

[73] (2008) 29 ILJ 1480 (LC).

[74] The relevant part of s 38(1) states: "(1) No person shall employ … (b) a foreigner whose status does not authorise him or her to be employed by such person …". In addition, s 49(3) makes it a crime to knowingly employ a foreigner in contravention of the Immigration Act.

was found to nullify the contract, the LC noted that the approach for interpreting statutes has changed since the advent of the Constitution.[75] Nowadays, if a provision is capable of being interpreted in a manner that did not limit constitutional rights, then that interpretation should be preferred.[76] Accordingly, the LC found that section 38(1) should not be construed as invalidating the contract. To hold otherwise would limit the worker's right to fair labour practices enshrined in section 23 of the Constitution. In addition, it was held that there is a good policy reason for this interpretation. If the contract were void, it would open the door for all sorts of abuses by unscrupulous employers willing to risk the criminal penalty. Such employers could for example refuse to remunerate a foreign employee properly or make them work hours in excess of the statutory maximum. The employee would have no recourse against the employer in these circumstances. The injustice is compounded by the fact that many foreign employees without authorisation to work are in precarious positions and may have few alternatives available to them other than accepting employment from an exploitative employer. Accordingly, the court held that the contract between the parties was valid and that the CCMA therefore had jurisdiction.[77] As for the objection that this result meant that the CCMA would necessarily condone illegality when it assumes jurisdiction in these circumstances, the court replied that rather than sanctioning illegality, granting jurisdiction would expose the illegality instead. This might ultimately be a stronger deterrent for employers not to contravene the Immigration Act, since there is a greater risk that their illegal conduct would come to light.

4 3 2 2 Sex work

The second important case is the difficult matter of *Kylie v CCMA*.[78] The appellant was a sex worker who alleged that she had been unfairly dismissed from her employment at a massage parlour. Once again, the question arose whether the CCMA had jurisdiction over the matter in view of the illegal nature of the appellant's employment.[79]

The LC took a different approach than in *Discovery*. It accepted that the appellant

[75] The LC also appeared to approve of literature that criticised the reasoning and outcome in *Lende*; *Discovery* par 27.
[76] *Discovery* para 28 relying on *NUMSA v Bader Bop (Pty) Ltd* 2003 3 SA 513 (CC) para 37.
[77] The court also held *obiter* that even if the contract had been void, an employment relationship existed between the parties. This fact satisfied the definition of 'employee' in the LRA, since the definition makes no mention of a valid contract of employment as a necessary requirement; *Discovery* para 35-50.
[78] 2010 4 SA 383 (LAC).
[79] Engaging in sex work is criminalised by s 20(1)(A)(a) of the Sexual Offences Act 23 of 1957.

may very well be an employee within the meaning of the LRA, even in the absence of a valid contract of employment. However, this was not the real issue at stake. Instead, the court defined the issue as:

> "[W]hether as a matter of public policy, courts (and tribunals) by their actions ought to sanction or encourage illegal conduct in the context of statutory and constitutional rights."[80]

The court answered the question in the negative. It found that if the contract of employment were enforced or the appellant's constitutional right to fair labour practices recognised in the circumstances, the court would be sanctioning illegal activity.[81] In other words, while the appellant may well be an employee within the statutory definition, it did not follow that she was entitled to protection.[82]

The LC also distinguished the appellant's case from that of an illegally employed foreigner. In the latter case, the illegality is concerned with the identity of the person undertaking the work, rather than the work itself. In addition, disallowing illegal foreigners labour rights encourages employers to employ them, which is exactly the situation that the Immigration Act intends to prevent.[83] The case of a sex worker is different, because the work itself is illegal. Accordingly, though accepting that sex workers are also typically in vulnerable positions, the court held that protecting them from exploitation would necessarily amount to sanctioning activities that the legislature has decided to prohibit.[84]

The LAC saw the matter differently. Its judgment is somewhat difficult to follow because the court did not clearly define the issues at stake.[85] It only cited the LC's formulation of the issue but engaged no further with it. The key to a clearer understanding of the case, it is suggested, lies in a closer analysis of the issues that were before the court. The question was whether the CCMA had jurisdiction over the claim – but what does that mean? Jurisdiction is a procedural question consisting of

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80 (2008) 29 ILJ 1918 (LC) para 23.

81 S 23(1) of the Constitution states: "Everyone has the right to fair labour practices."

82 This reasoning must be regarded with suspicion since the court was begging the question with the manner in which it framed the issue. The formulation is in fact the court's conclusion merely put as a question. It admits of only one answer since it would be patently absurd to hold as a general proposition that a court should sanction illegal conduct. It is analogous to positing an unfalsifiable hypothesis for a scientific experiment.

83 (2008) 29 ILJ 1918 (LC) para 70.

84 (2008) 29 ILJ 1918 (LC) para 71.

85 KJ Selala "The Enforceability of Illegal Employment Contracts According to the Labour Appeal Court: Comments on *Kylie v CCMA* 2010 4 SA 383 (LAC)" (2011) 14 *PELJ* 207 213. See also L Muswaka "Sex Workers and the Right to Fair Labour Practices: *Kylie v Commissioner for Conciliation Mediation and Arbitration*" (2011) 23 *SA Merc LJ* 533; D Smit & V du Plessis "'Kylie' and the Jurisdiction of the Commission for Conciliation, Mediation and Arbitration" (2011) 23 *SA Merc LJ* 476.

two legs, namely whether the CCMA is empowered to hear the matter and secondly whether it could effectively enforce an arbitration award in the circumstances.[86] The first leg, it is submitted, concerns the question whether the employee falls within the definition of the LRA. On this leg, there was significant debate about the reach of section 23 of the Constitution and the LRA that need not trouble us here. The LAC held that the appellant fell within the LRA's definition, notwithstanding the fact that the contract of employment was void due to illegality.[87] It was the second leg that posed the greater difficulty. The issue here was whether the CCMA could grant any remedy that would not amount to sanctioning illegal activity. This is so because the CCMA could only effectively enforce an award if that award did not amount to sanctioning an illegality. In other words, it could not issue an award that would require any of the parties to commit a crime.

On this issue the LAC found that the appellant was entitled to some protection under the LRA and Constitution. In support of this finding, the court placed particular emphasis on the fact that the appellant formed part of a vulnerable class by virtue of the work she performed[88] and was entitled to be treated with dignity despite the illegality of it.[89]

Although the court was not called upon to decide what kind of remedy should be awarded in the particular circumstances, it did give some guidelines on what might be appropriate. It stressed that the full suite of remedies provided for in the LRA would not necessarily be available in every case concerning illegal employment. In each case the tribunal or court will be required to weigh the competing policy considerations against each other.[90] Reinstatement was certainly not an option, since that would clearly undermine the Sexual Offences Act. Similarly, monetary compensation for a substantively unfair dismissal would also probably be unavailable in so far as it amounts to compensation for the loss of employment. However, for a procedurally unfair dismissal, monetary compensation could be an appropriate remedy since it is

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86 This analysis of the problem draws on Selala (2011) *PELJ* 207 215.

87 2010 4 SA 383 (LAC) para 37. This judgment is an example of a court using the narrow definition of the term 'illegal contract,' see 2 2 above.

88 The court noted that not all sex workers will necessarily be in a vulnerable position but regarded it as generally the case in the South African context. It was in any event clear that the appellant occupied a position of vulnerability in her employment: she lived with her employer, she was required to work long hours and had to follow a strict regime of rules; 2010 4 SA 383 (LAC) para 43.

89 2010 4 SA 383 (LAC) para 19, relying on *S v Jordan* 2002 6 SA 642 (CC) para 74.

90 2010 4 SA 383 (LAC) para 56; but see the criticism in J du Plessis "Some Thoughts on the Consequences of Illegal Contracts" (2021) *Acta Juridica* 177 n 76.

compensation not for the loss of employment, but for the loss of a fair procedure.[91] After the LAC referred the matter back to the CCMA, the parties reached a confidential settlement.[92] No case on illegal employment has been reported since then, so while it is now clear that employees working illegally may bring their disputes before the CCMA, it remains to be explored in more detail what remedies they would be entitled to. The challenge for justifying any remedy would be to show that it does not subvert the purpose of the infringed legislation, or if it does, that there are good reasons for it.

4 3 3 England

The contractual claims of migrants without work permits have received significant attention in English law. However, as with any aspect of the doctrine of illegality, this is a challenging area of the law. Part of the complexity is attributable to the fact that considerable disagreement remains about whether some of the leading cases on illegal migrant work should be classified as instances of statutory illegality or common-law illegality.[93] As was argued above, this distinction is often difficult to apply and may ultimately not be so helpful, since there is a considerable convergence in the way both categories of cases are dealt by the courts.[94]

The first case traditionally cited in employment matters dealing with illegality is *Hall v Woolston Hall Leisure* ("*Hall*").[95] There the court identified three categories in which illegality may operate as a defence. The first category is "where a contract is entered into with the intention of committing an illegal act."[96] The second "is where the contract is expressly or implicitly prohibited by statute."[97] This is the category typically regarded as statutory illegality by commentators. The third category is where the contract itself is lawful but performed in an illegal manner.[98] This is known as performance illegality.[99] What has become known as the *Hall*-test relates to this third category. It provides that illegality may only succeed as a defence against a contractual claim if the claimant knowingly participated in the illegal performance. In other words, knowledge plus

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91 2010 4 SA 383 (LAC) para 52-53.
92 Smit & Du Plessis (2011) 23 *SA Merc LJ* 487
93 See A Bogg "*Okedina v Chikale* and Contract Illegality: New Dawn or False Dawn?" (2020) 49 *ILJ* 258 271.
94 See 3 3 2 above.
95 [2001] 1 W.L.R. 225; see also *Robinson v HRH Al Qasimi* [2021] EWCA Civ 862; *Enfield Technical Services Ltd v Payne* [2008] ICR 1423.
96 [2001] 1 W.L.R. 225 para 30.
97 Para 30.
98 Para 31.
99 See 3 3 2 above.

participation is required.

The English courts have generally not come to the aid of employees whose immigration status did not permit them to work. A leading example is *Zarkasi v Anindita* ("*Zarkasi"*).[100] The claimant met her employer in Indonesia where they agreed that she would move to London for two years and work as a domestic worker in the home of the employer. The claimant then fraudulently obtained a passport and tourist visa under a false identity in order to enter the UK. During her employment she was paid less than the minimum wage. After the two years were over, her employer requested that she stay longer. The claimant wanted to return to Indonesia. She therefore approached a human trafficking charity to assist her, which in turn led to her instituting various claims against her employer. The Employment Appeal Tribunal ("EAT") held that the illegality in this case fell within the second category of *Hall*. Any contract of employment entered into by the claimant was illegal at the outset since she did not have the right to work in the UK. However, the EAT did not specify which statutory provision had been contravened.[101] It was simply assumed to be common knowledge that employing a foreigner without a work permit was a criminal offence. From this the EAT held that once a contract falls within the second category of *Hall,* the rule is clear that as a matter of public policy, the contract may not be enforced. In other words, preserving the integrity of the law was regarded as more important than any potential countervailing considerations.[102] Accordingly, the claimant's appeal was dismissed.[103]

The same result followed in *Blue Chip Trading Ltd v Helbawi.*[104] Here the EAT dismissed the claim of a foreign student who had worked more hours than his visa allowed for. Once more the EAT reached its conclusion without specifying the legislative provision that had been contravened.

The first indication of an approach more sympathetic to the plight of an illegal migrant came in *Hounga v Allen* ("*Hounga*").[105] The claimant was brought to the UK from Nigeria as a child to work as a domestic worker. She submitted false documentation to obtain a visitor's visa and remained in the country after it had

[100] [2012] ICR 788.
[101] Bogg (2020) *ILJ* 264.
[102] [2012] ICR 788 para 30.
[103] The argument by the claimant that she was a victim of human trafficking and therefore entitled to relief as an exception to the general rule, taking into account international instruments against human trafficking, also failed.
[104] [2009] IRLR 128. See also *Vakante v Governing Body of Addey and Stanhope School* (No 2) [2005] ICR 231.
[105] [2014] UKSC 47.

expired. She was never paid and endured severe abuse from her employer, who threatened that she would be imprisoned if she left the house and got caught since she was in the UK illegally. After being dismissed, the claimant sued her employer for unpaid wages and damages flowing from racial discrimination. Her contractual claim for unpaid wages was rejected by the EAT on the basis that she knew her employment was illegal, thus satisfying the *Hall*-test for performance illegality.[106] In subsequent appeals before the Court of Appeal and Supreme Court she did not pursue the contractual claim any further.[107]

The issue on appeal was only whether the illegality of her employment also barred her statutory tort claim for racial discrimination. On this issue, the Supreme Court held that it did not. In arriving at this conclusion, the court considered the following factors to be important. First, that awarding her claim did not allow her to profit from her wrongful conduct, since it amounted to compensation for hurt feelings resulting from her abusive employment situation and dismissal. Second, the compensation did not allow for an evasion of the penalty prescribed by criminal law for illegal employment. Third, dismissing the claim would compromise the integrity of the legal system more, since employers like Ms Allen may be encouraged to exploit employees in the situation of Ms Hounga if they know that they will have no claim against them. Finally, the court considered there to be strong evidence that Ms Hounga was a victim of human trafficking under international law and that this was another factor in favour of awarding her claim.[108]

From this reasoning it should be clear that *Hounga* was a prelude to the approach laid down in *Patel*, since the court applied a 'range of factors' approach to assessing the impact of the illegality. Indeed, in *Patel* itself both Lord Toulson and Lord Sumption suggested that she should arguably have succeeded with a claim for quantum meruit even if it were correct that Ms Hounga's contractual claim was unavailable.[109]

The Supreme Court in *Hounga* dealt with a tort claim, so the impact of *Patel* on the enforceability of an illegal contract of employment remains somewhat uncertain. The

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[106] *Hounga v Allen* [2011] Eq LR 569. Unlike the previous cases, the relevant statutory prohibition was identified as s 24(1)(b)(ii) of the Immigration Act 1971, which makes it a crime for someone who is not a British citizen not to observe a condition of their leave to remain in the UK.

[107] Indeed, the Supreme Court seemed to assume that her contractual claim was unavailable; *Patel* para 54. It has been suggested that this assumption was wrong; J O'Sullivan "Illegality and Contractual Enforcement*"* in S Green & A Bogg (eds) *Illegality after* Patel v Mirza (2018) 165 182

[108] *Hounga* para 47-49.

[109] *Patel* para 119, 243. See *Mohamed v Alaga & Co.* [2000] 1 WLR 1815, discussed above at 3 3 6.

best available guide to the question is the recent case of *Okedina v Chikale* ("*Okedina*").[110] The facts are similar to *Hounga* and *Zarkasi*. The claimant was a Malawian national brought to the UK by her employer, the appellant, to work as a domestic worker. She had a valid work visa that expired after six months. Despite the expiration, she continued to work for the appellant for another two years before being dismissed.

The claimant subsequently brought several claims against her employer for unfair dismissal, deduction of wages and race discrimination. Naturally the employer objected on the basis that the contract of employment was illegal. However, the claim could not simply be rejected on the basis of *Zarkasi* because it had one important distinguishing feature. The claimant was unaware of her illegal visa status. The employer had promised that she would take responsibility for extending the claimant's visa. She had in fact made a fraudulent application on the claimant's behalf that was rejected and never told the claimant about it.

The court categorised the case as a problem of statutory illegality. In other words, the question was whether the contract was impliedly prohibited by statute that had been infringed. The employer was constrained to rely on the statute, since the doctrine of common-law illegality was unavailable. The reason is that the knowledge-requirement of the *Hall*-test was not met. Strictly speaking, this made it unnecessary to apply the approach in *Patel*. Nevertheless, the court remarked that *Hall* was consistent with the approach in *Patel.* It approved of counsel's explanation that "*Hall* is how *Patel* plays out in a particular type of case."[111]

As for the question of statutory illegality, the court identified sections 15 and 21 of the Immigration, Asylum and Nationality Act 2006 ("the 2006 Act") as the provisions that had been contravened.[112] These provisions prescribe civil and criminal penalties for the conduct of knowingly employing a person who is disqualified from employment by virtue of their immigration status. After analysing the provisions, the court concluded that they were not intended by Parliament to invalidate a contract of employment with a foreigner who did not have the correct immigration status. Although there is a clear public interest in preventing foreigners with the wrong immigration status from working, the statutory provisions in question were directed only at the employer and not the

[110] [2019] I.C.R. 1635. For analysis, see Bogg (2020) *ILJ* 258.
[111] *Okedina* para 62.
[112] Para 25-28.

employee.[113] The court also noted that foreign workers are often vulnerable to exploitation and may be, as in the present case, genuinely mistaken about their immigration status. Accordingly, the contract was not unenforceable in the circumstances.

After *Hounga* and *Okedina* it would seem that the English courts are becoming more willing to assist illegal foreign workers than before. However, whether this trend will continue, at least in the context of contractual claims, is uncertain. The relevant legislation has been amended since the period with which *Okedina* was concerned. The Immigration Act 2016 ("the 2016 Act") now criminalises the conduct of the employee as well as the employer.[114] If one applies the reasoning in *Okedina,* it seems to follow that an illegal foreign employee would no longer have a valid contractual claim against their employer. This is because the court's main justification for its finding was that the prohibition in the 2006 Act was directed at the employer only. In addition, the 2016 Act allows for the potential confiscation of illegally earned wages as proceeds of crime.[115] It remains to be seen how the courts will apply this new provision.

4 3 4 Comparison

In both South Africa and England there is a trend towards affording greater protection to employees who are party to illegal contracts. In South Africa it is now beyond doubt that the CCMA has jurisdiction to arbitrate disputes concerning employees with illegal employment contracts and in England, *Hounga* and *Patel* have given foreign employees more ammunition with which to fight their cases.

This trend may arguably be explained as a development in judicial thinking about how various policy considerations interact in this context. In a case like *Lende,* the reasoning was simply that awarding any claim to the employee would undermine the applicable legislation. This would in turn damage the integrity of the legal system because it would render the law incoherent. However, in more recent cases such as *Discovery* and *Hounga,* it has been recognised that not awarding a remedy may in fact do more harm to the integrity of the legal system since it may allow employers to exploit their illegal employees with impunity. The fact that illegal employees are often vulnerable due to their personal circumstances may therefore warrant affording them

[113] Para 65.
[114] S 34.
[115] S 34.

some degree of protection.

The question is what sort of remedy would be appropriate. A good place to start may be to accept that reinstatement could never be an option, since this would amount to ordering the employer, and perhaps also the employee, to commit an illegality. The question is rather to what extent compensation may be awarded. It is difficult to justify the suggestion that compensation for future lost wages should be awarded, since that would probably be seen as perpetuating the illegal contract. On the other hand, there is a good case for awarding compensation for services already rendered by the employee. The German legislature has adopted this approach and in England, *Patel* has hinted that a quantum meruit should in principle be available in such a case. South African courts have not yet considered the point, but there is academic support for the idea.[116]

The underlying factor at stake here is the extent to which the contract has been performed. In a case where there is a greater disparity between the respective performances of the employee and employer, there is a stronger case for awarding some form of compensation. For example, in a case like *Nizamuddowlah,* the employer would have been significantly enriched at the expense of the employee if the employee's claim had been denied.[117] That is not to say that the award would necessarily have to be equal to the full salary of the employee. However, at the very least it would seem sensible that compensation for services rendered should at least accord with the minimum wage of the particular jurisdiction.[118]

Compensation in whatever form arguably amounts to indirect enforcement of an illegal contract to a greater or lesser extent. However, depending on what the compensation is for, it may nevertheless be the preferable outcome if it means avoiding an even greater evil, such as sanctioning the employer's exploitation of the employee.[119]

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[116] Beck (1984) *SALJ* 65-66.
[117] (1977) 399 NYS 2d 854.
[118] *Nizamuddowlah v Bengal Cabaret Inc* (1977) 399 NYS 2d 854. In this regard South Africa has recently passed the National Minimum Wage Act 9 of 2018; see Garbers et al 98-102 for a discussion.
[119] Birks (2000) *Theoretical Inq L* 174. German law also recognises the need to relax § 817(2) BGB where doing so is necessary to avoid a greater injustice; see 3 2 4 above.

4 4 Contracts that infringe construction law

4 4 1 Introduction

In the twenty-first century, legislation has come to regulate just about every industry in which services are provided to the public. Often the purpose of these laws is to protect consumers of these services. To achieve this aim, these laws often require service-providers in the relevant industry to acquire some sort of license or to register with an oversight body. In addition, they often require the contract to be in writing. A failure to comply usually attracts criminal and/or civil penalties. However, these laws do not always specify what consequences should follow for a contract concluded with a service provider who has not complied with the relevant statutory requirements. The suggestion that it is simply a matter of statutory construction is an insufficient answer. The language and purpose of the relevant provisions are indeed important, but other factors may be decisive depending on the context, particularly where the question is whether the service-provider is entitled to restitution of any benefits conferred under the tainted contract.

It would be impossible to consider every regulated industry with its own unique characteristics here. Instead, the focus will be on the building industry, understood in the wide sense of the term, as a good representative category.[120] As will become clear, although courts around the world reach different outcomes in similar cases, their reasoning is often founded on the same underlying policy factors.

The problem of illegal building contracts has already received some attention in Chapter 2's discussion of *Cool Ideas 1186 CC v Hubbard* ("*Cool Ideas*").[121] There the issue before the court was whether an arbitration award made in favour of a home builder could be enforced if the builder was not duly registered under the applicable legislation. A key part of the reasoning that led to the court's dismissal of the home builder's case was that in order to protect consumers, the contract between the parties had to be regarded as valid but was nevertheless unenforceable in the hands of the builder. The builder's claim therefore failed. As pointed out in Chapter 2, the problem with this finding is that it uncritically excluded the possibility of considering whether the builder may have been entitled to an enrichment claim. Although it was correct that

[120] This includes cases with builders as well as other contractors related to the building industry, such as electricians or home renovators.
[121] 2014 4 SA 474 (CC); see 2 6 above.

the arbitration award itself could not be enforced, there seemed to be a strong case in favour of awarding restitution in the form of an enrichment claim to the builder. It is not necessary to traverse *Cool Ideas* again here. Instead, it is suggested that the case provides a good point of departure for investigating the problem from a comparative perspective. A number of common-law jurisdictions have dealt with similar cases where a party to an agreement between a builder and a client raised the defence of illegality to resist a claim. In addition, there has recently been some interesting developments in Germany in cases relating to so-called clandestine work or *Schwarzarbeit*. These all merit investigation.

4 4 2 England

Despite the strictness of the reliance rule in the English law of the 20th century, there is one case where the court seemed content to allow the rule to be circumvented.[122] In *Strongman (1945) Ltd v Sincock* ("*Strongman*"), the plaintiff was a builder who had performed building work for the defendant, an architect by profession.[123] Licenses under wartime regulations were obtained, but they only authorised work up to the value of £2 150. The value of the work ultimately performed by the plaintiff amounted to £6 359. The defendant refused to pay more than the value authorised by the licenses and resisted the plaintiff's claim for the difference by relying on the illegality of the contract.

The court proceeded from the premise that the plaintiff clearly could not sue on the building contract. Contracts for work performed without a licence had previously been treated as unenforceable and infringing the regulations constituted a crime.[124] However, the plaintiff argued that it was not suing on the original contract. The defendant had promised that he would obtain all the necessary licences for the project. If the work exceeded the amounts of the original licences he would apply for supplementary ones. If he failed to obtain these supplementary licences, he would instruct the plaintiff to cease working. The court accepted the plaintiff's argument that this promise by the defendant amounted to a separate contract, collateral to the original one. The plaintiff could therefore be awarded damages for the defendant's

[122] The reliance rule provided that a claim cannot be enforced if a claimant has to rely on their own illegal conduct in order to establish their cause of action. This rule was followed in English law before *Patel v Mirza* [2016] UKSC 42 was decided; see 3 3 3 above.
[123] [1955] 2 QB 525.
[124] *Bostel Bros Limited v Hurlock* [1949] 1 KB 74. For Scotland, compare *Jamieson v Watt's Trustees* 1950 SC 265, discussed at 3 4 2 above.

breach of this collateral contract, provided that the plaintiff had not been negligent. The fact that awarding damages for breach of the collateral contract would yield the same outcome than if the original contract had been enforced did not seem to trouble Lord Denning, who delivered the leading judgment.[125] While it is true that illegality should not be circumvented, he said, the principle did not apply to a case such as this one, where the plaintiff was an innocent party.[126]

It is curious that the court in *Strongman* did not consider the policy objective of the regulations in its decision. Other than *Mohamed v Alaga & Co*, it was indeed a rare sight during the reign of the reliance rule for an English court to allow a contract that was so plainly illegal to be circumvented.[127] One can at this stage only speculate over what impact *Patel* will have on this kind of scenario.[128]

4 4 3 Australia

Pavey & Matthews v Paul (*"Pavey"*) is a decision by the High Court of Australia that is best known for recognising unjust enrichment as a unifying concept that may explain the imposition of obligations of restitution in Australian law.[129] The merits of the case, however, is what is of interest here. The appellant was a builder who had entered into an agreement with the respondent to renovate a cottage for her. After the work had been completed, the respondent paid only A$36 000 to the appellant, A$27 000 short of the A$63 000 that the appellant alleged to be the reasonable value of its services and the materials provided. The obstacle in the appellant's way was section 45 of the Builders Licensing Act 1971 (N.S.W) ("BLA"). The essence of the provision was that a contract for building work entered into by a licensed builder is not enforceable against the other party unless it is in writing, signed by both parties and sufficiently describes the building work being contemplated. The appellant was duly licensed. However, the agreement between the parties was not reduced to writing. In addition to what work should be performed, it provided only that the respondent would provide reasonable

[125] It is evident that Lord Denning was intent on coming to the aid of the plaintiff. Early in his judgment he declared: "The architect has no merits at all"; [1955] 2 QB 525 533. The defendant had cynically taken the point of illegality to avoid paying what he admitted would otherwise have been due.

[126] If the plaintiff had been negligent in trusting the defendant, the claim would have failed; *J. Dennis & Co. Ld. v Munn* [1949] 2 KB 327. The fact that the defendant in *Strongman* was an architect meant that the plaintiff was not negligent in trusting his assurances, since architects commonly took responsibility in construction contracts for obtaining the necessary licenses.

[127] [2000] 1 WLR 1815. On collateral contracts tainted by illegality in English law, see *Spector v Ageda* [1973] Ch 30; *Fisher v Bridges* (1854) 3 E & B 642.

[128] J Beatson, A Burrows & J Cartwright *Anson's Law of Contract* (2020) 423.

[129] (1987) 162 C.L.R. 221 256-257.

remuneration for the work, calculated with reference to the prevailing market rate in die building industry.

The majority of the court found that the contract was indeed unenforceable in the hands of the appellant due to section 45 of the BLA, but that this did not exclude an action on a quantum meruit based on unjust enrichment. In other words, the basis for the appellant's claim was not the promise of the respondent to pay contained in the contract. Instead, it was the appellant's execution of building work and its acceptance by the respondent. The relevance of the contract was only to show that the work was not intended as a gift.

Having established the basis of the claim, the court proceeded to consider whether awarding it would undermine the purpose of the BLA. As with the statute in *Cool Ideas,* it was held that its purpose was to protect building owners. This includes protecting the building owner from a claim where the written contract fails to describe the project sufficiently. However, said the court, it would be a stretch too far to accept that this statutory protection also extends to a building owner who requests and accepts building work and then refuses to pay for it after the fact because the contract did not comply with statutory formalities. It is difficult to imagine that such draconian implications were intended by the legislature and an interpretation that avoids such harshness without undermining the purpose of the BLA ought to be preferred. Accordingly, the court held that the term "unenforceable" in the BLA should be narrowly construed to refer only to the contract and not to include any non-contractual remedies that might be available.

4 4 4 Canada

In Canada the courts have been willing to excuse non-compliance with formalities, but not wholesale unlicensed work. So, for example in *C. Battison & Sons Inc. v Mauti* the plaintiff builder successfully enforced an oral contract despite infringing a municipal by-law that required the contract to be in writing.[130] The court held that the by-law should be narrowly construed so that it does not invalidate the contract. It regarded the existing criminal penalties imposed by the by-law to give sufficient effect to the purpose of the statute. In addition, it considered that the defendant would be unjustly enriched if the contract were unenforceable and that this would amount to a

[130] 1986 CarswellOnt 649.

disproportionate punishment for the plaintiff. However, the plaintiff in *Kocotis v D'Angelo,* an unlicensed electrician, did not receive the same leniency.[131] His attempt to enforce a contract for work he had performed was dismissed on the basis that it would undermine the intention of the legislature if his claim were allowed. These two cases turned on the enforceability of the contract.

The question whether a claim for quantum meruit could succeed was addressed in *688558 Ontario Ltd. v Morgan* ("*Morgan*").[132] The plaintiff was a general contractor engaged by the defendant to manage the renovation of her house. The plaintiff did not have the right licence for this kind of work, so it sought to recover the value of the labour and materials it provided with an enrichment claim. The court held that in adjudicating the claim it had to balance factors such as the purpose of the prohibition, the relative fault exhibited by the conduct of both parties, the appropriateness of the statutory penalty and the windfall granted if restitution is denied. Taking all these into account, it was held that that the claim could not be granted, because doing so would undermine the purpose of the legislation, which was to protect the public from unqualified renovators.[133]

In keeping with developments in other common-law jurisdictions, the Canadian courts have recently indicated that illegality is not an absolute bar to a claim for quantum meruit.[134] The claim may succeed if the plaintiff can show that allowing it would not undermine the integrity of the legal system. Whether this kind of argument will succeed in cases involving unlicensed builders or non-compliance with statutory formalities, remains to be seen.

4 4 5 Germany

It will be recalled that the consequences of an illegal transaction in Germany are mainly governed by three paragraphs in the BGB, namely § 134, § 138 and § 817(2). Where the provision of services is concerned, § 134 BGB is the likelier provision to be engaged, since the source of the illegality will be a statute regulating the particular industry. The first question will therefore be whether the relevant statute is a *Verbotsgesetz* or an *Ordnungsvorschrift*. If it is the latter, the illegality will have no

[131] [1958] O.R. 104.
[132] 1995 CarswellOnt 463.
[133] 463 para 99.
[134] *Kim v Choi* 2020 BCCA 98 para 47-50; *Lindsay v Ambrosi* 2019 BCCA 442 para 48.

impact on the validity of the contract. If it is the former, the contract will be void in terms of § 134 BGB, unless the purpose of the statute leads to a different conclusion. Finally, if the contract is void due to § 134 BGB but has been partially performed, a party may recover the value of any benefits they transferred with an enrichment claim, subject to the operation of § 817(2) BGB. In other words, if the claimant is equally tainted by the illegality, their enrichment claim will be barred.

It is hard to generalise in this context. Service-provision contracts that infringe legal rules will be valid in some cases and invalid in others.[135] Instead, the focus will be on the problem of *Schwarzarbeit*, an issue that has plagued the German courts for many years.[136] This area is interesting because there has been considerable development in German judicial thinking around the issue in recent years.

The paradigm case of *Schwarzarbeit* consists of an arrangement whereby a contractor agrees with a client to perform work without issuing an invoice.[137] These agreements are typically concluded orally and payment is made in cash. The contract price is therefore likely to be significantly lower since it does not include VAT. This means that, among other evils, the practice defrauds the revenue service and harms other contractors who operate legally, since they cannot compete with the artificially low prices.

The first relevant case on this issue is a decision of the BGH from 1990.[138] In this case, the claimant's husband had performed work for the defendant. The parties both knew that he was not registered in the Skilled Labour Register and that their contract was accordingly illegal because it amounted to *Schwarzarbeit*. The contractor also did not pay tax on the transaction. The defendant only paid a portion of the contract price. The claimant, who had taken cession of her husband's claim, then sought to recover the outstanding balance from the defendant.

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[135] In contrast to some of the other jurisdictions considered in this chapter, contracts with unregistered craftsmen (*Handwerker)*, are not void in Germany since the applicable legislation is classified as an *Ordnungsvorschrift*; BGH NJW 1984, 230. However, this is only to the extent that the contract does not amount to *Schwarzarbeit*.

[136] This fact pattern does not appear to have come before a South African court yet. However, see for Scotland *Cherrie v Vaughan* 2021 WL 01178110 and for England *Taylor v Bhail* [1996] CLC 377.

[137] The notion of *Schwarzarbeit* is defined in § 1 II of the Act to Combat Clandestine Employment (*Gesetz zur Bekämpfung der Schwarzarbeit*) 01 08 2004 ("ScwharzArbG") as undeclared work with one or more of the following features: failure to comply with duties prescribed by social security legislation arising from the work, failure to fulfil tax obligations arising from the work, receiving social security benefits without reporting their income arising from the work to their benefits provider, failure to register as an independent business or performing specialised work for which a licence is required without having obtained one.

[138] BGHZ 111, 308.

The BGH accepted as a starting point that the claimant had no effective contractual claim. In terms of the SchwarzArbG the contract was prohibited, which meant that it was void due to § 134 BGB. It also accepted that an enrichment claim would in principle be defeated by § 817(2) BGB, since the claimant knowingly entered into the illegal transaction. However, the court held that it would be irreconcilable with the standard of good faith contained in § 242 BGB if the defendant were allowed to keep that which he had received unlawfully without having to pay for it. The purpose of the ScwharzArbG was to deter illegal work. It was held that that this purpose was given sufficient effect by the risk of criminal sanction and the exclusion of contractual claims. However, it should not extend to enrichment claims as well. In other words, the BGH thought it unfair for the client to be left with a windfall. It could therefore achieve the result it desired with an appeal to § 242 BGB. In another *Schwarzarbeit* case decided in 2008, the BGH applied similar reasoning to allow an employer to exercise its warranty rights against the contractor despite the illegality.[139]

Then, in 2013, the BGH signalled a change in its attitude. Unlike the previous case where the court allowed the warranty claim of the employer on the basis of good faith, the BGH now found that the employer's warranty claim could not be enforced.[140] The reason was that amendments made to the SchwarzArbG in 2004 required that the statute be interpreted more strictly than the previous version.[141] Accordingly, the position was now that a contract will be void due to § 134 BGB if the contractor intentionally infringes the SchwarzArbG, the employer is aware of it and knowingly takes advantage of that fact.[142] This case dealt only with the position of the employer, so there was now some uncertainty about the position of the contractor.

A year later, the BGH had occasion to consider the status of the contractor's claim.[143] The claimant in that case was an electrician who undertook work on the property of the defendant. Although a written agreement was signed for the majority of the work, the parties had also orally agreed that an additional amount would be payable in cash, without an invoice. The claimant fully performed their end of the contract, but the defendant only paid a part of the agreed contract price. The claimant

[139] BGHZ 176, 198.
[140] BGHZ 198, 141.
[141] The 2008 case concerned an agreement made before the 2004 amendment to the SchwarzArbG came into effect.
[142] BGHZ 198, 141 para 13.
[143] BGHZ 201, 1.

therefore sought to recover the remainder of the price.

Even though only a part of the payment was agreed to without an invoice, the BGH held that the illegality tainted the entire transaction. Like the employer, the claimant could therefore not sue on the contract. The BGH then proceeded to find that the new version of the SchwarzArbG required that the claimant's enrichment claim be barred by § 817(2) BGB. It reasoned as follows:

> "The view taken by the BGH in its decision of 31 May 1990 … should not be followed. It contradicts the wording of the statute, which aims to exclude the enrichment claim. Anyone who deliberately violates a Verbotsgesetz deserves no protection from the consequences of that violation. Rather, granting protection would unreasonably favour such a person. The interests of the parties or considerations of fairness does not take precedence over this general preventative effect [of the statute]."[144]

Then in 2015, the BGH also refused the enrichment claim of a client who attempted to recover money he had paid to a contractor.[145] In this case the claimant sought to recover money that had been paid to a contractor as compensation in terms of a *Schwarzarbeit* agreement. If the contractor's enrichment claim was unavailable, it followed that the enrichment claim of the client would also fail for the same reasons. The legal position on *Schwarzarbeit* has therefore undergone a full reversal. Parties who knowingly enter into a *Schwarzarbeit* agreement, whether as a contractor or a client, have no remedy at their disposal. The contractor cannot recover anything from the client and the client cannot claim compensation for any damages resulting from defective work or recover any money that has already been paid to the contractor.

Two underlying justifications for this position can be discerned from the reasoning of the BGH in these cases. The first is known as the *Rechtschutzverweigerungstheorie*. The idea is that a person that steps outside the legal order deserves no protection from it.[146] This is said to justify the denial of the enrichment claims where the parties are both tainted by illegality.[147] The second is the

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[144] BGHZ 201, 1 para 8 (own translation). The original text reads: "Der vom Bundesgerichtshof in seiner Entscheidung vom 31. Mai 1990… vertretenen Auffassung … sei nicht zu folgen. Sie widerspreche dem Wortlaut des Gesetzes, das gerade auf den Verlust des Bereicherungsanspruchs abziele. Wer bewusst gegen ein Verbotsgesetz verstoße, verdiene keinen Schutz vor den Folgen des Verstoßes, sondern würde durch einen solchen Schutz gerade unbillig begünstigt. Gegenüber dieser generalpräventiven Wirkung hätten Parteiinteressen oder Billigkeitserwägungen keinen Vorrang."

[145] BGHZ 206, 69. See also BGH NJW 2017, 1808.

[146] See 3 2 4 above.

[147] L Klöhn "Die Kondiktionssperre gem. § 817 S. 2 BGB beim beidseitigen Gesetzes- und Sittenverstoß: Ein Beitrag zur Steuerungsfunktion des Privatrechts" (2010) 210 *AcP* 804 816; but see the criticism of this theory in H J van Kooten "Illegality and Restitution as a Matter of Policy Considerations: A Comparative Analysis of Dutch, English and German Law" (2001) 9 *RLR* 67 68-69.

idea that § 817(2) BGB has a deterrent effect.[148] In other words, excluding the enrichment claim of any party who knowingly participated in a *Schwarzarbeit* arrangement supports the aim of the SchwarzArbG, which is to deter and prevent these kind of arrangements.

4 4 6 Comparison

In every jurisdiction considered in this section we can observe that illegality tends to defeat claims based on construction contracts. That is understandable since the contracts in question are either expressly or impliedly prohibited by the applicable legislation. Accordingly, the concern not to undermine the intention of the legislature will invariably be important.

For example, in *Cool Ideas* the decisive consideration in the eyes of the court was that enforcing the arbitration award would undermine the purpose of the statute. This took precedence over considerations such as the fact that the legislation was not intentionally infringed, the builder had performed to a greater extent than the client and that the result would bear quite harshly on the builder.

In cases like *Pavey* and *Strongman* on the other hand, the courts displayed a greater concern to avoid a situation where the client receives an undeserved windfall. One hastens to add that the court in *Pavey* also took the view that the BLA could be interpreted in such a way that its aims were not undermined by awarding a quantum meruit.[149] Somewhat disappointingly, the court in *Strongman* did not engage very deeply with the question of how awarding damages in that case did not undermine the purpose of the regulations. Instead, the focal point of the court was the state of mind of the builder. That is, the builder was an innocent party who thought the work it performed was legal.[150]

A further distinction worth emphasising is the one drawn by the court in *Morgan.* When evaluating the viability of an unpaid builder's enrichment claim, different considerations may apply depending on the seriousness of the illegality. Rendering building services without a licence seems to be a more serious transgression than

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[148] B Häcker "Illegality and Immorality from a Civilian Angle" in S Green & A Bogg (eds) *Illegality after* Patel v Mirza (2018) 331 364.

[149] Birks (2000) *Theoretical Inq L* 182-183.

[150] It is noteworthy that the builder in *Cool Ideas* was also under the impression that it was acting lawfully and when it discovered that it was not, it took steps to comply with the statutory requirements. In fact, this consideration persuaded the High Court to find in favour of the builder; *Hubbard v Cool Ideas 1186 CC* 2013 5 SA 112 (SCA) para 8.

entering into an oral agreement with a contract where the applicable statute imposes formal requirements for that particular transaction. It is on this basis that *Morgan*, where the contractor's enrichment claim failed, may be distinguished from *Pavey*, where the claim succeeded.

In these contractor cases, as in the case of illegal loans, considerations of fairness are most potent where there is a risk that the illegality will leave one of the parties with an undeserved windfall, thus resulting in a harsh outcome for the losing party. This is especially so in cases like *Cool Ideas* and *Strongman*, where the contractor did not intentionally violate the law. German law could potentially contain this risk with § 242 BGB, as the BGH did in the 1990 case dealing with *Schwarzarbeit*. However, in that case the BGH was also satisfied that the purpose of the statutory prohibition would be given adequate effect by only excluding the contractual claim. Over time the court changed its view on the matter – a reversal that has garnered academic approval.[151] Now contractual and enrichment claims are unavailable in *Schwarzarbeit* matters where the claimant knowingly infringed the SchwarzArbG. The BGH has indicated that it remains possible in principle for § 242 BGB to override this position, but only in a very narrow set of circumstances.[152]

A final consideration that could be important in contractor cases, is the quantum of the claim under consideration. The quantum for an enrichment claim may be significantly lower than the contract price the parties had agreed to, depending on the circumstances. If the quantum is indeed lower, it may be arguable that the legislative prohibition could still be given sufficient effect despite allowing the claim. This could also be the case if any profit the contractor stood to make from the transaction is excluded from the quantum.[153]

4 5 Conclusion

The purpose of this chapter was to investigate and compare the policy factors that different jurisdictions take into account when determining the impact of illegality in three particularly difficult fact-patterns.

[151] J Stamm "Kehrtwende des BGH bei der Bekämpfung der Schwarzarbeit" (2014) *NJW* 2145; MüKo § 134 para 83.
[152] BGHZ 198, 141 para 30.
[153] See further 5 2 3 5 below.

In all three fact-patterns there were similar considerations that determined the outcomes in the cases. The question of whether the purpose of the infringed rule will be undermined by awarding the claim is always a relevant consideration where illegality is involved. Indeed, it is often decisive.

Another important consideration is the state of mind of the parties, in particular whether the claimant knowingly infringed the law or not. It may be preferable to allow an innocent party, whether a lender or a builder, to recover the value of benefits conferred under a tainted contract if that party unintentionally infringed the law.

Unfortunately, the consideration of a party's innocence will not always be regarded as a sufficient justification for allowing a claim. Courts rarely award a claim that indirectly enforces an illegal contract if doing so would undermine the integrity of the legal system, no matter how compelling the individual circumstances may be.

Another factor that may justify a claim for restitution is the extent to which the contract has been performed. Some courts express this factor as the need to avoid one party being allowed to obtain a windfall at the expense of the other. Thus, where one party has fully performed first, it may be particularly unpalatable to allow the other party to retain that performance without having to provide anything in return.

Finally, in the case of illegal employment, an important factor is the vulnerability of the employee. Many employees who work illegally are in precarious positions and thus vulnerable to exploitation by the employers. In these cases, awarding some form of compensation to the employee may be necessary to avoid an even greater evil.

The next chapter will conclude the thesis by setting out several normative propositions about how illegality in the law of contract should be dealt with and making some recommendations about how South African law may be reformed in light of those propositions.

CHAPTER 5: CONCLUSION

5 1 Introduction

The aim of this study is to investigate the determinants of the consequences of illegality in the law of contract. This chapter synthesises the findings of the previous chapters in order to develop a proposal for how the consequences of contractual illegality should best be determined. Following that, some recommendations are made on how this area of the law may be improved in South Africa.

5 2 Determining the consequences of illegal contracts: a suggested approach

5 2 1 The problem of accurate description

Any attempt to analyse the consequences of illegality in contract law immediately encounters a problem: how to describe those consequences in clear terms. Many of the authorities dealing with illegality use confusing language, which in turn makes subsequent analysis more difficult. Several pitfalls that should be avoided have been identified in this study.

The terms ‘void’ and ‘unenforceable’ should be used with care. Not only may their respective meanings differ depending on the jurisdiction, but they may also be associated with certain assumptions about whether restitution of benefits conferred under the failed contract is in principle available or not.[1] For example, in South Africa and Germany, describing a transaction as void (or *nichtig* in German) implies that any transfer under the failed contract had no legal basis. This is because these systems follow a so-called ‘absence of basis’ approach to enrichment liability. In other words, one of the requirements for a claim in unjustified enrichment is that the enrichment must be *sine causa*.[2] A contract described as ‘void’ in South African law therefore implies that restitution for any benefits that have been transferred is available in principle, subject to the other requirements for enrichment liability being met.[3] Conversely, where the contract is described as ‘merely unenforceable’, an enrichment claim is necessarily unavailable since there is still a legal basis for any transfer that

1 3 7 above. See also S Meier “Illegality” in N Jansen & R Zimmermann (eds) *Commentaries on European Contract Laws* (2018) 1910.
2 2 4 above.
3 2 6 above.

has been made.[4]

However, the term 'unenforceable' does not carry the same meaning in Scotland.[5] It relates only to the availability of a contractual claim, even though Scotland also follows an 'absence of basis' approach to enrichment liability.[6] An enrichment claim may nevertheless be available even if the contract is described as 'unenforceable' due to illegality. The Scottish position is arguably best understood as being a result of English influence. The effects of illegality on a contract have been described by English courts with a variety of terms, such as 'void', 'unenforceable' or 'voidable', but these terms have not been clearly distinguished from each other in the context of illegality.[7] Nevertheless, it seems that the preferred term in English law is also 'unenforceable.'[8] It also appears to be meant in the same sense as in Scots law. In other words, a contract described as unenforceable in English law is not considered an obstacle to the availability of an enrichment claim, otherwise the claimant in *Patel v Mirza* ("*Patel*") could not have succeeded.[9] The explanation for this might be that English law follows an 'unjust factor' approach to enrichment liability.[10] This means that it is less important to spell out the status of the underlying contract because the focus is instead on identifying a factor that justifies restitution.

Arguably the best way to avoid confusion with terminology is to adopt the approach of New Zealand and certain international model instruments, such as the Principles of European Contract Law.[11] A contract that infringes a rule is declared 'of no effect' or 'legally ineffective' as a point of departure, following which the rest of the consequences which are appropriate for the circumstances can be worked out. The advantage of this approach is that it separates the inquiry into the existence of illegality from the inquiry into the consequences of illegality.[12]

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4 *Cool Ideas 1186 CC v Hubbard* 2014 4 SA 474 (CC) para 49.
5 See 3 4 4 above.
6 *Shilliday v Smith* 1998 S.C. 725 727.
7 A Burrows "A New Dawn for the Law of Illegality" in S Green & A Bogg (eds) *Illegality after Patel v Mirza* (2018) 23 25.
8 J Beatson, A Burrows & J Cartwright *Anson's Law of Contract* (2020) 410.
9 [2016] UKSC 42; B Häcker "Illegality and Immorality from a Civilian Angle" in S Green & A Bogg (eds) *Illegality after* Patel v Mirza (2018) 331 336.
10 G Virgo *The Principles of the Law of Restitution* 3 ed (2015) 120.
11 See 3 5 - 3 6 above.
12 A failure to do this results in the kind of confusion encountered in *Dowling & Rutter v Abacus Frozen Foods Ltd* 2002 SLT 491, discussed above at 3 4 3.

5 2 2 The nature of an illegality analysis

Once it has been established that a contract has been tainted by illegality, one of two issues usually arise. The first is the enforceability question, i.e. whether the illegality means that the contract may not be enforced. The second, which we may call the restitution question, is whether any benefits that have been transferred under the illegal contract may be recovered. A key proposition advanced in this thesis is that determining the consequences of illegality, that is, answering these two questions, is essentially an exercise in balancing various policy considerations.[13] Building on this proposition, it is contended here that this is the nature of an illegality analysis irrespective of whether the dispute is concerned with statutory illegality or common-law illegality.

Most jurisdictions draw a distinction between statutory illegality and common-law illegality, but the distinction does not have the same meaning everywhere. In South Africa for example, the distinction refers to the source of the illegality.[14] In other words, if the contract infringes legislation the illegality is said to be statutory whereas any other defect in legality, such as a contract concluded with an unlawful purpose, is said to result from the common law.[15] In English law on the other hand, the reference is to the effect of the illegality on the contract rather than the source.[16] It has been argued that this version of the distinction does little to illuminate matters, because it is applied inconsistently by the courts.[17] In fact, as has been shown in the English cases dealing with work by undocumented migrants, the effect is often quite the opposite.[18]

Drawing the distinction between statutory illegality and common-law illegality, in whichever sense, is ultimately less helpful than it seems because the analysis in both kinds of illegality amounts to the same exercise in practice.[19] Various competing policy factors must be weighed and depending on the circumstances, some will be given effect to above others. Where specific legislation is involved, interpreting the text of

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13 2 3 above.
14 2 1, 3 2 2 – 3 2 3 above.
15 A similar distinction is drawn in German law. § 134 BGB deals with transactions that infringe legislation whereas § 138 BGB applies to transactions that infringe public morals.
16 3 3 2 above.
17 3 3 2 above.
18 4 3 3 above.
19 H MacQueen & A Cockrell "Illegal Contracts" in R Zimmermann, D Visser & K Reid (eds) *Mixed Legal Systems in Comparative Perspective: Property and Obligations in Scotland and South Africa (*2004) 143 172 suggest that the distinction "is of little value" and "should be discarded." In *Okedina v Chikale* [2019] I.C.R. 1635 para 58 the court described the distinction as being "in truth largely at the level of theory, since the same underlying principles are involved."

the relevant provisions will naturally play a central role in the determination of that dispute. But other than in the rare cases where the statute fully describes the consequences that should follow, other factors will invariably also have to be taken into account.

5 2 3 Factors determinative of the consequences of illegality

5 2 3 1 Introduction

Factors that potentially determine the consequences of illegality have been identified throughout the preceding chapters of the study. What remains to be done is explain in more detail how these factors function in the analysis. All the factors which follow will not necessarily be relevant in every case and they may at times overlap. However, it is suggested that any outcome of a case where the consequences of illegality had to be determined may be explained with reference to some or all of these factors.[20]

5 2 3 2 Purpose of the infringed rule

The starting point of an illegality analysis is almost always an inquiry into the purpose of the rule that has been infringed.[21] The rule may be non-statutory, such as the rule that contracts aimed at defrauding creditors may not be enforced.[22] Alternatively, the rule will be sourced in legislation. If that is the case, the rule will typically form part of a broader attempt by the legislature to achieve a certain goal.

One of the most common statutory goals is the protection of consumers. For example, in cases dealing with building contracts tainted by illegality, the purpose of protecting consumers is a central concern.[23] A court will normally decline to enforce these kinds of contracts if doing so would undermine the purpose that the applicable statute aims to achieve. If a licence requirement is imposed by a statute, then enforcing

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[20] Many of the factors that follow bear a close resemblance to those listed in art 15:102(3) PECL and art 3.3.1(3) PICC. These instruments also list some additional factors that are not included below. The reason is that these additional factors either play a less important role in the determination or because they overlap so significantly with the factors considered below that their individual treatment is unnecessary.

[21] *Swart v Smuts* 1971 1 SA 819 (A) 830A-B; § 134 BGB; *Patel v Mirza* para 120; Meier "Illegality" in *Commentaries* 1911.

[22] *Maseko v Maseko* 1992 3 SA 190 (W). The purpose of such a rule is to prevent a debtor from circumventing debt-collection procedures. It follows that any contract aimed at concealing assets from creditors will not enforced by a court.

[23] *Cool Ideas 1186 CC v Hubbard* 2014 4 SA 474 (CC) para 49; *Jamieson v Watt's Trustees* 1950 S.C. 265 278; *Pavey & Matthews v Paul* (1987) 162 C.L.R. 221; *Kocotis v D'Angelo* [1958] O.R. 104.

a contract with an unlicensed builder may undermine the purpose of consumer protection. The risk of criminal liability for not obtaining a licence may not be sufficient to deter unqualified builders from offering their services to members of the public if they knew that they were entitled to receive payment for the work they performed.

The inquiry into the purpose of the rule may also yield a converse result. A court may find that the illegal conduct in question did not in fact undermine the applicable statutory rule. Such a finding formed one of the justifications for the result in *Pavey & Matthews v Paul* ("*Pavey*").[24] The court concluded that the protective scope of the relevant legislation did not extend to the kind of consumer who requests and accepts building work but then refuses to pay because statutory formalities had not been complied with.[25] Accordingly, the purpose which the legislature sought to achieve by imposing formalities was not undermined by allowing the builder an enrichment claim for the value that had been transferred to the consumer.

An inquiry into the purpose of the rule is the starting point for determining the consequences of illegality because it may well be wholly determinative of the outcome. In other words, if it can be established by the claimant that awarding the claim would not undermine the purpose of the rule, then the claim is likely to succeed. On the other hand, if the defendant manages to prove the converse, then other countervailing considerations would have to weigh very heavily for the claim to still succeed.

5 2 3 3 State of mind of the parties

Another important factor that will often feature is whether the parties knew that their conduct was illegal. Some prohibitions are in fact only engaged if the infringement has been intentional. The cases dealing with *Schwarzarbeit* in Germany provide a good example.[26] Remedies in contract and unjustified enrichment are only excluded in *Schwarzarbeit* arrangements if the parties were aware of the illegality. Thus, if a client accidentally employed a contractor without knowing that the contractor is not acting in compliance with the SchwarzArbG, the client would still be able to sue on the contract, but the contractor will not.

In other cases, the absence of an illegal intent may be favourable to a claimant

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[24] (1987) 162 C.L.R. 221. The other determinative factor was the extent to which the contract had been performed, see 5 2 3 5 below.

[25] (1987) 162 C.L.R. 221 229; P Birks "Recovering Value Transferred under an Illegal Contract" (2000) 1 *Theoretical Inq L* 155 182-183.

[26] See 4 4 5 above.

seeking either enforcement or restitution. In *Strongman (1945) Ltd v Sincock* the court enforced a collateral contract which achieved the same outcome in substance as enforcing the original contract would have.[27] Arguably the most important factor that justified this result in the eyes of the court was the fact that the plaintiff was unaware of the illegality when the work was being performed. Similarly, in *Okedina v Chikale* one of the two reasons the claimant succeeded was because she was unaware that she had been working illegally.[28]

An innocent state of mind will not always save the claimant's case. Where a prohibition is clearly set out in a statute, the ignorance of the claimant is unlikely to be regarded as sufficiently important to justify awarding the claim. This is evident from the English cases dealing with consumer loans.[29] The court could do no more than express its dissatisfaction at the result that lenders who had inadvertently not complied with the relevant credit legislation could not recover any money they had paid over.

5 2 3 4 Seriousness of the infringement

The seriousness of the infringement is another factor that may be helpful for determining the consequences of the illegality.[30] A less serious infringement of the law is often used as a justification for providing some form of relief. We have seen that this is the most common justification in South African law for regarding some illegal contracts are void and others as valid but unenforceable. The argument is that voidness as a consequence should be reserved for more serious infringements of the law, whereas for less serious infringements the contract may remain valid, although it still cannot be enforced.[31]

The factor also features in the distinction in German law between an *Ordnungsvorschrift* and a *Verbotsgesetz*.[32] A contract that infringes an *Ordnungsvorschrift* is not invalid, because the illegality is not considered sufficiently serious to justify such a result. Conversely, a contract infringing a *Verbotsgesetz* will

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27 [1955] 2 Q.B. 525; discussed at 4 4 2 above. A claim on these facts would probably have failed in South Africa; see *Gibson v Van der Walt* 1952 1 SA 262 (A), discussed at 2 7 above.

28 [2019] I.C.R. 1635. The other reason was that the statutory prohibition was directed only at the employer.

29 4 2 2 2 above.

30 Art 15:102(3)(d) PECL; PICC 3.3.1(d).

31 However, it has been argued in this thesis that the justification is not particularly convincing since a finding of valid but unenforceable may end up generating a harsher result if it defeats an enrichment claim that would otherwise have succeeded; 2 3 above.

32 3 2 2 above.

usually be void.[33]

A final example is the reasoning in *688558 Ontario Ltd v Morgan*.[34] In that case the court regarded the performance of building work without a licence as too serious an infringement of the law to permit the builder's enrichment claim to succeed.[35] By contrast, since non-compliance with statutory formalities is a less serious infringement of the law, an enrichment claim could succeed in cases like *C. Battison & Sons Inc. v Mauti*[36] and *Pavey*.

5 2 3 5 Extent to which contract has been performed

When determining the restitution question, one of the most important considerations is the extent to which the contract has been performed. Other things being equal, the greater the disparity in the performances rendered between the parties, the more pressing the need to grant restitution may become.[37] This is because it is generally considered undesirable for one party to be left with an undeserved windfall or as it were, unjustly enriched at the expense of the other.[38]

The fact-pattern that illustrates the point most clearly is the case of an illegal consumer loan.[39] The nature of a loan agreement means that a lender must always perform first. If it turns out that the applicable credit legislation was not complied with, it would typically be quite unsatisfactory if the borrower who repaid little or nothing could retain the capital in cases where the infringement was not intentional.[40] On the other hand, allowing the lender to recover the money in such a case may subvert the purpose of the infringed rule, because the result would be similar to enforcing the illegal agreement.

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33 Unless it can be shown in terms of § 134 BGB that the statute in question demands a different result.

34 1995 CarswellOnt 463; discussed at 4 4 4 above.

35 That is not to say that performing work without a licence will always be too serious for an enrichment claim to be awarded. For example, it has been argued that the builder in *Cool Ideas 1186 CC v Hubbard* 2014 4 SA 474 (CC) would have been entitled to an enrichment claim notwithstanding the fact that it operated without a licence; 2 6 above.

36 1986 CarswellOnt 649.

37 Conversely, it might be argued that if both parties have fully performed, then neither has been enriched at the expense of the other so there is no reason for the court to order restitution. However, this view is less persuasive if the contract is prohibited, because not unwinding the transaction might then have the effect of undermining the purpose of the prohibition; *Afrisure CC v Watson NO* 2009 2 SA 127 (SCA) para 46-50; *Legator McKenna Inc v Shea* 2010 1 SA 35 (SCA) para 28-29; J Du Plessis *The South African Law* of *Unjustified Enrichment* (2012) 209-212.

38 *Klokow v Sullivan* 2006 1 SA 259 (SCA) para 18; *Pavey & Matthews v Paul* (1987) 162 C.L.R. 221*; Strongman (1945) Ltd v Sincock* [1955] 2 Q.B. 525; *Tsoi v Lai* 2012 BCSC 1082 para 20.

39 4 2 above.

40 RGZ 161, 52; *Orakpo v Manson Investments Ltd* [1977] 3 All ER 1 8; *Wilson v First County Trust Ltd* [2004] 1 A.C. 816 para 72-73.

Stuck between Scylla and Charybdis, it has been suggested above that the court's best escape from the problem is to allow the lender to reclaim the capital but forfeit any interest that would have been due.[41] This gives some effect to the statutory rule because the lender would earn no profit from the transaction while also avoiding a situation where the borrower is unjustly enriched.

The idea of excluding profit from the quantification of an enrichment claim may also make the remedy more attractive in other illegality cases where there is a similar risk of indirect enforcement. For example, in Chapter 2 it was argued that awarding an enrichment claim in *Cool Ideas 1186 CC v Hubbard* ("*Cool Ideas"*) that excluded the builder's profit would have been a more satisfactory outcome to the case.[42]

However, excluding profit is not a one-size-fits-all-solution. In some cases, it may be quite difficult to quantify the plaintiff's profit. For example, if the performance consisted purely of a service, then the only option may be to estimate the profit with reference to the prevailing margins in the particular industry.[43]

5 2 3 6 Vulnerability

In some cases, the vulnerability of one of the parties may help persuade the court to award a claim despite the illegality of the contract.[44] This factor is particularly notable in cases dealing with illegal employment.[45] Courts across jurisdictions have come to recognise that employees who work illegally are often in vulnerable positions and susceptible to being exploited by their employers.[46] Awarding a remedy on the basis of an illegal employment contract does indeed subvert the purpose of the governing legislation to some degree. However, in view of the vulnerability of this particular class, this outcome is regarded as preferable to a result where employers are left free to exploit their illegal employees with impunity.

5 2 3 7 Proportionality

Courts in several jurisdictions have identified the need for achieving outcomes that are proportional to the infringement as a relevant consideration in cases involving

41 4 2 4 above.
42 2014 4 SA 474 (CC); 2 6 above.
43 Virgo *Restitution* 98-99.
44 It may also justify an application of the *par delictum* rule in South Africa rather than its relaxation; *Jordan v Penmill Investments CC* 1991 2 SA 430 (E) 440.
45 4 3 above.
46 *Kylie v CCMA* 2010 4 SA 383 (LAC) para 44; *Hounga v Allen* [2014] UKSC 47 para 52; *Nizamuddowlah v Bengal Cabaret Inc* (1977) 399 NYS 2d 854.

illegality.[47] Yet, proportionality is the kind of notion that is easy to recognise but difficult to define.[48] One intuitive expression of the idea is to say that one should not use a sledgehammer to crack a nut.[49] This means, for example, that it would be disproportionate for one party to be left with a large and undeserved windfall if the claim for restitution is denied in a case where the illegal conduct of the claimant was relatively trivial. While the notion of proportionality carries considerable persuasive force in illegality cases, it is not clear that it operates on the same level of abstraction as the other factors considered above. Rather, it seems to function more like an overarching standard than a factor *per se*.[50] One might therefore rather say that it is desirable that the other factors are balanced in such a way that the court's decision is a proportionate response to the illegality.

5 2 3 8 Preserving the integrity of the legal system

In English[51] and Canadian[52] jurisprudence reference is often made to the need to preserve the integrity of the legal system. The idea is that where one area of the law prohibits certain conduct, it is undesirable for another area of the law to tolerate that conduct.[53] This factor is said to explain the cases dealing with illegality where an enrichment claim is refused. If the law of contract prohibited the conduct, then it would lead to inconsistency if the law of unjustified enrichment could be used to achieve the same or a similar result than the one that had been contemplated in the contract.

However, it is questionable how useful this factor is in practice.[54] The reason is that it is difficult to distinguish this factor from the factor of considering the purpose of the prohibition.[55] Harm to the integrity of the legal system is the consequence of

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47 *Standard Bank v Estate van Rhyn* 1925 AD 266 274; *Patel v Mirza* [2016] UKSC 42 para 120; *Kim v Choi* 2020 BCCA 98 para 64; *Ochroid Trading Ltd v Chua Siok Lui* [2018] SGCA 5 para 176. See also art 15:102(3) PECL.

48 See the attempt by ZX Tan "The Proportionality Puzzle in Contract Law: A Challenge for Private Law Theory?" *Can J Law Jurisprud* 33 (2020) 215 217-225

49 C Hoexter *Administrative Law in South Africa* 2 ed (2012) 344. For a comparison of the role played by proportionality in private law and public law, see E Lim & FJ Urbina "Understanding Proportionality in the Illegality Defence" (2020) 136 *LQR* 575.

50 *Ting Siew May v Boon Lay Choo* [2014] 3 SLR 609 para 68.

51 *Patel v Mirza* [2016] UKSC 42 para 99; *Hounga v Allen* [2014] UKSC 47 para 44.

52 *Kim v Choi* 2020 BCCA 98 para 47-50. *Hall v Hebert* [1993] 2 SCR 159.

53 An analogous idea is the suggestion that the law should not 'stultify' or make nonsense of itself; Birks (2000) *Theoretical Inq L* 155.

54 For example, A Burrows *Restatement of the English Law of Contract* (2016) 230 argues that the term 'inconsistency' is ambiguous and could justify any result.

55 See the formulations in *Kim v Choi* 2020 BCCA 98 para 63 and *Patel v Mirza* [2016] UKSC 42 para 120.

undermining the purpose of the prohibition. It provides an explanation for why the purpose should not be undermined, rather than constituting a self-standing factor. In other words, an inquiry into stultification, or preserving the integrity of the legal system, may amount to only being code for considering the purpose of the prohibition.

5 2 3 9 Penalties and deterrence

Finally, two interrelated factors said to be of importance in an illegality analysis are the penalty imposed by the statute and the need for illegal activity to be deterred.[56] The penalty required by a statute is less useful than it appears to be at first glance. The reason is that the existence of a penalty may justify a conclusion in either direction.[57] On the one hand, it could be argued that by imposing a penalty, the legislature wished to signal its disapproval of the conduct and therefore intended to invalidate the contract too.[58] Conversely, it might also be argued that the legislature considered the penalty a sufficient sanction for the illegality and did not mean to invalidate the transaction as well.[59]

Although the idea that illegal conduct should be deterred is unobjectionable, this factor is also not particularly helpful on its own. The deterrent value of denying a claim for enforcement is likely to be considered as part of the court's inquiry into the purpose of the infringed rule already. Moreover, with regard to the restitution question, it is questionable whether denying restitution to a plaintiff tainted by illegality really serves the goal of deterrence.[60] The BGH in Germany did indeed rely heavily on the rationale of deterrence when it decided that enrichment claims were no longer allowed in cases of *Schwarzarbeit*.[61] However, in those cases the justification may have carried more weight because the prohibition on *Schwarzarbeit* only operates in cases where the infringement is intentional. As a general proposition it is more difficult to justify a denial of restitution on the basis of deterrence, because the argument depends on a number of assumptions, for example that the plaintiff is aware of the illegality and the *par delictum* rule or its functional equivalents.[62]

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56 Meier "Illegality" in *Commentaries* 1912.
57 J du Plessis "Some Thoughts on the Consequences of Illegal Contracts" (2021) *Acta Juridica* 177 186
58 St John Shipping Corporation v Joseph Rank Ltd [1957] 1 QB 267 288.
59 *Wierda Road West Properties (Pt) Ltd v Sizwe Ntsaluba Gbodo Inc* 2018 3 SA 95 (SCA) para 20.
60 Virgo *Restitution* 714; HJ van Kooten "Illegality and Restitution as a Matter of Policy Considerations: A Comparative Analysis of Dutch, English and German Law" (2001) 9 *RLR* 67 69-70.
61 BGHZ 206, 69 para 17; 4 4 5 above.
62 Virgo *Restitution* 714.

5 2 4 The case for a discretionary approach

Having examined the most important considerations for determining the consequences of illegality, the final question to be answered is what method is best for giving effect to them. In Chapter 3 it was shown that there are a variety of ways in which to approach illegality. It was also argued that these approaches lie on a spectrum of rule-based approaches on the one end and discretionary approaches on the other.[63]

In a rule-based system such as Germany, the consequences of illegality are determined with reference to fixed rules.[64] Typically these rules provide that a) an illegal contract may not be enforced and b) restitution of any benefits conferred under the illegal contract may only be obtained if the claimant was not a willing and equal participant in the illegality. Although these rules are strictly applied, over time several exceptions inevitably develop in order to avoid manifestly unjust outcomes. The advantage of a rule-based approach is supposedly that it brings about a greater degree of legal certainty.[65]

The best examples of discretionary approaches are found in New Zealand[66] and England[67] as well as international model instruments such as the PECL and PICC.[68] Under this kind of regime, the consequences of illegality are determined via a judicial discretion, which must be exercised with reference to a list of factors. The advantage of this approach is that it grants the court much more flexibility in resolving the dispute.

It is true, as a general proposition, that the law should have clear rules wherever possible. However, the contention here is that in the context of illegality this is impossible. This area of the law is simply too complex to allow for the formulation of rules that will have a high rate of delivering just outcomes while remaining user-friendly. The best available alternative appears to be to leave a discretion for judges to determine the consequences of illegality.[69]

Whenever a rule-based approach has been discarded in favour of a discretionary

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63 Some jurisdictions, such as South Africa and Scotland, lie in the middle of the spectrum since they contain both discretionary and rule-based elements in their respective approaches to illegality.

64 See 3 2 4 above.

65 J Gleim "*Patel v Mirza* und die Illegality-Doktrin im Vergleich zum deutschen Recht" (2018) 2 *ERPL* 227 244.

66 3 5 above.

67 3 3 4 above.

68 3 6 above.

69 See further MacQueen & Cockrell "Illegal Contracts" in *Mixed Legal Systems in Comparative Perspective* 166-167; Burrows "A New Dawn" in *Illegality after* Patel v Mirza 23-24.

one in the context of illegality, the most common objection is that the discretionary approach will generate such uncertainty.[70] This was the case when New Zealand passed its Illegal Contracts Act 129 of 1970[71] ("ICA") and most recently when the UK Supreme Court decided *Patel*.[72] While it is probably too early to assess the impact of *Patel* in this regard, it can be said with confidence that New Zealand's ICA did not generate an intolerable amount of uncertainty. The provisions of the ICA have stood virtually unchanged for half a century and all indications suggest that the statute functions well.[73] By contrast, the rule-based approach that prevailed in England before *Patel* has been the subject of sustained criticism.[74] In Germany, § 817(2) BGB is also regarded by many as deeply unsatisfactory.[75]

It should also be stressed that the discretion is not unfettered. The same kind of factors that underlie the approaches to illegality in rule-based regimes continue to play an important role in a discretionary approach. The only difference is that these factors must be considered more explicitly in exercising the discretion.

5 3 Proposals for reform in South Africa

It was argued in Chapter 2 that a considerable degree of uncertainty remains in South African law about some aspects of illegal contracts. In particular, it is unclear why the courts find illegal contracts void in some cases and valid but unenforceable in others.[76] A comparison with the law of Scotland revealed that the reason for this classification is probably historical. Describing the consequence of illegality as rendering a contract 'unenforceable' is a result of the influence that English law has exerted on both

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70 This kind of objection is often less forceful than its proponents would like it to be. As Bigwood and Dietrich suggest: "In short, in order to have genuinely persuasive force, arguments from uncertainty must credibly rise above the level of assertion or speculative fear on the part of those who advance them and be grounded instead in either experience or fully articulated reason." R Bigwood & J Dietrich "Uncertainty in Private Law: Rhetorical Device or Substantive Legal Argument?" (2021) 45 (Adv) *Melbourne Univ LR* 1 3. It is questionable whether the objection from uncertainty raised in the context of illegality meet these criteria.

71 MP Furmston "The Illegal Contracts Act 1970 – An English view" (1972) 5 *NZULR* 151.

72 See the dissents in *Patel v Mirza* [2016] UKSC 42 of Lord Sumption (para 263) and Lord Mance (para 206).

73 3 5 above.

74 3 3 3 above.

75 As Klöhn remarks: "No other norm causes more headaches in civil-law scholarship than § 817(2) BGB"; L Klöhn "Die Kondiktionssperre gem. § 817 S. 2 BGB beim Beidseitigen Gesetzes- und Sittenverstoß: Ein Beitrag zur Steuerungsfunktion des Privatrechts" (2010) 210 *AcP* 804 806; Häcker "Illegality and Immorality" in *Illegality after* Patel v Mirza 359; R Zimmermann *The Law of Obligations: Roman Foundations of the Civilian Tradition* (1996) 864. See further 3 2 4 above.

76 2 3 above.

jurisdictions.[77] History notwithstanding, it has been suggested that most of the justifications for characterising an illegal contract as valid but unenforceable are unconvincing. The view that it amounts to a less serious consequence than voidness does not hold for all cases, since a finding of validity but unenforceability excludes the availability of a claim in unjustified enrichment. This is because any enrichment arising from performance is regarded as being supported by a legal ground (*cum causa*).[78] In a case where an illegal contract has been partially performed, it is desirable to evaluate, with reference to the factors set out above, whether a duty of restitution should be imposed if one party has been enriched at the expense of the other.

One of the most important types of contracts regarded as valid but unenforceable are agreements in restraint of trade that are considered contrary to public policy. Describing these contracts as merely unenforceable has the advantage of keeping the contract valid so that it may perhaps be enforced at a later stage, when doing so would be appropriate. However, this construction again becomes unhelpful when it must be determined whether the covenantee may recover any money it paid in return for the restraint with an enrichment claim. In some case restitution might well be necessary, but that would require the court to ignore the *sine causa* requirement of enrichment liability if the contract is unenforceable as opposed to void. One can also imagine a scenario where the restraint is so oppressive that it could never be enforced. In such a case it may perhaps be more appropriate for the contract to be declared void. Instead of treating every restraint of trade agreement that is contrary to public policy as valid but unenforceable, the court should perhaps have a discretion to declare the agreement void in some cases and unenforceable in others. And if the question of enrichment liability arises and the contract has already been declared unenforceable, it may well be appropriate to nevertheless award the claim if that is what the relevant policy considerations demand.

In addition, reference to the *ex turpi* and *par delictum* maxims should be discontinued. As the comparative analysis has revealed, these maxims and their functional equivalents in other countries tend to confuse the issue.[79] The courts need not continue to insist that the *ex turpi* rule is inflexible, because it is plainly not true. The courts have always enforced illegal contracts in appropriate circumstances if an

[77] 3 7 above.
[78] 5 2 1 above.
[79] 2 11 above; Du Plessis (2021) *Acta Juridica* 193.

interpretation of the infringed legislation revealed that invalidation was not required. That is not to say that the policy underlying the *ex turpi* maxim is not important. It is rather to recognise that it is one of several important factors that must be considered. A better approach to the enforceability question would be for the court to exercise a discretion with reference to the factors that have been identified above. In most cases a contract that is strictly prohibited will still not be enforced, but whatever the result, it will be reached with transparent reasoning rather than a reliance on a misleading rule.

As for the *par delictum* rule, the decision in *Jajbhay v Cassim* was decades ahead of its time and remains good law.[80] The decision introduced necessary flexibility into the determination of whether an enrichment claim should be awarded despite the plaintiff's illegal conduct. However, reference to the *par delictum* rule is also unhelpful since it is not clear why a transfer should remain with the defendant by default simply because both parties are tainted by illegality. Rather than frame the issue as whether the *par delictum* rule should be relaxed, the court should just consider from the start whether the enrichment claim should be awarded despite the illegality, with reference to the factors that determine the consequences of illegality.[81]

5 4 Concluding remarks

The consequences of illegality in South African private law have received relatively limited academic attention outside of the standard textbooks since the advent of the constitutional era. It is hoped that this thesis will contribute to a better understanding of this complex area of the law.

Nevertheless, there is much that remains to be said of illegality in private law. This thesis has focused on illegal contracts, but there has recently been a renewal of academic interest in the common-law world on the role of illegality in tort law.[82] The impetus for this development is probably attributable to two cases recently decided by the UK Supreme Court.[83] The question of whether illegality may provide a defence to a delictual claim has not yet been considered by a South African court.[84] However, it

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80 1939 AD 537.

81 2 6 above; Du Plessis (2021) *Acta Juridica* 189.

82 See J O'Sullivan "Illegality and Tort in the Supreme Court" (2021) 80 *CLJ* 215; JC Fisher "*Gray* Areas in Tort: Illegality and Authority after *Patel v Mirza* (2021) 84 *MLR* 1122; L Shmilovits "When is Illegality a Defence to a Tort?" (2021) *LS* 1.

83 *Stoffel & Co v Grondona* [2020] UKSC 42; *Henderson v Dorset Healthcare University NHS Foundation Trust* [2020] UKSC 43.

84 Recently in *Minister of Police v Underwriters of Lloyds of London* 2021 ZASCA 72 para 14, the Supreme Court of Appeal deftly avoided the issue.

is conceivable that the same fact patterns that have led to developments in this area overseas may arise in South Africa one day. Whether South African law would benefit from recognising such a defence is therefore a promising area for future research.

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