

# **The legal nature of preference contracts**

Tjakkie Naudé

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Promoter: Prof GF Lubbe



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## **Declaration**

I, the undersigned, hereby declare that the work contained in this dissertation is my own original work and that I have not previously in its entirety or in part submitted it at any university for a degree.

Signature:

Date:.

## Summary

The various constructions of rights of pre-emption encountered in South African case law all have some merit. This is confirmed by the multiplicity of types of preference contracts encountered in German law especially. The tendency of South African courts and writers to portray one approach as the only correct one to the exclusion of all other views, results in tension and confusion, all the more because of the failure to investigate the relevant policy considerations comprehensively. The confusion is compounded by what amounts to a breakdown of the system of precedents with judgments being based on incorrect interpretations of previous decisions and with scant regard for contrary decisions.

No certainty exists regarding the construction of the contractual right of pre-emption in Roman and Roman-Dutch law, nor is it clear what figure or figures were received into South African law. The Germanic concept of tiered ownership that forms the historical basis for the *Oryx* remedy, does not form part of our law. This accounts for the difficulty that courts and writers have in explaining this remedy in terms of Romanist terminology, and the resort to the language of fiction.

German law and English law, relied upon in South African case law, do not support a uniform construction of all rights of pre-emption as creating an enforceable duty to make an offer upon manifestation of a desire to sell. The almost unanimous support of US courts for a remedy by which the holder can ultimately obtain performance of the main contract upon conclusion of a contract with a third party, challenges the hypothesis suggested by German law that the default construction of preference contracts should be the bare preference contract which only creates a negative obligation.

The very cryptic way in which rights of pre-emption are normally drafted, makes it difficult to even identify the main purpose of the parties. It is therefore not easy to classify preference contracts into the different types identified in this study as notional possibilities. A default regime is therefore highly desirable in the interest of legal

certainty. The choice of a default regime should be made on the basis of recognised policy considerations, particularly on the basis of an equitable balancing of typical parties' interests and in view of communal interests balanced against the demand for legal certainty. The choice of default regime cannot be based merely on historical authority or precedent (which is in any event unclear in the present context) or unsubstantiated claims that one model is more logical or commercially useful than another. When rules are chosen as the default regime, these rules must, as far as possible, be reconciled with the existing conceptual structure of our law to prevent contradictions and inconsistencies.

A policy analysis reveals that three default types of preference contract should be recognised, each with a clearly delineated field of application. Firstly, where the agreement allows the grantor to contract with a third party, the holder has the right to contract with the grantor at the terms agreed with the third party. Such a preference contract can therefore be regarded as an option conditional upon conclusion of a contract with a third party. Such contracts are rare in South Africa. In other cases, the default rule should be that the grantor must first give the holder an opportunity to contract before he contracts with a third party. The default construction of this latter type of preference contracts depends on whether the preference contract itself predetermines the main contract price. If so, the holder has a right or option to contract at that price upon any manifestation of a desire to conclude the relevant type of contract. However, where the preference contract does not predetermine the price, or refers to a price that the grantor would accept from third parties, any manifestation of a desire to sell should not be sufficient to trigger the holder's right. The grantor and society have an interest in having her freedom to negotiate with third parties to obtain the best possible price curtailed as little as possible. In such cases, the default rule should be that the holder is only entitled to conclusion of the main contract upon breach in the form of a contract with or offer to a third party. The default rule should also be that such preference contracts – which will be treated as ordinary preference contracts – only terminate upon the grantor actually contracting with and performing to a third party within a reasonable time after the holder declined the opportunity to match those terms, and provided the identity of the third party was disclosed to the holder on request. The holder therefore cannot lose his preferential right by a rejection of an outrageously high offer by the grantor.

Options and preference contracts are closely related and overlapping concepts. The type of preference contract that grants a conditional right to contract can often be understood as a conditional option (or at least as a conditional option subject to a resolutive condition that the grantor does not want to contract anymore). The traditional distinction between options and rights of first refusal can only be maintained in respect of some types of preference contracts. These are negative or bare preference contracts which only give rise to remedies aimed at restoring the *status quo ante* the breach, as well as those preference contracts creating conditional rights to contract which courts refuse to treat as conditional options because their wording implies a duty to make or accept an offer, or because the requirement of certainty precludes them from being options.

## Opsomming

Die verskillende konstruksies van voorkeepsregte aanvaar in Suid-Afrikaanse beslissings het almal meriete. Dit word bevestig deur die verskillende tipes voorkeepskontrakte wat veral in die Duitse reg erken word. Die neiging van Suid-Afrikaanse howe en skrywers om een benadering as die enigste korrekte een te tipeer veroorsaak spanning en onsekerheid, des te meer weens die versuim om die relevante beleidsoorwegings deeglik te ondersoek. Boonop is die presedentestelsel telkens verontagsaam deur verkeerde interpretasies van vorige uitsprake en deurdat teenstrydige uitsprake bloot geïgnoreer is.

Geen sekerheid bestaan oor die konstruksie van die kontraktuele voorkeepsreg in die Romeinse of Romeins-Hollandse Reg nie. Dit is ook nie duidelik watter figuur of figure in die Suid-Afrikaanse reg geresipieer is nie. Die Germaanse konsep van gesplitste eiendomsreg wat die historiese basis van die *Oryx*-meganisme daarstel, vorm nie deel van ons reg nie. Dit verduidelik hoekom howe en skrywers sukkel om dié remedie te verduidelik aan die hand van Romanistiese verbintenisreg-terminologie, en die gevolglike gebruikmaking van fiksie-taal.

Die Duitse en Engelse reg waarop gesteun is in Suid-Afrikaanse regspraak, steun nie 'n uniforme konstruksie van alle voorkeepsregte as behelsende 'n afdwingbare plig om 'n aanbod te maak by enige manifestasie van 'n begeerte om te verkoop nie. Die byna eenparige steun van Noord-Amerikaanse howe vir 'n remedie waarmee die voorkeepsreghouer uiteindelik prestasie van die substantiewe kontrak kan kry by sluiting van 'n kontrak met 'n derde, is 'n teenvoeter vir die hipotese gesuggereer deur die Duitse reg dat die verstekkonstruksie van voorkeurkontrakte behoort te wees dat slegs 'n negatiewe verpligting geskep word.

Die kriptiese wyse waarop voorkeurkontrakte normaalweg opgestel word, maak dit moeilik om selfs die hoofdoelstelling van die partye te identifiseer. Dit is daarom nie maklik om voorkeurkontrakte te klassifiseer in die verskillende tipes wat in hierdie studie geïdentifiseer is nie. 'n Verstekregime is daarom wenslik in die belang van

regsekerheid. Die keuse van verstekregime behoort gemaak te word op die basis van erkende beleidsoorwegings, spesifiek op die basis van 'n billike balansering van tipiese partybelange en in die lig van gemeenskapsbelange gebalanseer teen die vereiste van regsekerheid. Die keuse van verstekregime kan nie gebaseer word bloot op historiese gesag en vorige beslissings nie (wat in elk geval in die huidige konteks onduidelik is). Dit kan ook nie gebaseer word op ongemotiveerde aansprake dat een model meer logies of kommersieel bruikbaar as 'n ander is nie. Wanneer verstekreëls gekies word moet dit, sover moontlik, versoen word met die bestaande begrippe-struktuur van ons reg om teenstrydighede in die sisteem te vermy.

'n Beleidsanalise laat blyk dat drie verstektipes voorkeurkontrakte erken behoort te word, elk met 'n duidelik afgebakende toepassingsveld. Eerstens, waar die ooreenkoms toelaat dat die voorkeurregiewer eers met 'n derde party kontrakteer, het die voorkeurreghouer 'n opsie om te kontrakteer op die terme ooreengekom met die derde. Die voorkeurkontrak kan daarom beskou word as 'n opsie onderhewig aan die voorwaarde van sluiting van 'n kontrak met 'n derde. Sulke kontrakte is raar in Suid-Afrika. In ander gevalle behoort die verstekreël te wees dat die voorkeurregiewer eers die houer 'n geleentheid moet gee om te kontrakteer voordat sy met 'n derde 'n kontrak aangaan. Die verstekkonstruksie van hierdie laasgenoemde tipe voorkeurkontrak hang daarvan af of die voorkeurkontrak self die substantiewe kontraksprys vasstel. Indien wel het die houer die reg of opsie om te kontrakteer teen daardie prys by enige manifestasie van 'n begeerte om die spesifieke soort kontrak te sluit. Maar waar die voorkeurkontrak nie die prys vasstel nie, of verwys na 'n prys wat die gewer sou aanvaar van 'n derde, behoort enige manifestasie van 'n begeerte om te kontrakteer nie genoeg te wees om die houer se reg afdwingbaar te maak nie. Die voorkeurregiewer en die gemeenskap het 'n belang daarby dat die gewer se vryheid om met derdes te onderhandel so min as moontlik beperk word sodat sy die beste moontlike prys kan kry. In sulke gevalle behoort die verstekreël te wees dat die houer slegs geregtig is op die voordeel van die substantiewe kontrak by kontrakbreuk in die vorm van 'n kontrak met of aanbod aan 'n derde. Die verstekreël behoort ook te wees dat sulke voorkeurkontrakte in beginsel slegs beëindig word wanneer die voorkeurregiewer inderdaad kontrakteer met en presteer aan 'n derde binne 'n redelike tyd nadat die voorkeurreghouer die geleentheid gegee is om daardie terme te ewenaar. Dit behoort ook vereis te word dat die identiteit van die derde aan die houer geopenbaar word op sy

versoek. Die houer kan dus nie sy voorkeurreg verloor deur nie-aanvaarding van 'n belaglik hoë aanbod deur die voorkeurreggewer nie.

Opsies en voorkeurkontrakte is oorvleulende konsepte. Die tipe voorkeurkontrak wat 'n voorwaardelike reg om te kontrakteer verleen kan dikwels verstaan word as 'n voorwaardelike opsie (of minstens as 'n voorwaardelike opsie onderhewig aan 'n ontbindende voorwaarde dat die gewer glad nie meer wil kontrakteer nie). Die tradisionele onderskeid tussen opsies en voorkeurregte kan slegs behou word tot sommige voorkeurkontrakte. Hulle is die “negatiewe” voorkeurkontrakte, wat slegs aanleiding gee tot remedies gemik op herstel van die *status quo ante* kontrakbreuk sowel as daarde voorkeurkontrakte wat voorwaardelike regte om te kontrakteer skep wat houe weier om as voorwaardelike opsies te behandel omdat hulle bewoording wys op 'n plig om 'n aanbod te maak of te aanvaar, of omdat die vereiste van sekerheid hulle verhoed om opsies te wees.

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# 1 Introduction

Lease contracts often contain a clause providing that if the lessor should decide to sell the leased premises, the tenant will first be given the opportunity to buy the premises, before it may be sold to an outsider.<sup>1</sup> Such a clause allows the lessee the freedom of exiting the lease relationship after the initial period, and therefore maintains flexibility, whilst preventing opportunism on the part of the lessor. It may often be more desirable than a long-term or short-term contract. One benefit for the lessor is that it creates an incentive for the lessee to invest in the property.<sup>2</sup> Similar arrangements are encountered in other contracts concerning immovable property. Occasionally a seller will insist on a choice to buy back the land should the buyer decide to sell.<sup>3</sup> Her purpose may be, for example, to keep the land in the family or to control the use of the sold land to prevent interference with her activities on neighbouring land. Sometimes the seller of a portion of his property agrees that the buyer be given the first opportunity to buy the remainder of the land.<sup>4</sup> A person interested in acquiring land adjoining his may conclude a similar agreement with his neighbour.<sup>5</sup> The function of such restraints on alienation in the context of sales of land is to prevent bargaining breakdown between the grantor and the holder who is supposed to be the person who values the property most, whilst

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<sup>1</sup> See regarding business or industrial premises: *Owsianick v African Consolidated Theatres (Pty) Ltd* 1967 3 SA 310 (A); *Crossroads Properties (Priv) Ltd v AI Taxi Service Co (Priv) Ltd* 1954 4 SA 514 (SR); *cf Ramburan v Minister of Housing (House of Delegates)* 1995 1 SA 353 (D&C). In respect of agricultural land see: *Van der Hoven v Cutting* 1903 TS 299; *Sher v Allen* 1929 OPD 137; *Hattingh v Van Rensburg* 1964 1 SA 578 (T); *Hartsrivier Boerderye (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T); *Krauze v Van Wyk* 1986 1 SA 158 (A); *Hirschowitz v Moolman* 1985 3 SA 729 (A); *Rogers v Phillips* 1985 3 SA 183 (E) and *Stewart v Breytenbach* 1986 3 SA 47 (A).

<sup>2</sup> Mitchell "Can a Right of First Refusal be Assigned?" 2001 *University of Chicago Law Review* 985 989.

<sup>3</sup> For example in *Malan v Schalkwyk & Odendaal* 1852 1 S 225; *Meyer, Smuts Executrix v Meyer* 1858 2 S 75; *Smith & Os v Momberg* 1895 SC 295; *Le Roux v Odendaal & Os* 1954 4 SA 432 (N); *Crous NO v Utilitas Bellville* 1994 3 SA 720 (K).

<sup>4</sup> *Joseph's Executor v Peacock* 1868 Buch 247.

<sup>5</sup> *Cf Manchester Ship Canal Company v Manchester Racecourse Company* [1901] 2 Ch 37 (CA).

simultaneously retaining flexibility.<sup>6</sup> Former co-owners are likely to include an analogous clause in favour of one another in their agreement of partition.<sup>7</sup> Joint operation (or partnership) contracts also often contain similar restraints.<sup>8</sup>

Another important application of agreements entitling a class of persons to be preferred as buyer pertains to company shares. A private company is obliged by the Companies Act to limit the rights of its shareholders to freely transfer their shares.<sup>9</sup> For this reason company statutes often provide for an arrangement identical or akin to rules 21-24 of Table B of the Companies Act 61 of 1973, in terms of which other shareholders will be given the first chance to buy the shares of a member intending to sell his shares.<sup>10</sup> A purported transfer of shares to any outsider in contravention of these rules is void *ab initio*.<sup>11</sup> Occasionally a shareholder agrees to prefer a non-shareholder in a like manner.<sup>12</sup> Partnership contracts may also contain such an obligation to prefer the other partners on sale of an interest in the partnership.<sup>13</sup>

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<sup>6</sup> Mitchell 2001 *University of Chicago Law Review* 985 990.

<sup>7</sup> *Wissekerke v Wissekerke* 1970 2 SA 550 (A). A right of pre-emption was granted to a mortgage holder in *McGregor v Jordaan* 1921 CPD 301. The mortgagee's real right does of course limit the owner's capacity to alienate the property without the bondholder's consent. (Van der Merwe *Sakereg* 2<sup>nd</sup> edition (1989) 624). See generally *Transvaal Silver Mines v Jacobs, Le Grange & Fox* 1891 4 SAR 116 and *Minter v Robinson D.M. Co Ltd* 1897 CLJ 205.

<sup>8</sup> Cross "The ties that bind: preemptive rights and restraints on alienation that commonly burden oil and gas properties" 1999 *Texas Wesleyan Law Review* 193.

<sup>9</sup> Section 20 (1) of The Companies Act 61 of 1973.

<sup>10</sup> As sanctioned by s 59 (2). See also Basson "Beware of those pre-emptive rights" *Finance Week* 2001-06-01 43; *Irish & Co Inc (Now Irish & Menell Rosenberg Inc) v Kritzas* 1992 2 SA 623 (W); *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 4 SA 15 (SCA). Such an arrangement may also be created by a shareholders' agreement as in *Bellairs v Hodnett* 1978 1 SA 1109 (A). Cf also *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd* 1982 3 SA 893 (A) and Coetzee "Total demp Sasol/Engen-transaksie" *Finansies & Tegniek* 1995-07-21 13.

<sup>11</sup> *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 4 SA 15 (SCA).

<sup>12</sup> *Skinner v Goldberg* 1943 WLD 42; *Cohen v Behr* 1946 CPD 942; *Oryx case supra*.

<sup>13</sup> *Savage & Pugh v Knox* 1955 3 SA 149 (N).

Clauses that grant a publisher the first opportunity of publishing a possible future work of the author are widely used.<sup>14</sup> A publisher agreeing to publish an author's first work takes the risk that the immense cost of publishing and marketing the work of an unknown author will not be covered by the proceeds thereof. By obtaining a preference to publish future works, the publisher is in a position to spread the risk of the initial investment over a range of potential works. For similar reasons, a music recording company might insist on a comparable clause when concluding an agreement to record and market an artist's work. The opportunity of acquiring possible future rights to designs or products developed by a struggling or start up developer of computer software would likewise make it worthwhile for an investor in this field to infuse funds into the development and marketing of a concept or product.<sup>15</sup> Such an arrangement might also enable the company to restrain their employees or independent contractors, in whom they might have invested significantly, from developing products that compete with those of the company, without the need to resort to a typical restraint of trade.<sup>16</sup>

Some employment contracts give the employer an opportunity to match any offer from another company, for example for a certain period after the expiration of the original employment contract.<sup>17</sup>

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<sup>14</sup> See for example, Schricker *Bappert & Maunz: Verlagsrecht* 3rd edition (2001) 132; Bappert & Wagner *Rechtsfragen des Buchhandels* 2nd edition (1958) 155, par 20.4; Haberstumpf & Hintermeier *Einführung in das Verlagsrecht* (1985) 115-120 (§ 1 RdNr 44); Brandi-Dohrn *Der urheberrechtliche Optionsvertrag: Urheberrechtliche Abhandlung des MPI, Heft 6* (1967). No such clause has apparently been considered by our courts.

<sup>15</sup> Rosenoer "Acquiring rights in tomorrow's software: first refusal and first negotiation rights under Californian law" 1990 (7) *The Computer Lawyer* 13.

<sup>16</sup> *Ibid.*

<sup>17</sup> See for example, *American Broadcasting Companies Inc v Wolf* 76 AD2d 162, 430 NYS2d 275, 277 (1980), cited by Mitchell 2001 *University of Chicago Law Review* 985 at n 4. See also Wonnell CT "The Contractual Disempowerment of Employees" 1993 *Stanford Law Review* 87, 108. Such terms are often inserted in employment contracts in the sports sector. See, for example, *Golden Lions Rugby Union v AJ Venter & Others*, an unreported judgment by Swart J in the TPD dated 11 February 2000 (case number 2007/2001) at p 28. Cf also Milner "Ajax spreads its wings" *Mail & Guardian* 1999-01-15 54 on the

The licensor of a patent may insist in the patent licensing agreement that it be granted a right to match a third party offer to obtain the licensee's business, if the licensor is dependent on the licensee for manufacturing or commercialization.<sup>18</sup> A distributorship agreement may also contain a similar right for the distributor to be preferred above third parties in respect of the distribution of any new product which the manufacturer may produce.<sup>19</sup>

In some franchise agreements the franchisee agrees not to sell the business without allowing the franchisor the chance to purchase. This also places a restraint on the franchisee's freedom to trade.<sup>20</sup> Such a term appears to serve as a catch-all clause should the customary "no sale without the consent of the franchisor" clause be unenforceable as an unreasonable restraint of trade. It also entrenches the franchisor's control over the identity of a future purchaser, if a court should hold that its consent to a sale was unreasonably withheld.<sup>21</sup> The franchisor could then buy and operate the business until an acceptable buyer is found. The franchisor might, however, also agree to give the franchisee the first opportunity to purchase any future franchises that might be developed in a certain area.<sup>22</sup> A right of first refusal to renew a short-term franchise contract is regarded as an incentive to invest as the franchisee is not in danger of losing the benefits of his investments, but still maintains his exit-option.<sup>23</sup>

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agreement between the Dutch soccer club Ajax and a South African club requiring Ajax to invest in the South African club in return for the preferential opportunity to "buy" the South African club's players.

<sup>18</sup> Chambers GW & Consalvi MS "Patent and High Technology Licensing" *Practising Law Institute PLI Order No. G0-00SG San Francisco* 2001-05-16, New York City 2001-06-11 *Patent & High Technology Licensing* 652 PLI/Pat 457.

<sup>19</sup> Siviglia "Helpful Practice Hints: Rights of first refusal" 1994 *New York State Bar Journal* 56.

<sup>20</sup> *Longhorn Group (Pty) Ltd v The Fedics Group (Pty) Ltd* 1995 3 SA 836 (W); Mitchell 2001 *University of Chicago Law Review* 985.

<sup>21</sup> Cf the wording of the agreement in the *Longhorn* case at 838C-G.

<sup>22</sup> See for example the agreement considered in *Schupack v McDonald's System Inc* 200 Neb 485, 264 NW2d 827, 828 (1978) discussed by Mitchell 2001 *University of Chicago Law Review* 985 1000 *et seq.*

<sup>23</sup> Mitchell 2001 *University of Chicago Law Review* 985 1000 *et seq.*

A holder of mineral rights may agree to an analogous restriction on its ability to freely alienate or lease the rights.<sup>24</sup> The parties' primary purpose may be to preclude a competitor from getting hold of these rights.<sup>25</sup>

An agreement binding a trader to purchase its total requirement of a specific commodity from a certain supplier means that the supplier must be preferred above all others when the buyer wishes to buy.<sup>26</sup>

The traditional terminology applied to all these types of arrangements have been that they give rise to "rights of pre-emption," connoting preferential rights to buy, or "rights of first refusal," which suggests a wider concept – a right to be given the first opportunity to decide whether to enter into a specific transaction or not.<sup>27</sup>

Such agreements to prefer a specific person when transacting are indeed not only directed at contracts of sale. Some lease agreements, for example, oblige the lessor, on termination of the lease, to first give the tenant the opportunity to conclude another lease contract before agreeing to lease the premises to a third party.<sup>28</sup>

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<sup>24</sup> *Dithaba Platinum v Erconovaal* 1985 4 SA 615 (T); Mitchell 2001 *University of Chicago Law Review* 985; Cross 1999 *Texas Wesleyan Law Review* 193.

<sup>25</sup> *Dithaba Platinum v Erconovaal* 1985 4 SA 615 (T). Evidence was lead that the holder did not wish to acquire the mineral rights, but desired the power to prevent the rights from falling into the hands of a specific competitor (621C-D).

<sup>26</sup> *Kimberley Waterworks Co v De Beers Consolidated Mines Ltd* 1897 AC 515; *Shell SA (Pty) Ltd v Corbitt & Another* 1986 4 SA 523 (C); Lubbe 1986 *Annual Survey of South African Law* 141-143; Tew "Rights of First Refusal: The 'Options' That Are Not Options, But May Become Options" 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-10.

<sup>27</sup> The term "right of first refusal" has also been used interchangeably with "right of pre-emption", for example in the *Dithaba Platinum* case.

<sup>28</sup> *Soteriou v Retco Poyntons* 1985 2 SA 922 (A); *Aronson v Sternberg (Pty) Ltd* 1985 1 SA 597 (A).

Therefore a broader or more general term than “pre-emption contracts” is needed to describe these transactions. As an alternative to “first refusal contracts,” a number of writers have appositely termed these transactions “contracts of preference” or “voorkeurkontrakte”.<sup>29</sup>

However, arrangements granting a preferential right to contract are not only created contractually. The same phenomenon is often encountered in wills, where a testator provides that a beneficiary may not sell the inherited object without giving another person a chance to buy it first. Adiation of such an inheritance brings about the same obligation for the heir or legatee as a contract of preference would have.<sup>30</sup>

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<sup>29</sup> Reinecke & Otto “Voorkope en ander voorkeurkontrakte” 1986 *TSAR* 18 21; Van der Merwe *et al Contract: General Principles* (1993) 62. Reinecke & Otto 1986 *TSAR* 18 suggests the term “voorkeurreg” for the general concept which they state is usually termed a “right of first refusal” in English. See also Kerr *The Law of Sale and Lease* 2<sup>nd</sup> edition (1996) 338 (“preferent conditional right”), Van der Merwe *et al Contract* 62 (“preferential right”, “preferential right to buy”, “preferential right to lease”). As various other rights are described as “voorkeurregte” or “preferential rights”, it is submitted that such terms are not apt to describe the preference holder’s claim in the present context. See for example Van der Merwe *Sakereg* 82 n151 (“voorkeurreg” created by s 20 of the *Alienation of Land Act*), *Van Zyl NO v Look Good Clothing CC* 1996 3 SA 523 (SEC) (“voorkeurreg” to payment out of the proceeds of a claim ceded *in securitatem debiti*), *Trisilindo v DeVries* 1994 4 514 (O) (“preferential right” of a mortgagee), *Land- & Landboubank van SA v Cogmanskloof Besproeiingsraad* 1992 1 SA 217 (A) (“voorkeurregte” created by legislation in favour of both parties), Poolman *J Emmissie van genoteerde, gewone aandele met voorkeurreg in Suid-Afrika gedurende die tydperk 1950 tot 1964* M Com dissertation (Pretoria 1966). The term “preferential right to transact” (“voorkeurreg om te kontrakteer”) would exclude such other meanings. “Right of first refusal” is also not objectionable, but is perhaps not wide enough to encompass all forms of preferential rights to transact, and has been said to automatically encompass a duty to make an offer. This is disputable, however, and this loaded term will therefore not be generally used in this thesis.

<sup>30</sup> *Van Wyk v Posemann & Another* 1915 CPD 672; *Fick v Fourie* 1934 EDL 152; *Engelbrecht v Mundell’s Trustee* 1934 CPD 111; *Ex parte Zunckel* 1937 NPD 295; *Bodasing v Christie NO* 1961 3 SA 553 (A). Cf *Schoeman v Rossouw & Others* 1915 CPD 446.

Legislation has also been used to create a such preferential rights to contract, often in favour of the state or one of its organs.<sup>31</sup> Such a statutory preference may also be created to protect certain classes of private persons.<sup>32</sup>

The focus here will be on preference contracts.

Rights of pre-emption are traditionally discussed in conjunction with a related concept - options.<sup>33</sup> An option contract is an agreement restricting the offeror's capacity to revoke an offer.<sup>34</sup> A right of pre-emption is said to differ from an option in the sense that an option holder has an immediate power to bring the substantive contract into existence on accepting the offer entrenched by the option contract, without any further action being required from the grantor of the option. In the case of a right of pre-emption, the holder might never get the opportunity to buy the property, even if she declares herself willing to do so. If the person obliged to give the preference never manifests a desire to contract, the holder will never have the power to conclude the main contract.

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<sup>31</sup> For example, the now repealed Community Development Act 3 of 1966, considered in *Ah Ling v Community Development Board & Os* 1972 4 SA 35 (E). Statutory rights of pre-emption are widely used in certain overseas jurisdictions to enable the state or local authorities to obtain land for the furtherance of projects relating to land development, redistribution or conservation. See for example §§ 24-26 *Baugesetzbuch* (Germany).

<sup>32</sup> Section 10 of the Share Titles Act 95 of 1986 (which obliges the developer of a sectional title scheme in respect of an existing building to give the lessees the first chance to buy the unit they occupy). In Germany and Switzerland, for example, legislation creates a preference in favour of co-heirs to buy property which a heir intends to sell. See § 2034 *Bürgerliches Gesetzbuch (BGB)*. Cf also the English Landlord and Tenant Act 1987 which grants certain tenants of flats a preferential right to buy the premises if the landlord intends to sell.

<sup>33</sup> See, for example, Van der Merwe *et al Contract* 55 *et seq*; Hackwill *Mackeurtan's Sale of Goods in South Africa* 5<sup>th</sup> edition (1984) 275, 44; Belcher *Norman's Purchase and Sale in South Africa* 4<sup>th</sup> edition (1972) 95 *et seq*; cf Kerr *Sale and Lease* (1996) 408 *et seq*; Christie *The Law of Contract in South Africa* 4<sup>th</sup> edition (2001) 59 *et seq*.

<sup>34</sup> In the words of Van der Merwe *et al Contract* 56-57. See also, for example, *Hirschowitz v Moolman supra* and *Stewart v Breytenbach supra*; Kerr *The Principles of the Law of Contract* 5<sup>th</sup> edition (1998) 77; Christie *Contract* 59.

Preference contracts and options are traditionally classed together under the umbrella concept of *pacta de contrahendo*.<sup>35</sup> A *pactum de contrahendo* has been defined as “an agreement to make a contract in the future,”<sup>36</sup> and more widely, as “a contract aimed at the conclusion of another contract,”<sup>37</sup> and “agreements which may lead to a future contract.”<sup>38</sup> Options and preference contracts could be described as “unilaterally binding” *pacta de contrahendo* as they only limit the grantor’s freedom to contract with others, but leave the holder totally free to decide whether to contract. This label distinguishes them from agreements that bind both parties to contract in the future, which also qualify as enforceable *pacta de contrahendo* in some foreign legal systems.<sup>39</sup> On the other hand, as the holder of an option or right of first refusal sometimes undertakes a counter-performance in return for his right, obligations may be created for both parties, which

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<sup>35</sup> *Hirschowitz v Moolman supra* 765-766; Reinecke & Otto 1986 *TSAR* 18 33; Van der Merwe *et al Contract* 58.

<sup>36</sup> *Hirschowitz v Moolman supra* 765-766; Nienaber “Formaliteit by Koop en Sessie tov Grond: die Jongste Beslissing” 1964 *THRHR* 44; De Wet & Van Wyk *Die Suid-Afrikaanse Kontrakereg en Handelsreg vol I* 5<sup>th</sup> edition (1992) 34 (“an agreement to conclude an agreement in the future”).

<sup>37</sup> Van der Merwe *et al Contract* 56. *Cf* Du Plessis *Die spesifieke nakoming van voorkeepsregte en ander verwante regte in die Suid-Afrikaanse en Franse Reg* unpublished LLM thesis, University of Stellenbosch (1997) 10.

<sup>38</sup> Lotz “Purchase and Sale” in Zimmermann & Visser *Southern Cross: Civil Law and Common Law in South Africa* (1996) 358.

<sup>39</sup> The (bilaterally binding) *Vorvertrag* of German law is an example of such an “agreement to agree”. On *Vorverträge* generally, see Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* (1965) 84 *et seq.* Such “agreements to agree” are not unknown in our law, but, as Van der Merwe *et al Contract* 58 point out, “their applicability is limited by the requirement of certainty as interpreted by the courts, and by the unwillingness of the courts to enforce an oral agreement to conclude a substantive contract, which is required by law to be in writing.” I use the term *pacta de contrahendo* in a wide sense to also include agreements which merely prohibit the grantor from concluding the specific contract with a third party, although they do not grant the holder an enforceable right to conclude the contract. For a similar wide definition see Lotz “Purchase and Sale” 358 (“agreements which may lead to contracts”). If a *pactum de contrahendo* is defined as an agreement to conclude an agreement or if Reinecke & Otto is correct in stating that a *pactum de contrahendo* necessarily implies the existence of a “substantive offer”, I submit and will show that this term is not wide enough to include all types of preference contracts.

then contradicts the “unilaterally binding” label. Whether all preference contracts are indeed *pacta de contrahendo* under both the narrow and wide definitions of that concept, will be considered in a later chapter.

## 1 1 **Problematic aspects**

As the traditional labels of “rights of pre-emption” or “rights of first refusal”, appear to refer to personal rights *ex contractu*, one would expect the normal remedy of specific performance to be available to the preference holder. Specific performance in this context has traditionally been understood by commentators to encompass an order to make an offer when the grantor has manifested a desire to transact.<sup>40</sup> Our courts have however been loath to grant such an order, as appears from a line of cases in which specific performance in this form was not granted, and mostly not even asked for.<sup>41</sup>

The matter came to a head in *Owsianick v African Consolidated Theatres (Pty) Ltd*<sup>42</sup> where the minority of the Appellate Division was prepared to grant an order for specific performance. The minority thereby confirmed the view that a contract of preference creates a positive duty to make an offer. However, the majority, per Botha JA, confirmed the traditional view that only an order for damages may be obtained.<sup>43</sup> The majority regarded the duty on the grantor as merely a negative one – the grantor may not sell to an

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<sup>40</sup> Floyd “Die Voorkoopreg” 1986 *THRHR* 253 257 *et seq* and authorities there cited; Flack “The Pre-emption Agreement: Is it a viable option?” 2001 *SALJ* 842; Eiselen “*Soteriou v Retco Poyntons (Pty) Ltd* 1958 2 SA 922 (A)” 1986 *THRHR* 95 99. *Cf* Van der Merwe *et al Contract* 68; Reinecke & Otto 1986 *TSAR* 18 21, 22. This view is based on the notion that the grantor has a duty to make an offer once she decides to conclude the main contract.

<sup>41</sup> *Joseph’s Executor v Peacock* 1868 Buch 247; *Transvaal Silver Mines v Jacobs*; *Le Grange & Fox* 1891 4 SAR 116; *Van Pletzen v Henning* 1913 AD 82; *McGregor v Jordaan* 1921 CPD 301; *Sher v Allen* 1929 OPD 137.

<sup>42</sup> 1967 3 SA 310 (A).

<sup>43</sup> Wessels and Potgieter JJA concurred with Botha JA.

outsider.<sup>44</sup> In a further decision of the Appellate Division on this matter, *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd*,<sup>45</sup> it was again questioned whether specific performance in the form of an order to make an offer could be made. Instead, the court granted the holder a more drastic remedy. It held that the holder of a right of pre-emption may by unilateral declaration of will bring a contract of sale into existence once the grantor of the preference had concluded a contract of sale with a third party without first giving the holder the opportunity to buy. In effect, a direct claim to delivery of the *merx* is available on breach. This remedy came to be known as the *Oryx* mechanism – an indication that it is considered a novelty in our law.<sup>46</sup>

The position is not in fact crystal clear after the *Oryx* case. Thus the judges deciding the case of *Crundall Brothers (Pvt) Ltd v Lazarus NO and Another*<sup>47</sup> confessed that they “have some difficulty in understanding the effect of the order made in the *Bakeries* case – a difficulty apparently shared by the two Judges of Appeal who dissented in that case, and by Professor Kerr...”<sup>48</sup> The cogency of the reasons for the decision in *Oryx* has been questioned.<sup>49</sup> The court’s failure to spell out the basis of the *Oryx* mechanism has left an impression that a fiction is at work with all the dangers flowing therefrom.<sup>50</sup> One

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<sup>44</sup> These constructions of preference contracts will be discussed in depth the next chapter.

<sup>45</sup> 1982 3 SA 893 (A), which was the next decision of the Appellate Division on this matter but for *Bellairs v Hodnett supra*.

<sup>46</sup> See Lubbe 1986 *Annual Survey* 136 139; Lubbe & Murray *Farlam & Hathaway’s Contract: Cases, Materials and Commentary* 3<sup>rd</sup> edition (1988) 93 n 5, Du Plessis “Die remedies van die huurder by omskepping van huurgeboue in deeltitelskemas” 1996 *Stell LR* 329 337; Du Plessis *Spesifieke nakoming* 29. Cf Van der Merwe *et al Contract* 66.

<sup>47</sup> 1992 2 SA 423 (ZSC).

<sup>48</sup> 429D.

<sup>49</sup> Eiselen 1986 *THRHR* 95 99.

<sup>50</sup> Radesich “*Soteriou v Retco Poyntons (Pty) Ltd* 1985 2 SA 922 (A): Landlord and tenant – lease - right of first refusal” 1985 *De Jure* 407 409. See also *Hirschowitz v Moolman supra* 763I-J where the court states that a difficulty with the *Oryx* mechanism is that the formalities legislation requires a written offer “in fact (and not merely notionally).” The *Oryx* court’s words “’n Koopkontrak word dan *geag* aangegaan te gewees het...” (907F) is pure fiction language. See Olivier *Legal Fictions: an analysis and evaluation*

commentator has even declared that the precise nature, effect and basis of the so-called *Oryx* mechanism *cannot* be ascertained with certainty.<sup>51</sup>

The court in *Oryx* also expressly left open certain important questions affecting the operation of preference contracts, *inter alia* whether not only a contract of sale would trigger the *Oryx* mechanism, but also an offer to sell to a third party, and whether the preference contract must conform with the formalities prescribed for the eventual substantive contract.<sup>52</sup> The *Oryx* mechanism as formulated by the court, appears inappropriate in some situations, for example where the terms agreed with the third party differ from those to which the holder is entitled in terms of the contract of preference.<sup>53</sup> These shortcomings place a question mark behind the court's rejection of the alternative constructions advocated in *Owsianick*.<sup>54</sup>

The cases following upon the *Oryx* case have not satisfactorily resolved the controversial issues either. In *Hirschowitz v Moolman*<sup>55</sup> the Appellate Division assumed for the purposes of the case, without deciding the question, that the *Oryx* mechanism is also triggered by the grant of an option, and that an order for specific performance in the form of an order to make an offer is still available as an alternative remedy to the *Oryx* mechanism.<sup>56</sup> The court did decide one question left open in the *Oryx* case, in holding that

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(1973), especially at 96-98 and Lubbe & Murray *Contract* 442 n 6 on the dangers of using fictions to solve legal problems. Cf Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 280.

<sup>51</sup> Du Plessis 1996 *Stell LR* 329 337. Cf Van der Merwe *et al Contract* 66; Lubbe & Murray *Contract* 93-94.

<sup>52</sup> 908F-G.

<sup>53</sup> Reinecke & Otto 1986 *TSAR* 18 24. See also Lubbe 1985 *Annual Survey* 141 and 1982 *Annual Survey* 130 and Floyd 1986 *THRHR* 253 266.

<sup>54</sup> I use the word "construction" to refer to a view or explanation of the rules relating to a specific type of contract, which include the reserve rules or *naturalia*, but also the criteria for classifying a transaction under that type.

<sup>55</sup> 1985 3 SA 729 (A).

<sup>56</sup> At 763F-G and 764G-H respectively. This assumption may have been made as the application was launched before the decision in *Oryx*. See Lubbe 1985 *Annual Survey* 139.

a contract of pre-emption in respect of land must comply with the formalities legislation.<sup>57</sup>

The confusion has been exacerbated by statements in other cases which conflict with the *Oryx* case. *Rogers v Phillips*<sup>58</sup> holds, in conflict with the *Oryx* case, that a right of pre-emption merely gives the holder a personal right to an offer by the owner. The court effectively held that the holder cannot become a purchaser unless an offer is actually made to the holder.<sup>59</sup> In *Dithaba Platinum v Erconovaal*<sup>60</sup> the court never referred to the *Oryx* mechanism, but surprisingly held that the *Oryx* case confirmed that specific performance can be granted to enforce a pre-emptive right and that a court has a discretion to refuse this remedy.<sup>61</sup>

Thus the exact construction of preference arrangements remains uncertain. The contrary views in the case law on the enforceability of the primary duty of the person obliged to give the preference, place the nature of the preference holder's claim in question.

## 1 2 Academic views

Various writers have pointed out the uncertainty surrounding contracts of preference, especially after the decision in *Oryx*.<sup>62</sup>

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<sup>57</sup> 767G-H.

<sup>58</sup> 1985 3 SA 183 (E) 187D.

<sup>59</sup> 188C-D.

<sup>60</sup> 1985 4 SA 615 (T).

<sup>61</sup> 627D-E.

<sup>62</sup> Lubbe 1982 *Annual Survey* 128; Reinecke & Otto 1986 *TSAR* 19 21; Floyd 1986 *THRHR* 253; Lambiris *Orders of Specific Performance and Restitutio in Integrum in South African Law* (1989) 78; Van der Merwe *et al Contract* 64-66. Cf Eiselen 1986 *THRHR* 95 100; Du Plessis 1996 *Stell LR* 329 336; Du Plessis *Spesifieke nakoming* 24, 31; Janisch "Maintaining the distinction between options and pre-emption agreements" 1990 *Responsa Meridiana* 434 441; Flack 2001 *SALJ* 842 831.

Their views on the remedies available to the preference holder diverge. Various writers insist that logically an order for specific performance in the traditional sense (that is in the form of an order to make an offer) must be available to the holder of a right of pre-emption.<sup>63</sup> Some consider that the *Oryx* mechanism negates the discretion of the court to grant or refuse specific performance of contracts.<sup>64</sup> Thus they either reject the *Oryx* mechanism and advocate a remedy of specific performance in the traditional sense only,<sup>65</sup> or insist that the *Oryx* mechanism should be recognised as a form of specific performance, so that the court's sanction must be sought for the contract of sale to be created.<sup>66</sup>

However, many writers welcome the new direction taken in *Oryx*, especially the practical consequences for a holder who wants to acquire the property on breach.<sup>67</sup> Some of these writers still foresee a need for an order of specific performance in the traditional sense in circumstances where the *Oryx* mechanism cannot be available.<sup>68</sup>

A number of writers have recognised the underlying problem with the decision in *Oryx* to be the court's failure to spell out the precise construction of the contract of preference, and thus the legal explanation of the holder's ability to unilaterally conjure up a contract of sale.<sup>69</sup> Alternative legal explanations have been proposed,<sup>70</sup> none of which have so far

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<sup>63</sup> Eiselen 1986 *THRHR* 95 99; Floyd 1986 *THRHR* 253 268; Flack 2001 *SALJ* 842 842.

<sup>64</sup> Eiselen 1986 *THRHR* 95 99, Floyd 1986 *THRHR* 253 267. *Cf* the minority in the *Oryx* case *supra*.

<sup>65</sup> Eiselen 1986 *THRHR* 95 99

<sup>66</sup> Floyd 1986 *THRHR* 253 267. *Cf* also Van der Merwe *et al Contract* 68 *in fine*; Du Plessis *Spesifieke nakoming* 57.

<sup>67</sup> Kerr *Sale & Lease* 410; Cooper *The South African Law of Landlord and Tenant* (1994) 144-146; Reinecke & Otto 1986 *TSAR* 18 21; Du Plessis *Spesifieke nakoming* 31. *Cf* Van Rensburg & Treisman *The Practitioner's Guide to the Alienation of Land Act* (1984) 70-71 and Lubbe 1982 *Annual Survey* 128 130.

<sup>68</sup> See the text at n 53 above. Floyd 1986 *THRHR* 253 267 n 145 and n 268 advises a holder who does not know the terms agreed with the third party, to opt for a prayer for specific performance in the traditional sense. See also Kerr *Sale & Lease* 410.

<sup>69</sup> Reinecke & Otto 1986 *TSAR* 18 21, 24; Eiselen 1986 *THRHR* 95 99; Lubbe 1982 *Annual Survey* 128 130. *Cf* Radesich 1985 *De Jure* 407 409; Du Plessis 1996 *Stell LR* 329; Du Plessis *Spesifieke Nakoming* 31.

received the approval of the courts.<sup>71</sup> Some of these explanations or constructions have in turn been described as problematical by other writers or are simply ignored in their discussion.<sup>72</sup>

The writers' opinions on the construction advocated by the majority in *Owsianick* (per Botha JA) also diverge. A few, especially those writing before the decision in the *Oryx* case, support the negative construction advocated by Botha JA and the court in *Hartsvrivier Boerderye (Edms) Bpk v Van Niekerk*.<sup>73</sup> Those who reject the negative

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On the other hand, some appear to be content with the fact that, if not a fiction, something very close to it, has been introduced into our law. See Janisch 1990 *Responsa Meridiana* 434 444 (who expressly regards the creation of a legal fiction as the preferable explanation). Cf Cooper *Landlord and Tenant* 146 (the holder's right of pre-emption is converted into an option); Van Rensburg & Treisman *The Practitioner's Guide* 71 (the offer to the third party constitutes an offer to the holder).

<sup>70</sup> Reinecke & Otto 24 *et seq*; Lambiris *Specific Performance* 82-85; Van der Merwe *et al Contract* 68; Floyd 1986 *THRHR* 253 258 & 267. Flack 2001 *SALJ* 842 suggests, on the one hand, that rights of pre-emption should be treated as conditional options (832), but then ultimately argues that the court should, subject to its general discretion in the context of specific performance, compel the grantor to make a *bona fide* offer to the grantee (843).

<sup>71</sup> Cf *Soteriou v Retco Poyntons (Pty) Ltd supra* 932E and *Hirschowitz v Moolman supra* 765F-G where the Supreme Court of Appeal in effect rejected the conditional offer construction proposed by Reinecke & Otto 1986 *TSAR* 18.

<sup>72</sup> See Lubbe 1982 *Annual Survey* 28 130; Van der Merwe *et al Contract* 67 *in fine* – 68; Floyd 1986 *THRHR* 253 267; Janisch 1990 *Responsa Meridiana* 434 444.

<sup>73</sup> 1964 3 SA 702 (T). These constructions will be discussed in depth in the following chapter. See Joubert *General Principles of the Law of Contract* (1987) 54, who does not refer to either *Owsianick* or *Oryx*, and Mostert *et al Die Koopkontrak* (1972) 277-278. Neither De Jager *Vervreemding van Grond = Alienation of Land* (1982) 125, nor the writers of *Mackeurtan's Sale of Goods* (1<sup>st</sup> to 5<sup>th</sup> editions), nor the writers of the first three editions of *Norman's Purchase and Sale in South Africa* discuss the availability of an order for specific performance or of the *Oryx* mechanism. This is so despite some references to a positive duty to give the holder the opportunity of refusing the land. (See for example *Norman's Purchase and Sale in South Africa* 1<sup>st</sup> edition (1919) 59-60, 2<sup>nd</sup> edition (1939) 106 & 3<sup>rd</sup> edition (1961) 84.) In the fourth edition of *Norman's Purchase and Sale* (1972) 95 *et seq*, Botha JA's construction is rejected, but still no mention is made of specific performance or of a remedy like the *Oryx* mechanism. Van Rensburg & Treisman *The Practitioner's Guide* 70-71 consider the *Oryx* mechanism to be available only once a contract of sale has

construction do so on very vague grounds, merely calling on commercial efficacy,<sup>74</sup> principle,<sup>75</sup> practical utility,<sup>76</sup> reasonableness<sup>77</sup> and logic.<sup>78</sup> Such construction has also been called “erroneous” and “a misleading simplification”, without any explanation.<sup>79</sup> These writers merely assume that a preference contract creates a directly enforceable obligation on the grantor to make an offer, or at least a right to contract for the holder.<sup>80</sup> On the other hand, certain writers are prepared to concede that the parties may expressly agree a procedure for the exercise of the right so that the results are the same as the rules set out in the *Hartsvivier Boerderye* case.<sup>81</sup> This concession somewhat undermines the

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been concluded with an outsider. In the case of a lesser manifestation of a desire to sell, they advocate an approach which boils down to that advocated in the *Hartsvivier* case.

<sup>74</sup> Cooper *Landlord and Tenant* 144; cf Du Plessis *Spesifieke nakoming* 14. The latter relies on the inadequacy of damages where the grantor has contracted with and delivered to a *mala fide* third party. However, in such a case damages is not the only remedy anyway – the transfer may be set aside by reason of the doctrine of notice. See also *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 4 SA 15 (SCA).

<sup>75</sup> Cooper *Landlord and Tenant* 144.

<sup>76</sup> Reinecke & Otto 1986 *TSAR* 18 20.

<sup>77</sup> Eiselen 1986 *THRHR* 95 97 (“dat dit [*refusal imports an offer*] vanuit 'n praktiese oogpunt die enigste redelike benadering is, is duidelik.”).

<sup>78</sup> Reinecke & Otto 1986 *TSAR* 18 21 n 26. See also Flack 2001 *SALJ* 842 833 who says of the *Hartsvivier* approach that it is “the least realistic”, and that “it is unclear how the right affords anything more than nominal preference.”

<sup>79</sup> In the words of Cooper *Landlord and Tenant* 143.

<sup>80</sup> Cf the writers mentioned in n 74 – n 78, for example Cooper (the existence of an enforceable positive duty on the grantor “is in accordance with principle”). See also Kerr *The Law of Lease* (1969) 146, *Sale and Lease* 1<sup>st</sup> edition (1984) 165; *Sale and Lease* 2<sup>nd</sup> edition (1996) 408; Belcher *Norman's Purchase and Sale in South Africa* 4<sup>th</sup> edition (1972) 97; Du Plessis *Spesifieke nakoming* 14-16. Lubbe 1985 *Annual Survey* 139; Lubbe & Murray *Contract* 92 n 3 and Van der Merwe *et al Contract* 63 reject Botha JA’s approach by implication, by their view that the operation of a right of pre-emption is conditional in the sense that its exercise is linked to the trigger event. This premises that the holder is entitled to become a purchaser at that point. Lambiris *Specific Performance* 82-85 also rejects the negative construction by implication, as he gives only two possibilities for the construction of a contract of pre-emption, namely a conditional future contract of sale or a conditional option.

<sup>81</sup> Eiselen 1986 *THRHR* 95 97; Lubbe & Murray *Contract* 92; Van der Merwe *et al Contract* 62-63; Floyd 1986 *THRHR* 253 261; Flack 2001 *SALJ* 842 833; Lubbe 1986 *Annual Survey* 144-145. Lubbe in this last

argument that such a construction never makes practical or commercial sense. The same honour does not befall Botha JA's approach.

One is left with the impression that the writers' diverging opinions on the nature of contracts of preference have contributed to the complexity of the subject.

There thus remains a need to arrive at a clear exposition of the parties' primary rights and duties and corresponding remedies.

Apart from the basic construction of preference arrangements, less fundamental, but practically important, issues also need to be resolved. For example, if the grantor of a preference should make an offer to the holder when not considering a sale to a third party, would the holder lose his preference on rejection of such offer? What if the holder in such a case alleges that the offer was not *bona fide*? Must a contract of preference in respect of land always comply with the formalities prescribed by the Alienation of Land Act 68 of 1981? What transactions or actions by the grantor or third parties would trigger the availability of the *Oryx* mechanism or an order for specific performance? What, for example, would be the effect of a sale in execution? What if the terms agreed in a contract of sale with a third party cannot be applicable to the holder? What if the grantor only sells a portion of the property, or sells it as part of a larger parcel? What precisely must the grantor who wishes to sell to an outsider disclose to the holder about the

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article states, correctly in my view, that there are various ways in which parties may contract in order to afford one of them a preference should the other decide to sell an asset of his. However, he does not give any clear guidelines on which construction should apply in which situation, and which should be the default one if the preference contract only speaks of a right of pre-emption or right of first refusal. His proposal that grants specifying the pre-emptive price or, expressly or tacitly, incorporating the price at which the grantor is prepared to sell to a third party, will have to be recognized as more akin to option contracts than previously thought, is not very clear. Most rights of pre-emption that do not specify a price, and where there is no usual or market price, could arguably be construed as incorporating the price at which the grantor is prepared to sell to a third party. Does this mean that he proposes a conditional option construction as the default construction where the preference contract does not specify a price clearly or where there is no usual or market price?

intended transaction? How, if at all, may the grantor's duty in this regard be enforced? Should rights of pre-emption be cedable?

Many of the consequences that the law would imply into preference arrangements in the absence of express provisions by the parties are thus uncertain. This problem is exacerbated by the very terse formulations generally resorted to by drafters of preference arrangements in South Africa, which do not provide any guidance on the parties' intention with respect to these questions.<sup>82</sup>

It is submitted that such questions that relate to the implied terms or *naturalia* of a certain type of contract should not be answered without simultaneously considering the basic legal construction of the contract.<sup>83</sup> This does not mean that once the "legal nature" of a contract type is established, the *naturalia* can be simply deduced from it as a mere matter of logic. The typical interests of parties to such contracts and any relevant public policy considerations must still be considered in respect of each specific issue. A coherent, consistent and therefore predictable construction of the entire contract type requires that the primary rights and duties of the parties should be clearly delineated.<sup>84</sup>

The basic construction of preference arrangements will be examined by way of an investigation into the case law, the historical development of our law and the position in certain overseas jurisdictions. Further motivation for this research strategy will be supplied in the relevant chapters. Conclusions will be coupled with an examination of the methodological place of these arrangements among related concepts, such as options and *pacta de contrahendo*. Methodological models for identifying specific contract types, such as the traditional *essentialia-naturalia* model will also be investigated. My proposal

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<sup>82</sup> For example, "Should the grantor wish to sell the property, he shall first offer it to the holder." (as in *Smith & Os v Momberg & Os* 1895 SC 295). See par 2 1 1 at n 5 *infra* for a further example. A number of typical formulations is also considered in par 7 3 *infra*.

<sup>83</sup> Reinecke & Otto 1986 *TSAR* 18 19; Joubert "Die regsraad van die finansiële huurkontrak" 1989 *TSAR* 568.

<sup>84</sup> See further chapter 6 where such methodological considerations are investigated.

will also address some of the more specific questions relating to rights of first refusal mentioned above, although I will focus on the basic rights and remedies of the parties.

The traditional terms “right of pre-emption” or “right of first refusal” as well as the term “preferential right to transact” will be used to describe the claim of the person to whom the preference has been given. The preference holder will be referred to as “the holder” and the person who must prefer the holder will be referred to as “the grantor”.<sup>85</sup> The object or property at which the preference arrangement is directed, will be referred to as “the object” or “the property”. Many writers and decisions describe the right of pre-emption as a preferential right to transact, conditional upon the event described in the contract of pre-emption, usually the manifestation of the grantor’s desire to sell.<sup>86</sup> When discussing this view, the term “trigger event” will be used to refer to such event.<sup>87</sup> I use the verb “construct” to refer to the formulation of rules surrounding a specific contract type. It encompasses the process of incorporating a specific contract type, identified in practice, into the legal system, which enables comparisons with other provisions.<sup>88</sup> A category of contracts is therefore described and coherent rules developed for it, which category is then added to the pantheon of separately regulated specific contract types.

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<sup>85</sup> This term is of course incorrect in the case of preference arrangements created by will or statute, or if it is accepted that a preferential right to buy land could in some circumstances operate against successors in title of the grantor.

<sup>86</sup> *Breytenbach v Stewart* 1985 1 SA 167 (T) 176; Floyd 1986 *THRHR* 253 258; Reinecke & Otto 1986 *TSAR* 18 24; Du Plessis 1996 *Stell LR* 329 333. Cf Lubbe 1982 *Annual Survey* 136; Van der Merwe *et al Contract* 63.

<sup>87</sup> Snellergebeurlikheid” according to Kriegler J in *Breytenbach v Stewart supra* 176. See also Lubbe 1985 *Annual Survey* 138.

<sup>88</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 268. The definition of “construct” as verb in the *Concise Oxford Dictionary* reads as follows: “fit together, frame, build (lit. or fig.); (Gram.) combine (words) syntactically; draw, delineate, esp. According to given conditions...”. As a noun it is defined as “thing constructed, esp. by the mind...” (Pearsall (ed) *Concise Oxford Dictionary* 10<sup>th</sup> edition (2001)).

## 2 Divergent views in the case law

Although courts sometimes acknowledge that the rights and duties of the parties to a preference contract are a matter of interpretation, they tend to deal with preference arrangements as if they belong to a contract type with an invariable, uniform set of default rules.<sup>1</sup> A court encountering a view on the parties' rights, duties and remedies inconsistent with its own, might very well reject that construction rather than to recognize it as based upon the interpretation of a specific, differently worded clause encountered in a different context. Thus the general pronouncements on the right of first refusal in *Hartsvivier Boerderye v Van Niekerk*, belie the statement of the court that "Die verskyningsvorme kan wissel," especially since the clause in question simply provided that if the grantor should decide to sell the land, the holder shall possess the first right of refusal to purchase.<sup>2</sup>

Those decisions that deal with the right of first refusal as a uniform concept reveal two contrasting views. Firstly, some judges espouse the view that a right of first refusal merely places a negative obligation on the grantor not to transact with a third party. This negative obligation terminates if the holder is given an opportunity to transact, but turns it down. The holder does not acquire a right to obtain the subject matter of the right, other than through the acceptance of a voluntary offer made by the grantor.

A second view is that the duty of the grantor is merely initially a negative one, but that on the occurrence of the trigger event she has a duty to act positively to enable the holder to become the purchaser of the property. Adherents of this view can in turn be divided into two camps. There are decisions holding that enforcement of the duty would imply an order against the grantor to make an offer. Secondly, there are decisions which deny the

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<sup>1</sup> Cf Botha JA in *Owsianick v African Consolidated Theatres (Pty) Ltd* 1967 3 SA 310 (A) who stated that his decision depended upon the true construction of the clause but then pronounced upon rights of pre-emption in general.

<sup>2</sup> 1964 3 SA 702 (T).

need for such an order, and which simply grant the holder a power to bring about a contract extra-judicially on the occurrence of the trigger event. A further possible variation holds the right of first refusal to be specifically enforceable by means of a “short-circuited” order. Thus on breach, a court will refrain from an order that an offer be made and simply order the grantor to transfer the property to the holder.<sup>3</sup>

This chapter considers the plurality of constructions of the case law in order to assess whether all these constructions merit further consideration. To this end some brief comments will be made on possible policy considerations supporting each construction.<sup>4</sup> The origin of each construction will be examined briefly to establish which construction, if any, is the authoritative one in our law.

## **2 1 A negative duty**

### **2 1 1 Botha JA in *Owsianick v African Consolidated Theatres (Pty) Ltd***

The most overt and forceful argument that the grantor bears no directly enforceable duty to act positively was made on behalf of the majority of the court by Botha JA in *Owsianick v African Consolidated Theatres (Pty) Ltd*.<sup>5</sup>

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<sup>3</sup> In the case of a right of pre-emption. In a right of first refusal to conclude a lease, the order would be for the lessee to be given possession of the property.

<sup>4</sup> The relevant policy considerations will be investigated more fully in chapters five, six and seven below.

<sup>5</sup> *Supra*. The clause considered provided that “if [the grantor/lessor]...should desire to sell..., she shall, before concluding any sale, offer the leased premises” to the holder/tenant “at the same price and upon the same terms and conditions as she is prepared to sell the leased premises to any *bona fide* purchaser.” The statements of the court relating to the construction of the right of pre-emption were *obiter*, as the decision turned on the fact that the grantor could not be said to have manifested a desire to sell during the currency of the lease. This was also pointed out in *Hirschowitz v Moolman* 1985 3 SA 729 (A) 760G-H.

Quoting *Van Pletzen v Henning*,<sup>6</sup> Botha JA held that a right of pre-emption does not normally impose any enforceable obligation upon the grantor of the right, but merely restrains the grantor from selling to a third party, save under the conditions prescribed in the agreement.<sup>7</sup> The obligation imposed to offer to the holder under certain circumstances is not an enforceable one, but merely refers to the means or method whereby the property may be freely sold.<sup>8</sup> Botha JA concluded that *before* a sale by the grantor, the holder may not compel a sale to himself.<sup>9</sup> He held that no procedure is known to our law whereby the holder could in the event of a sale in conflict with his rights, demand that he be allowed to step into the buyer's place.<sup>10</sup>

Botha JA did not specifically pronounce on whether a grantor could be ordered to make an offer once he did conclude a sale with a third party. He unfortunately also did not state specifically whether the grantor would after a sale be under threat of an interdict or a claim for damages only. His statement that the obligation imposed under certain circumstances to make an offer is merely a means whereby the property can be freely sold, would, however, appear to cover the situation where the grantor sells the property to a third party.<sup>11</sup>

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<sup>6</sup> 1913 AD 82.

<sup>7</sup> 321F-G.

<sup>8</sup> 323G-H.

<sup>9</sup> 322H-J.

<sup>10</sup> 323E.

<sup>11</sup> This is how Van Heerden AJA in *Oryx* (at 905A) and Corbett JA in *Hirschowitz v Moolman supra* (at 760A) interpreted his view. It may perhaps be argued that Botha JA did not exclude the possibility that the holder would have a positive remedy upon the grantor actually contracting with a third party, although this is how the majority decision is generally understood. In his discussion of the *ius commune* texts on *naastingsrechte*, Botha JA emphasised that none of these texts grants the holder the right to obtain the object before conclusion of a contract with a third party. This suggests that Botha JA does not totally exclude the possibility of a positive remedy upon a sale in breach of the preference contract. On the other hand, his statement that *Van Zutphen* wrongly imported, in relation to a conventional *voorkeopsreg*, the legal position under the Dutch law of *naesting* or the legal *ius retractus*, suggests that he disagrees with the view that the holder might ever be entitled to performance on the terms agreed with the third party.

This viewpoint may be interpreted to mean that an order for specific performance, in the form of an order that the grantor must make an offer, can never be obtained.<sup>12</sup> This would be so simply because there never is an enforceable obligation upon the grantor to make an offer. Once a contract is concluded with a third party, the holder may only interdict the grantor and third party from giving and taking transfer. The grantor does not then have to make an offer to the holder. Even if he transfers to a *mala fide* third party, the holder may be able to have the transfer set aside, but not to oblige the grantor to make an offer. The grantor may thereafter simply retain the property. In this manner, the grantor may come to realize that the only means of escaping the restriction on his capacity to alienate is to make an offer to the holder. The holder can never become a purchaser through his own declaration or through an order of court directing the grantor to make an offer or to deliver the object. Only if the grantor voluntarily makes an offer to the holder can the holder become a purchaser by its acceptance. The right of first refusal merely confers on the holder “a weapon which may or may not...persuade the grantor to offer to sell to him.”<sup>13</sup> In other words, according to the majority view in *Owsianick*, the grantor only ever has a negative obligation, an *obligatio non contrahendo cum tertii*.<sup>14</sup> This obligation is subject to a resolutive condition, namely that the holder should reject an offer to contract by the grantor. The grantor can therefore not be forced to make the offer by the court, but making the offer is the only way in which he would be released from the *obligatio non contrahendo cum tertii*.<sup>15</sup>

This interpretation of Botha JA’s view implies that he would not regard the holder’s right as subject to the condition that the grantor should wish to sell. The nature of the right does not change before or after the grantor decides to sell: it remains an entitlement to a *non facere* and nothing more. The occurrence of “the trigger event,” if it amounts to a

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<sup>12</sup> See also Lubbe 1982 *Annual Survey* 129; Du Plessis *Spesifieke nakoming* 12.

<sup>13</sup> In the words of advocate O’Donovan, *Bellairs v Hodnett* 1978 1 SA 1109 (A) 1113.

<sup>14</sup> An obligation not to contract with third parties.

<sup>15</sup> This point is laboured here as Botha JA’s statement that the making of an offer is merely intended as a means whereby the property concerned may be freely sold, has been described as “so obscure, with respect, that it is not clear what the learned judge intended to convey....” (Cooper *Landlord and Tenant* 144).

breach, merely gives rise to the normal remedies for enforcing a negative duty, that is, a prohibitory interdict or damages.

It is submitted that Botha JA's construction is not meaningless from a practical or commercial perspective. The balance of bargaining power in a particular case could very well result in the grantor agreeing only to be subject to an interdict or damages claim in case of breach (or the setting aside of a transfer to a *mala fide* third party).<sup>16</sup> The holder might also be satisfied with such an arrangement. In any event, regardless of the construction followed, there is always a danger that the grantor may sell and transfer to a *bona fide* third party, so that only damages may be claimed. No one contends that to restrict relief to a claim for damages in such a situation makes no commercial sense. If the holder discovers in time that the grantor has concluded a sale and intends to transfer, or has transferred to a *mala fide* third party, an interdict (and an order setting aside the transfer) will adequately restore the *status quo*, a solution that makes practical sense.

The negative construction does not make of the holder's right something other than a "right of first refusal" or a "right of pre-emption". Although not enjoying a conditional right to purchase, the holder still has a preferential right: he must be preferred above any other potential purchaser by the grantor. A "preference" implies a negative: the non-selection of others, but does not necessarily indicate when and how a selection must take place. The construction is therefore not "illogical". Neither does logic dictate that "'refusal' imports an offer",<sup>17</sup> from which a duty to make an offer is to be inferred. As was stated by Botha JA in *Soteriou v Retco Poyntons*,<sup>18</sup> "a right of first refusal" could

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<sup>16</sup> Or a third party who did not know about a right of pre-emption in company statutes (*Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 4 SA 15 (SCA)).

<sup>17</sup> As was held in *Manchester Ship Canal Company v Manchester Race Course Company* [1901] 2 Ch 37 (CA). This statement was relied on by the majority in *Soteriou v Retco Poyntons* 1985 2 SA 922 (A) 932G. The court in *Cohen v Behr* 1946 CPD 942 was also influenced by this reasoning as appears from 946-948. See also Flack 2001 *SALJ* 842 834 and Du Plessis *Spesifieke nakoming* 17, who accept this statement as a truism.

<sup>18</sup> *Supra*.

also refer to the first chance to refuse any voluntary offer which the grantor may, but is not obliged to make.<sup>19</sup>

The construction of a right of pre-emption would be very simple and not give rise to theoretical problems if the view of Botha JA should be accepted as the only correct one.<sup>20</sup> It also accords with the policy consideration that restraints on alienation must be narrowly construed, as too many restrictions on an owner's capacity to alienate are not in the interest of commerce.<sup>21</sup>

However, the cases relied upon by Botha JA arguably do not support his position. In *Sher v Allen*,<sup>22</sup> for instance, the court specifically stated that the holder was entitled to an offer by the grantor.<sup>23</sup> The decision in *Van Pletzen v Henning*<sup>24</sup> turned on the fact that the grantor had not attempted to sell to anyone else. Therefore, the nature of the duty on the grantor could not have changed in any event from a mere negative one as no trigger event had occurred. The court did state *obiter* that it is for the holder to make an offer, which

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<sup>19</sup> See the minority judgment of Botha JA at 936B-C, approved of by Radesich 1985 *De Jure* 407 408-410. Du Plessis *Spesifieke nakoming* 17 therefore incorrectly states that no objection had been made against the conclusion reached by the majority in *Soteriou* that "refusal imports an offer." In the *Manchester* case, the holder was in any event merely granted an interdict to protect his right. Cf Siviglia's comment on the term "right of first refusal": "Some agreements merely state that one party will have a 'right of first refusal', but standing alone, that term has little, if any, meaning. Certainly, in this spare form, it is an invitation to dispute. If an agreement must contain a right of first refusal, the mechanics of the right should be clearly stated." ("Helpful Practice Hints: Rights of first refusal" 1994 *New York State Bar Journal* 56).

<sup>20</sup> Reinecke & Otto 1986 *TSAR* 18 20.

<sup>21</sup> As confirmed at 321E of the judgment, relying on Voet 18 3 9 – 18 3 10 and *Robinson v Randfontein Estate Gold Mining Co Ltd* 1921 AD 168 188. See also Mostert *et al Die Koopkontrak* 277. Cf Van der Merwe *Sakereg* 70 and 80.

<sup>22</sup> 1929 OPD 137, referred to by Botha JA at 321F-G.

<sup>23</sup> 143. The court in *Sher v Allen supra* primarily relied on *Manchester Ship Canal Company v Manchester Racecourse Company supra* in favour of its view that the grantor has a duty to make an offer (142). Whether the *Manchester* case provides authority for this view, will be investigated in par 4 2 *infra*.

<sup>24</sup> *Supra*, referred to by Botha JA at 321F-G.

the grantor must prefer to that of any other buyer.<sup>25</sup> By implication, the grantor is not compelled to accept the holder's offer, but may just not accept a similar or lower offer by a third party. However, the court did not pronounce on the holder's remedy if the grantor sold without allowing the holder to submit an offer. The possibility that the holder may then be entitled to become a purchaser was not discussed and therefore not ruled out by the court. It does, however, appear from these cases that opposing formulations of the nature of the grantor's right predate the *Owsianick - Oryx* saga.

Whether *SA Breweries v Francis & Sons*<sup>26</sup> constitutes authority for Botha JA's statement that the Dutch law of *naasting* is not part of the modern law is also questionable. This aspect and Botha JA's interpretation of the Roman-Dutch sources will be investigated further in the next chapter.

## **2 1 2 Hartsrivier Boerderye v Van Niekerk**

The court here regarded the essence of a right of first refusal to be that the grantor obliges himself not to sell to another, unless the holder has been granted a reasonable opportunity and nevertheless did not offer to buy.<sup>27</sup> It does place a positive duty on the grantor, in the sense of requiring her to give notice that she wants to sell.<sup>28</sup> If the holder does submit an

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<sup>25</sup> 95.

<sup>26</sup> 27 NLR 648.

<sup>27</sup> 1964 3 SA 702 (T) 705H. At 706A De Vos J stated that, "Die verskyningsvorme kan wissel". However, his pronouncements on the right of first refusal in general show that he regarded it as a uniform concept, especially in the light of the general wording of the clause. Perhaps he intended to allow only for express deviations in the rights and duties of the parties. The clause simply provided that if the grantor should decide to sell the land, the holder shall possess the first right of refusal to purchase. The grantor had given the holder notice of his intention to sell. At issue was whether the period fixed by the grantor in which the holder should convey whether he wishes to buy was a reasonable one and whether an oral indication that he wanted to buy was sufficient.

<sup>28</sup> 706B.

offer, the grantor is free to reject it, but then forfeits his right to sell to a third party.<sup>29</sup> The holder thus has a right to make an offer, not a right to buy.<sup>30</sup>

The offer by the holder must be a valid one, complying with any prescribed formalities.<sup>31</sup> Otherwise, the seller would be precluded from selling to another even though he is not yet able to conclude a binding contract with the holder.<sup>32</sup> The court considered this to unfair to the grantor.<sup>33</sup>

Certain aspects of this construction are unclear. The holder's remedies should the grantor fail to give notice of his intention to sell were not mentioned.<sup>34</sup> The court thus did not rule out the possibility that the grantor may be ordered by way of an order for specific performance to furnish such notice. The question also remains whether the grantor is only prohibited from selling to a third party at the same or lower price than that offered by the holder. Thus the question remains whether the grantor may immediately upon rejection of the holder's offer sell to a third party at a higher price than that offered by the holder, without first giving notice to the holder of her intention.

Assuming that specific performance is not available upon breach of the preference contract, this construction does not differ drastically from that proposed by Botha JA. In terms of both approaches, the grantor cannot be compelled to make an offer on manifesting a desire to sell. The grantor may however be interdicted from selling and giving transfer to a third party should he have failed to notify the holder of the intention to sell before doing so. If the grantor makes no offer to the holder or rejects the holder's offer the effect will be the same: the grantor may not sell to the third party.

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<sup>29</sup> 707C.

<sup>30</sup> *Ibid.*

<sup>31</sup> 706H.

<sup>32</sup> *Ibid.*

<sup>33</sup> *Ibid.*

<sup>34</sup> On the facts such notice was given.

Because of the unclear aspects of *Hartsvivier*, it is difficult to say which approach takes the more restrictive view of the grantor's duties. *Prima facie*, the *Hartsvivier* approach appears to leave the grantor more freedom to deal with her property. If the grantor is set on selling to an outsider and not to the holder, the grantor could test the holder's attitude without binding herself. The grantor must simply give notice to the holder of her intention to sell and may then freely reject the holder's offer and lose the chance of selling to the third party at that price. In terms of Botha JA's approach, if the grantor is set on selling to an outsider, she must first submit an offer reflecting the terms on which she is prepared to sell to the holder, and in so doing, take the risk that the holder might accept such offer. A grantor who does not wish to sell to the holder at all, would thus rather breach the agreement of pre-emption by selling to the third party without any offer to the holder. The *Hartsvivier* approach is thus perhaps preferable as it makes a breach of the grantor's duty less tempting. However, if the court in *Hartsvivier* foresaw the possibility of an order that notice of intention to sell be given on breach, the *Hartsvivier* approach could be said to place a positive duty on the grantor.

Authority for the court's approach can be found in Voet 18 3 10, where he says that "if the buyer has covenanted with a stranger for the sale of the property at a definite price, he ought to give *notice* of that fact to the original seller, so that, if the latter so thinks good, he may within two months of the *notice* make it clear that he wishes to hold the property as bought for the same price."<sup>35</sup> In *Van Pletzen v Henning*,<sup>36</sup> an *obiter dictum* of Innes JA also suggests that a right of pre-emption compels the grantor to prefer the holder's offer above that of any other buyer if he decided to sell.<sup>37</sup>

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<sup>35</sup> Gane's translation (my italics). The court in *Sher v Allen* used "intimate" and "intimation" instead of "notice" in its translation.

<sup>36</sup> *Supra* at 95.

<sup>37</sup> Moreover, according to *Sher v Allen supra* 142-143, the grantor must lay before the holder "by his written *notice* something in respect of which his (so-called) option – his ... first refusal – shall operate." (My italics.) However, the court rejected the view that the right of pre-emption means no more than that the holder should have the first right to make an offer (at 142).

Remarkably, the court in *Hartsrivier* simply ignored several preceding cases in which it was stated that the *grantor* must make an offer.<sup>38</sup>

## **2 2 A positive duty enforceable by an order that an offer be made**

In a minority decision in *Owsianick v African Consolidated Theatres*,<sup>39</sup> Ogilvie Thompson JA concluded that the grantor has a duty to make an offer to the holder on the occurrence of the trigger event. This duty is, subject to the normal discretion of the court in this regard, enforceable by an order for specific performance in the form of an order that an offer be made.<sup>40</sup>

In a separate minority judgment in the same case, Williamson JA pointed out that Ogilvie Thompson JA's view is the logical result of the approach confirmed at that stage in *Haynes v Kingwilliamstown Municipality*,<sup>41</sup> namely that specific performance should in principle be available as a remedy in respect of a duty to act positively, and that this implies an order that the defendant be ordered to carry out "precisely what he had bound himself to do...."<sup>42</sup>

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<sup>38</sup> See *Sher v Allen supra* 143 and *Cohen v Behr supra* 942 (both cases relying on *Manchester Ship Canal Co v Manchester Racecourse Co supra*) and *Le Roux v Odendaal* 1954 4 SA 432 (N) 441G-H. However, specific performance of the duty to make an offer was not ordered in any of these cases.

<sup>39</sup> *Supra*.

<sup>40</sup> 320H-321A.

<sup>41</sup> 1951 2 SA 371 (A).

<sup>42</sup> *Owsianick* case at 327B-E. This principle was subsequently affirmed in cases like *Benson v SA Mutual Life Assurance Society* 1986 1 SA 776 (A) 783. Ogilvie Thompson JA therefore implicitly views the absence of orders for specific performance in earlier cases not as confirmation of Botha JA's contrary construction, but rather as the reflection of the influence on our law at that time of the English view on the availability of this remedy.

The climax of Ogilvie Thompson JA's argument was the decision in *Le Roux v Odendaal*,<sup>43</sup> but his view that specific performance of the right of pre-emption had been granted in that case, is incorrect. The plaintiff in *Le Roux's* case had in fact accepted a voluntary offer by the grantor and obtained specific performance of the contract of sale.<sup>44</sup> Ogilvie Thompson JA thus took out of context the statement in *Le Roux* that "the holder is by due exercise of his right entitled to become a purchaser."<sup>45</sup> It is submitted that on the facts the "due exercise of the right" referred to the scenario that the grantor had duly (and therefore voluntarily) made an offer to the holder who had thereafter exercised his right by accepting it. It cannot be concluded from this statement that the court was of the view that the holder would be automatically entitled to make himself a purchaser (whether by court order or unilateral declaration) in the absence of a voluntary offer by the grantor.

The apparently forgotten case of *Engelbrecht v Mundell's Trustee*<sup>46</sup> does, however, provide support for Ogilvie Thompson JA's approach. The court in *Engelbrecht* accepted that it could grant specific performance of a right of pre-emption in the form of an order "to sell", although such an order was eventually not granted.<sup>47</sup> In *Lindner v National Bakery (Pty) Ltd*<sup>48</sup> the court stated *obiter* that a holder may compel a grantor who has concluded a sale with a third party to submit to him the offer so accepted.<sup>49</sup> Neither of these decisions was apparently referred to in subsequent cases.

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<sup>43</sup> *Supra*, quoted and applied by Ogilvie Thompson JA at 320D-G.

<sup>44</sup> 320G.

<sup>45</sup> 442F.

<sup>46</sup> 1934 CPD 111.

<sup>47</sup> 119. The court declined to order specific performance in the absence of the bondholders with an interest in the property.

<sup>48</sup> 1961 1 SA 372 (O).

<sup>49</sup> 381F. The grantor was not in fact ordered to make an offer: a prayer that the grantor must furnish a notice setting out the terms of any offer received was not granted. The reason for refusing this order was merely that the offer would amount to the disposal of the whole or greater part of the assets of the grantor company, which required approval of the "company in general meeting" (s 70 of the Companies Act 46 of 1926). The court held that the company had a duty to seek to obtain such a resolution from its

By confirming the possibility of an enforceable duty to make an offer, Ogilvie Thompson JA recognises that a party might stipulate for a right of pre-emption precisely in order to acquire the property in question as soon as the grantor is willing to sell. For example, a person who wishes to obtain the land adjoining hers, but who is only able to obtain a right of pre-emption from the neighbour, has an interest in acquiring the property when the neighbour concludes a contract of sale with an outsider in breach of his duty. It can be argued that such an interest would not be served adequately by an interdict or claim for damages alone.

### **2 3 A positive duty enforceable by the Oryx mechanism**

*Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd*<sup>50</sup> was the first reported decision in more than a hundred years in which a holder was actually declared to be entitled to obtain the property on exercising his right of pre-emption.<sup>51</sup>

The language used to describe the holder's remedy is couched in the terms of the Germanic *naastingsreg*: the holder may, upon a sale in breach of his right, step into the place of the third party by a unilateral declaration of will.<sup>52</sup> To avoid the impression that it was the intention to deprive the third party of the benefits of a valid contract of sale,

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shareholders. Until it obtained such a resolution it could not be compelled to submit an offer to the holder, but it also could not sell its assets to another. Counsel for the grantor apparently did not argue the construction of a right of pre-emption. The court's only authority for its "positive" construction was *D 18 1 7 5*, *D 19 1 21 5* and Holmes *Mackeurtan on Sale* (3rd edition) 83. As pointed out in n 73 of par 1 2 *supra*, the latter work does not discuss the availability of a remedy of specific performance if the grantor does not in fact offer to contract with the holder before selling to a third party. Accordingly, it does not provide support for the court's construction. Whether the two Digest texts support the construction will be investigated in the next chapter.

<sup>50</sup> 1982 3 SA 893 (A).

<sup>51</sup> See the discussion of *Malan v Schalkwyk & Odendaal* 1 S 225 (decided in 1852) at n 59 below.

<sup>52</sup> 907F. See further the discussion of the historical development of our law in the next chapter.

namely a claim for damages, the court later clarified its description of the remedy. The holder's unilateral declaration brings an independent contract into existence between herself and the grantor on the same terms as agreed with the third party.<sup>53</sup>

Van Heerden AJA (as he then was), who delivered the majority judgment, expressed grave doubts as to whether a court could order a seller who acted in breach of a right of pre-emption to make an offer to the holder; that is, to grant an order of specific performance of the holder's right in the traditional sense.<sup>54</sup> He also questioned whether a court has a discretion in respect of what has come to be known as the *Oryx* mechanism.<sup>55</sup> Unfortunately, no reasons were given for these reservations.

The remedy proposed by the court plus specific performance of the contract of sale created by the holder, provide a speedy, effective remedy for the holder who wishes to acquire the property.

Although it thus appears that Van Heerden AJA did not consider the court's sanction to be necessary for the creation of the contract of sale by the holder, the *Oryx* mechanism as an extra-judicial remedy does not, as some believe, deprive courts of all power to deny the holder the ability to acquire the property in the interests of justice.<sup>56</sup> Once the holder has extra-judicially created a contract of sale by way of the *Oryx* mechanism, a refusal by the grantor to transfer or deliver the property may result in a claim for specific performance of the contract. The court then has a discretion to refuse the order for transfer. If the court should in addition have a discretion to decide whether a contract of

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<sup>53</sup> 919D.

<sup>54</sup> 919H.

<sup>55</sup> 913E-G. The minority (per Botha AJA, Hoexter JA concurring) disagreed with him on this point. See n 46 in par 1 *supra* on the term "*Oryx* mechanism."

<sup>56</sup> See Eiselen's criticism of the case at 1986 *THRHR* 95 99 and Du Plessis *Spesifieke nakoming* 57-58. Cf Floyd 1986 *THRHR* 253 267. What Floyd 1986 *THRHR* 253 proposes at 265 as "'n verkorte vorm van spesifieke nakoming" appears to refer to the *Oryx* mechanism itself, thus a unilateral declaration by the holder that he wishes to be bound, but exercised under supervision of the court. See also the last paragraph on 267. This also appears to be what Van der Merwe *et al* proposes at 68 *in fine*.

sale should come into existence in the first place, it may have to exercise essentially the same discretion twice over. The practical effect of the court refusing to grant specific performance at either of the two stages would be the same. Damages would be granted on the basis of what the holder's position would have been had he obtained delivery of the property.

However, Van Heerden AJA's approach is problematic, as the authorities he relied upon do not provide clear support for the existence of the remedy. The Roman-Dutch and Roman law sources considered by Botha JA in *Owsianick* were understood in a different sense, and no attempt was made to counter Botha JA's statement that the Dutch law of *naasting*, relied upon by Van Heerden AJA, is not part of the modern law. These aspects will be examined in the next chapter (on the historical development of our law). The court also wrongly relied on the minority judgment of Ogilvie Thompson JA in *Owsianick* in support of the *Oryx* mechanism.<sup>57</sup>

Whether German and US law indeed supports Van Heerden AJA's interpretation of preference contracts will be investigated later.<sup>58</sup>

## **2 4 A positive duty enforceable by a short-circuited order for specific performance?**

In *Malan v Schalkwyk & Odendaal*,<sup>59</sup> apparently never referred to in subsequent decisions, the court held the contract between the grantor and the third party was null and

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<sup>57</sup> More specifically, insofar as it is suggested (at 904A-B) that Ogilvie Thompson JA had been of the opinion that the holder obtains a claim over the *merx* as soon as the condition, which lends only latent operation to the right of pre-emption was fulfilled. See also the discussion in par 1 1 and Reinecke & Otto 1986 *TSAR* 18 20 n 17.

<sup>58</sup> Chapter 4 *infra*.

void and ordered that the holder “become entitled to and become possessed [of the land]; he...paying [to the third party] the original purchase price and the value of the improvements, if any.”

It appears that the court disregarded an order that an offer be made on breach, and immediately granted an order for the performance of the contract of sale which would have existed had the land been duly offered to the holder. An order that the grantor be ordered what he had agreed to do, to make an offer, was therefore bypassed or short-circuited.

Similarly, in *Dithaba Platinum v Erconovaal*<sup>60</sup> the court immediately granted an order for the *transfer* of the mineral rights to the holder on a sale thereof to a third party. The court did this after stating that the main feature of a right of first refusal is that the grantor must make an offer to the holder,<sup>61</sup> and thereafter holding that the *Oryx* case confirmed that specific performance of a right of pre-emption can be ordered.<sup>62</sup> If the order actually made is what the court intended by specific performance of the duty to make an offer under the pre-emptive right, it was a short-circuited order as well.

Such a short-circuited order makes practical sense in cases where the grantor clearly does have a duty to make an offer: the court is aware of the grantor’s refusal to make an offer, and also knows that the holder is desirous of acquiring the property; otherwise the parties would not be in court. To leave it at that appears unfair, as the grantor had at the conclusion of the agreement promised to make an offer. To order him to make one now would just waste time. The grantor might still refuse to do so, forcing the holder to approach the court again to obtain another, equally ineffective order that he does so. To

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<sup>59</sup> 1 S 225 (decided in 1852). The clause provided that should the grantor (the buyer) incline to part with the land, he would “give” it to the holder (the seller) for the original purchase price plus the value of the improvements.

<sup>60</sup> 1985 4 SA 615 (T).

<sup>61</sup> 623E-F.

<sup>62</sup> 627D-E.

rather authorise an official such as the sheriff to make an offer would make as much sense as the judge (also a public official) making such an offer. Practically the court may therefore just as well enforce the agreement of pre-emption by immediately ordering transfer.

The “verkorte vorm van spesifieke nakoming” referred to by Floyd<sup>63</sup> appears to differ from what is here termed a “short-circuited” order aimed directly at transfer. Floyd does not expressly state that what he is referring to is designed not only to enable the holder to establish a substantive contract, but is also directed at an order that the grantor must transfer or deliver the property. Moreover, he appears to limit this “shortened form” of specific performance to situations in which the holder is entitled, willing and able to agree to the exact terms agreed with the third party. He does not regard the “shortened” specific performance as a substitute for specific performance in the traditional sense: he clearly foresees situations in which a remedy of “shortened” specific performance would not be available, for example when the contract of pre-emption also entitles the holder to buy should the grantor exchange or donate the property.<sup>64</sup> The short-circuited specific performance identified here rather envisages the holder being able to approach the court directly on breach, the court determining in one step the terms of the offer which the grantor should have made to the holder and then ordering that transfer should take place provided the holder tenders performance according to those terms. It makes no difference whether the contract of pre-emption entitles the holder to obtain the property on the same terms agreed with the third party or on different terms. Availability of such a remedy therefore precludes the need for an order for specific performance in the ordinary

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<sup>63</sup> 1986 *THRHR* 253 265 *et seq.* See n 56 above.

<sup>64</sup> 268 at n 155, which refers back to n 145. In another situation referred to in n 145, namely when personal terms form a substantial part of the contract with the third party, the holder would arguably not be entitled to any form of specific performance unless the pre-emption contract specifically provided for the terms on which the holder may buy in such a situation. Floyd’s interpretation of *Bellairs v Hodnett supra* in the same footnote, namely that the grantor may freely determine the terms of the offer to the holder, is problematic: the decision in that case was ultimately based on the interpretation that in such a case the parties intend that the offer to the holder should be in similar terms as that agreed with the third party. A short-circuited order for specific performance as described here would then be apposite.

sense.<sup>65</sup> The holder does not first have to bring a contract into existence by a unilateral, extra-judicial declaration before approaching the court, nor is the court's order directed merely at sanctioning a declaration by the holder that he wishes to be bound by the terms agreed with the third party.

Practically the effect of such a short-circuited approach is the same as that followed in the *Oryx* case, resulting in an order for performance of the contract of sale, not of the contract of pre-emption. Under the *Oryx* mechanism, however, the court need not skip or short-circuit a step; the holder has a power to bring a contract of sale into existence extra-judicially, before the court is approached. If, in terms of either of the two approaches, an order for specific performance is refused, the holder would be granted damages on the same basis, namely the position he would have been in had he obtained transfer compared with the position he is in now.

There appears to be very little authority for a short-circuited approach. No reasons for the decision in the *Malan* case were reported,<sup>66</sup> and the order in *Dithaba Platinum v Erconovaal* was apparently based on a wrong interpretation of the *Oryx* case.<sup>67</sup> An interesting aspect of the *Malan* case is that the holder as original seller had not yet given transfer under the contract of sale. Perhaps it could therefore be argued that the court's order amounts to cancellation of the contract of sale and restoration of the *status quo ante*

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<sup>65</sup> However for this short-circuited remedy to be of value to a holder who does not know the terms of the agreement with the third party, it should be coupled with an enforceable duty on the grantor to give notice of the terms of any agreement entered into with a third party. See Voet 18 3 10 discussed at n 35 above.

<sup>66</sup> It can perhaps be argued that the order in *Malan's* case simply follows the pattern of the remedy which the holder of a *naastingsreg* had: the holder stepped into the third party's contract but had to pay the purchase price to the third party. However that does not explain the court's order that the contract with the third party is null and void.

<sup>67</sup> Compare the text at n 62 with that at n 54 *supra*. However, the court in *Oryx* did give some indication that it might consider the *Oryx* mechanism to be "specific performance in the wide sense". At 919A the court stated that "indien ek 'n wye diskresie sou hê om nie 'n bevel gemik op spesifieke nakoming, in die breë sin, te verleen nie, ek...dit nie ten gunste van die respondente sou uitoefen nie."

as a result of the breach of the contract of sale containing the term of pre-emption, instead of specific performance of the agreement of pre-emption

If the effect of *Malan* and *Dithaba* is in fact that a holder can obtain specific performance of his right of first refusal by way of a short-circuited order to transfer, this is in conflict with *Van der Hoven v Cutting*,<sup>68</sup> where the court stated that if the holder were able to obtain specific performance of his contract of first refusal, he would obtain not the land, but merely the first refusal or right to purchase.<sup>69</sup>

## 2 5 Conclusion

An overview of the various constructions of rights of pre-emption reveals that each approach has some merit. The tendency to portray one approach as the only correct one to the exclusion of all other views results in tension and confusion, all the more because of the failure to investigate the relevant policy considerations comprehensively.

The breakdown of the system of precedents which occurred time and again as wrong interpretations of previous decisions were relied upon and contrary decisions were disregarded, adds to the confusion. Moreover, pronouncements on the nature and enforceability of the grantor's duty in the two leading decisions, *Owsianick* and *Oryx*, may be argued to constitute *obiter dicta*.<sup>70</sup> In neither case was full argument heard on these issues.<sup>71</sup>

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<sup>68</sup> 1903 TS 299.

<sup>69</sup> 315.

<sup>70</sup> This is undisputedly true in the case of *Owsianick*. See n 5 *supra*. Williamson JA's criticism that the court should never have considered the question of enforcement of the grantor's duty was probably a cogent one. He pointed out that this matter was raised only on appeal, with argument heard from one side only, which argument did not cover all the Roman-Dutch authorities. In the *Oryx* case both counsel

As the controversy regarding the holder's remedies turns to some extent upon the interpretation of the Roman and Roman-Dutch sources and the question whether certain rules expounded by the old authorities were received into our law, the historical sources of our law will be examined next. The study will also seek to establish whether the plurality of approaches in our case law can be explained by the historical development of the law on rights of pre-emption.

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agreed that the holder may lay claim to the *merx* after a sale in breach of his right, as Van Heerden AJA pointed out at 904D.

<sup>71</sup> *Ibid.*

## 3 Historical perspective

### 3.1 Introduction

The construction of preference arrangements in Roman law will be investigated to evaluate Van Heerden AJA's reliance on Roman law texts in support of the *Oryx* mechanism<sup>1</sup> and to establish what rules of Roman law were received in Roman-Dutch law.

Because the concept of *naasting* (or *naesting*), or *ex lege* rights of retraction, which crops up in the two leading cases, is of Germanic origin, the position in Germanic law before the reception will also be considered.<sup>2</sup> The majority of the court in *Owsianick* maintained (per Botha JA) that the Roman-Dutch construction of contractual preference arrangements differed from that of the Germanic *ex lege* right of retraction,<sup>3</sup> whereas in *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd*<sup>4</sup> the self-same texts were read as favouring the opposite view.<sup>5</sup> Ogilvie Thompson JA in *Owsianick* also relied on historical sources to support his view that specific performance may be granted.

The deference to the old sources in the two leading cases assumes that the Roman-Dutch position on preference contracts is of decisive importance for the law of today. The

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<sup>1</sup> *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd & Andere* 1982 3 SA 893 (A) 905E-G. See paras 1.1 and 2.3 *supra*.

<sup>2</sup> See generally, Zimmermann "Kaufvertrag" in Feenstra & Zimmermann (eds) *Das römisch-holländische Recht: Fortschritte des Zivilrechts im 17. und 18. Jahrhundert* (1992) 144-191 *et seq*; De Blécourt & Fischer *Kort Begrip van het Oud-Vaderlands Burgerlijke Reg* 7<sup>th</sup> edition (1967) 97 *et seq*; Moorman van Kappen *Met open buydel en in baren gelde* (1973) 39; Schurig *Das Vorkaufsrecht im Privatrecht - Geschichte, Dogmatik, ausgewählte Fragen* (1975) 37 *et seq*.

<sup>3</sup> *Owsianick v African Consolidated Theatres (Pty) Ltd* 1967 3 SA 310 (A) 321H-322F.

<sup>4</sup> *Supra*.

<sup>5</sup> 907B-D.

consideration of *ius commune* authorities outside Holland in the two leading cases is in conflict with the narrow historical method that claims that our common law is the law applied in Holland at the height of its development.<sup>6</sup> According to this view, a court faced with conflicting possible interpretations of a legal rule should endeavour to establish what the correct legal position was in Holland with reference to the broader *ius commune*.<sup>7</sup>

There is support for the view that our courts take a broader European perspective not merely as indirect evidence to establish the law of Holland, but more directly because the legal tradition transplanted was a supra-national one, a *ius commune*.<sup>8</sup>

Moreover, our courts do not consistently lay down that the opinions of old authorities from the province of Holland should necessarily outweigh those from other Dutch provinces and other countries.<sup>9</sup> Indeed, courts have sometimes been willing to accept rules formulated by writers from other countries in the face of acknowledged opposition to those rules by writers of Holland, often on the basis of “fairness” and “sound reason.”<sup>10</sup>

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<sup>6</sup> See, for example, the concurring judgment of Corbett JA in *Du Plessis v Strauss* 1988 2 SA 105 (A) 149 *et seq.* Cf the comments of Van Heerden JA in the same case at 133. See also the judgment of Van den Heever JA in *Tjollo Ateljees (Eins) Bpk v Small* 1949 1 SA 856 (A) 865 and his judgment in *Gerber v Wolson* 1955 1 SA 158 (A) 170 *et seq.* See also *Sishen Hotel (Edms) Bpk v Suid Afrikaanse Yster en Staal Industriële Korporasie Bpk* 1987 2 SA 932 (A) 950E. Cf Fagan “Roman-Dutch Law in its South African Historical Context” in Zimmermann & Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 33 41 *et seq.*

<sup>7</sup> *Ibid.*

<sup>8</sup> Hahlo & Kahn *The South African Legal System and its Background* (1968) 562 *et seq.*; Zimmermann “Synthesis in South African Private Law: Civil Law, Common Law and *Usus Hodiernus Pandectarum*” 1986 *SALJ* 103 268; Fagan “Roman-Dutch Law” 45; Van der Merwe “The Roman-Dutch law: From Virtual Reality to Constitutional Resource” 1998 *TSAR* 1 7.

<sup>9</sup> Fagan “Roman-Dutch Law” 41 *et seq.*; Lubbe 1997 *Zeitschrift für Europäisches Privatrecht* 428 429-430 and cases there cited. Cf Zimmermann “Roman Law in a Mixed Legal System: The South African Experience” in Evans-Jones (ed) *The Civil Law Tradition in Scotland* (1995) 41 *et seq.*, 62 *et seq.*

<sup>10</sup> See eg *Kroonstad Westelike Boere Koöp v Botha* 1964 3 SA 216 (K) and *Gerber v Wolson* 1955 1 SA 158 (A), especially at 183A-184B per Fagan JA.

In fact, a number of decisions show that South African courts do not consider themselves immutably bound to follow the opinions of the old authorities.<sup>11</sup> Decisions often display a willingness to adapt common law institutions in the face of changing circumstances or views on public policy considerations and the dictates of equity.<sup>12</sup> The oft-quoted *dicta* of Sir James Rose Innes in *Blower v Van Noorden*<sup>13</sup> and Lord Tomlin in *Pearl Assurance Co v Union Government*<sup>14</sup> immediately springs to mind. Sir Rose Innes stated that:

“There come times in the growth of every living system of law when old practice and ancient formulae must be modified in order to keep in touch with the expansion of legal ideas, and to keep pace with the requirements of changing conditions. And it is for the courts to decide when the modifications, which time has proved to be desirable, are of a nature to be effected by judicial decision, and when they are so important or so radical that they should be left to the Legislature.”

To that, Lord Tomlin added that our Roman-Dutch common law “is a virile, living system of law, ever seeking, as every such system must, to adapt itself consistently with its inherent basic principles to deal effectively with the increasing complexities of modern organised society.”<sup>15</sup>

This provides support for the view that courts should not simply state a rule of law on the strength of historical authority, without considering whether the result accords with

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<sup>11</sup> Fagan “Roman-Dutch Law” 43-44; Lubbe “Legal History in South Africa: Reflections of a Non-Historian” 1997 *Zeitschrift für Europäisches Privatrecht* 428 429-430 and cases there cited. *Cf Meyer v The Master* 1935 SWA 3 9.

<sup>12</sup> Lubbe 1997 *Zeitschrift für Europäisches Privatrecht* 428 429-430.

<sup>13</sup> 1909 TS 890 905.

<sup>14</sup> 1934 AD 560 563.

<sup>15</sup> See also *Jajbhay v Cassim* 1939 AD 537 at 542; *Phame v Paizes* 418H - 419C; *Alpha Trust (Edms) Bpk v Van der Watt* 1975 3 SA 734 (A) 749D-E; Olivier JA in *Eerste Nasionale Bank v Saayman NO* 1997 4 SA 302 (A) 319 *et seq*; *Payen Components SA Ltd v Bovic Gaskets CC* 1994 2 SA 464 (W) 475H *et seq*; *Janse van Rensburg v Grieve Trust* 2000 1 SA 315 (C) 323 *et seq*. *Cf Minister of Justice v Hofmeyr* 1993 3 SA 131 (A) 157; *Willis Faber Enthoven (Pty) Ltd v Receiver of Revenue and Another* 1992 4 SA 202 (A) 220D - 221; *S v Graham* 1975 3 SA 569 (A) 576F.

modern needs and the values that modern law seeks to advance.<sup>16</sup> I agree that, in the face of judicial conflict on the construction of a legal figure or institution in the historical sources, historical research should not be aimed at speaking the final word on what the law was in the province of Holland at a certain time so as to dictate what the South African law is today.

Historical argument should be regarded rather as an avenue of approach to the legal problem, which may ultimately be solved differently to the historical position.<sup>17</sup> “[H]istorical argument involves a methodology in which texts are revitalised by means of a productive reinterpretation to produce results adequate to the needs of the times.”<sup>18</sup> In fact, the reception in Holland itself amounts to a selective, as opposed to a wholesale, adoption of rules from Roman law adapted to suit the requirements of the day.<sup>19</sup>

A thorough historical study of a legal institution or rule is also necessary to understand the reasons for its development and its underlying premises. Such understanding serves to test the rule’s compatibility with modern values or policy considerations and other established legal principles.

The purpose of this chapter is therefore not an exhaustive sociological-historical study in order to make a final pronouncement on how preference arrangements were understood

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<sup>16</sup> *Ex parte De Winnaar* 1959 1 SA 837 (N) 839. Van der Merwe “Ramus, Mental Habits and Legal Science” in Visser (ed) *Essays on the History of Law* (1989) 32 59; Lubbe 1997 *Zeitschrift für Europäisches Privatrecht* 428–435 and authorities there cited.

<sup>17</sup> Van der Merwe 1998 *TSAR* 1 14: “the function of Roman-Dutch law – it’s only function - is to provide lawyers with historically located arrangements and historically located conversations within a particular expression of the civilian tradition, that would enable them to indulge in a ‘sustained conversation about our arrangements.’” See also Visser “The legal historian as subversive or: Killing the Capitoline Geese” in Visser (ed) *Essays on the History of Law* (1989) 1 2 *et seq*; Lubbe 1997 *Zeitschrift für Europäisches Privatrecht* 428 434. Cf Thomas “*Fin de siècle* of funksionele Romeinse Reg” 1997 *THRHR* 202 212; Van der Merwe “Ramus, Mental Habits and Legal Science” 59.

<sup>18</sup> Lubbe 1997 *Zeitschrift für Europäisches Privatrecht* 428 432-3.

<sup>19</sup> Cf Schurig *Das Vorkaufsrecht* 37.

in Roman-Dutch law and the *ius commune* and what rules were received into our law. The emphasis will rather be on examining whether the texts selected by the judges in the two leading cases do indeed provide authority for their conflicting propositions according to traditional understandings of the theory of sources as well as to establish the reasons for the development of different constructions. This would serve to determine their compatibility with modern legal principles and policy considerations.

To these ends, the known Roman and Roman-Dutch texts on contractual preference arrangements and those of the *ius commune* writers relied upon in the leading cases will be considered. The old authorities from Holland will be considered separately from those from other areas to render the study more acceptable to proponents of the narrow definition of Roman-Dutch law.<sup>20</sup> Where relevant, reference will be made to modern writers on Roman law and the *ius commune*.

The historical researcher should be prepared to accept that there might very well not be any clear historical position. In such a case all the different possible interpretations must be treated as potential solutions or avenues of approach, to be evaluated in the light of modern policy considerations.

## **3 2 Roman Law**

Two fragments in the Digest of Justinian, *D 18 1 75* and *D 19 1 21 5*, deal with sales of land on condition that the buyer should not sell to anybody but the seller.<sup>21</sup> The latter text was relied upon in *Owsianick v African Consolidated Theatres (Pty) Ltd*<sup>22</sup> and *Associated*

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<sup>20</sup> As law is, at least to some extent, a “discourse of persuasion”, it seems sensible to use a strategy more likely to also persuade the traditionalists. (The terminology is that of Hutchinson, quoted by Van der Merwe “Roman-Dutch Law” 15). Cf Lubbe 1997 *Zeitschrift für Europäisches Privatrecht* 428 435 and Fagan “Roman-Dutch Law” 45 for indications that some kind of hierarchy of authorities may be useful.

<sup>21</sup> *D 18 1 75* (Hermogenianus) and *D 19 1 21 5* (Paulus). See n 32 and n 33 below for the full text.

<sup>22</sup> *Supra* 320A.

*South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd.*<sup>23</sup> Another text mentions an agreement between co-heirs that, if one of them should sell his part, it would be sold only to his co-heirs at a fixed price.<sup>24</sup>

Such preferential opportunities to buy were not only created by agreement. At the *venditio bonorum*, or sale in execution of a judgment debtor's estate, certain persons had the preferential opportunity to better the highest bid obtained.<sup>25</sup> In Justinian's time, the *emphyteuta* (quitrent holder) wishing to sell his *emphyteusis* (quitrent right) had to notify the owner of the terms of the proposed contract of sale. The owner could then declare his wish that the quitrent right be sold to him at the same price within two months.<sup>26</sup> Where a sale was concluded subject to the seller not receiving a better offer within a specified period, the buyer had the preferential opportunity to obtain the *merx* on the same terms as any better offer received in the absence of contrary agreement.<sup>27</sup>

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<sup>23</sup> *Supra* 905E-G.

<sup>24</sup> *D* 45 1 122 3 (Scaevola): "Coheredes cum praedia hereditaria diviserant, unum praedium commune reliquerunt sub hoc pacto, ut, si quis eorum partem suam alienare voluisset, eam vel coheredi suo vel eius successori venderet centum viginti quinque: quod si quis aliter fecisset, poenam centum invicem stipulati sunt: quaero, cum coheres mulier coheredis liberorum tutores saepius testato convenerit et desideraverit, ut secundum conventionem aut emant aut vendant, hique nihil tale fecerint, an, si mulier extero vendiderit, poena ab ea centum exigi possit. Respondit secundum ea quae proponerentur obstaturam doli mali exceptionem."

<sup>25</sup> *D* 42 5 16 (Gaius): "Cum bona veneunt debitoris, in comparatione extranei et eius, qui creditor cognatusve sit, potior habetur creditor cognatusve, magis tamen creditor quam cognatus, et inter creditores potior is, cui maior pecunia debetur." See also *D* 4 4 35 (Hermogenianus) which gives a minor who lost to a higher bid at an auction, the possibility of *restitutio* if he can show that the thing belonged to his ancestors, provided he is willing to pay the seller the difference between his own and the higher bid. ("Si in emptionem penes se collatam minor adiectione ab alio superetur, implorans in integrum restitutionem audietur, si eius interesse emptam ab eo rem fuisse adprobetur, veluti quod maiorum eius fuisset: ita tamen ut id, quod ex licitatione accessit, ipse offerat venditori").

<sup>26</sup> *C* 4 66 3. See Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* (1956) 15 for Baldus's gloss on this text.

<sup>27</sup> *D* 18 2 7 (Paulus): "Licet autem venditori, meliore allata conditione, addicere posteriori: nisi prior paratus sit plus adicere." *D* 18 2 8 (Paulus): "Necesse autem habebit venditor meliore condicione allata

These texts do not label such arrangements. The term *pactum protimeseos*, generally used by Romanists to describe an agreement granting a seller a preferential right to buy,<sup>28</sup> was apparently first used in a post-Justinian Greek novella.<sup>29</sup> For convenience' sake this term will be used to refer to such agreements.

Not much is known about the construction of the *pactum protimeseos* and the exact remedy available to the seller on breach.<sup>30</sup> The *pactum protimeseos* was not widely used as it did not form part of the *numerus clausus* of actionable agreements (*contractus*). If it was concluded ancillary to and simultaneously with a *contractus bonae fidei*, like *emptio venditio* (sale), it could be indirectly enforced by the action on the main contract – usually with the *actio venditi* (action on sale). It was thus recognised as a *pactum adiectum*, or ancillary pact.<sup>31</sup>

*D* 19 1 21 5 (Paulus) simply refers to the *actio venditi* being available on a sale to a third party, without stating precisely what may be claimed.<sup>32</sup> *D* 18 1 75 (Hermogenianus)

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priorem emptorem certiore facere, ut, si quid alius adicit, ipse quoque adicere possit.” This type of pact is known as an *in diem addictio*. Cf Schurig *Das Vorkaufsrecht* 22. See also Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 16 and Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht nach dem schweizerischen Zivilgesetzbuche* (1918) 6-7 who state that the buyer had the right to “step into” the better offer made by the third party.

<sup>28</sup> See eg ZimmErman *The Law of Obligations: Roman Foundations of the Civilian Tradition* (1990) 570; Kaser *Das Römische Privatrecht* 2<sup>nd</sup> edition (1971) 561 n 68.

<sup>29</sup> Peters *Die Rücktrittsvorbehalte des Römischen Kaufrechts* (1973) 282-283 at n 3 – n 4.

<sup>30</sup> See Floyd “Die Voorkoopreg” 1986 *THRHR* 253 254, 255 and 261.

<sup>31</sup> The formula of the *actio venditi* ordered the *iudex* to take *bona fides* into account when reaching his verdict. If the parties to a sale concluded ancillary agreements relating to the main agreement, good faith demanded that these agreements be honoured. Only *pacta adiecta* entered into simultaneously with the main contract could in themselves give rise to the action on sale. If such a *pactum* was entered into later, it could only give rise to a defence. *D* 2 14 7 5 (Ulpianus), Zimmermann *Obligations* 510.

<sup>32</sup> *D* 19 1 21 5: “Sed et ita fundum tibi vendidero, ut nulli alii eum quam mihi venderes, actio eo nomine ex vendito est, si alii vendideris.”

grants the seller the action on sale (*actio venditi*) “ad complendum id quod pepigerunt.”<sup>33</sup> This phrase has been translated as “to enforce execution of the bargain,”<sup>34</sup> “for the honoring of such obligation”<sup>35</sup> and “om die beding af te dwing.”<sup>36</sup> However, the text does not clarify what relief exactly the *actio venditi* would be directed at.

Many writers treat this subject rather cursorily and do not discuss the exact remedy available to the preference holder.<sup>37</sup>

A German Romanist, Peters, identifies four possible outcomes that could arguably be obtained with the *actio venditi* in this context:

1. The *actio venditi* could be directed at restoration of the *merx*, on the basis that the sale to an outsider gives the seller the right to cancel the original sale causing the *merx* to fall back into the hands of the seller. On this construction the *pactum protimeseos* operates like a *lex commissoria*.

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<sup>33</sup> D 18 1 75: “Qui fundum vendidit, ut eum certa mercede conductum ipse habeat vel, si vendat, non alii, sed sibi distrahat vel simile aliquid paciscatur: ad complendum id quod pepigerunt ex vendito agere poterit.”

<sup>34</sup> Mackintosh *The Roman Law of Sale (with modern illustrations): Digest XVIII.1 and XIX translated with notes and references to cases and the ‘Sale of Goods Bill’* (1892) 127, relied upon by Ogilvie Thompson JA in *Owsianick* 320A.

<sup>35</sup> Watson’s translation in Mommsen *et al The Digest of Justinian II* (1985).

<sup>36</sup> Van Heerden AJA in the *Oryx case* 905E-F.

<sup>37</sup> See, for example, Zimmermann *Obligations* 570; Kaser *Das Römische Privatrecht* 561. Cf Schurig *Das Vorkaufsrecht* 25 who states without reference to authority that the *pactum protimeseos* obliges the buyer to sell the thing to the seller on the same terms as agreed with a third party interested in buying the thing. Cf also Floyd 1986 *THRHR* 253 255 n 23 who concludes that the discussion by De Zulueta *The Roman Law of Sale: introduction and selected texts* (1945) 57, Moyle *The Contract of Sale in the Civil Law* (1892) 176, and Buckland *A Text-book of Roman Law from Augustus to Justinian* 3<sup>rd</sup> edition (1963) 495 rests on mere speculation.

2. The *actio venditi* could be directed at delivery of the thing to the seller, on the basis that the sale to an outsider brings about a second contract of sale with the erstwhile buyer as seller.
3. The *actio venditi* could be directed at a contractual penalty.
4. The *actio venditi* could be directed at the payment of damages.

According to Peters, only the fourth possibility holds water.<sup>38</sup>

His reason for rejecting the first possibility is that, if the *pactum protimeseos* had the effect of a *lex commissoria*, there would have been no need for the usual agreement requiring the buyer to sell to the seller, when the buyer wants to alienate. However, that argument wrongly presumes that the texts mention a duty on the buyer to sell to the seller. The emphasis in the texts is rather on the negative obligation: the buyer may not sell to anyone else than the seller.<sup>39</sup>

The second possibility, supported by various writers,<sup>40</sup> is based especially on Hermogenianus's formulation "ad complendum id quod pepigerunt."<sup>41</sup> Thus Peters admits that *complendum* ("fulfilment") could be directed at the seller's desire to obtain the land.<sup>42</sup>

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<sup>38</sup> 283-284.

<sup>39</sup> See n 32 and n 33. Peters *Die Rücktrittsvorbehalte* agrees that the primary purpose of the *pactum protimeseos* was to prevent the thing from falling into the hands of a third party rather than to give the seller a claim to the thing (282). See also Laue *Begriff und Wesen des Vorkaufsrechts nach BGB* (1905) 9 who states that the texts dealing with contractual *pacta protimeseos* show that they function rather as *pacta de non contrahendo* or *pacta et nulli alii quam mihi venderes*. The negative obligation is in the forefront.

<sup>40</sup> See Peters *Die Rücktrittsvorbehalte* 284 n 8.

<sup>41</sup> For the full text see n 33 *supra*.

<sup>42</sup> That admission presupposes the existence of such a desire, whereas the seller could merely have a desire to ward off unwanted buyers of the land formerly belonging to him (Schurig *Das Vorkaufsrecht* 26 at n 66–67).

The main reason why Peters rejects an order to deliver as possible relief is the absence of any indication in *D 18 1 75* and *D 19 1 21 5* as to the terms of the contract of repurchase. The texts do not state that the seller would be entitled to buy on the terms which the buyer is prepared to accept from a third party or on the terms of the original contract of sale.<sup>43</sup> Another argument militating against enforced delivery of the goods to the seller, is that, during the classical period, all judgments would have had to sound in money in accordance with the rule *omnis condemnatio pecuniaria est*. Even in Justinian's time, it cannot be concluded with certainty that a buyer would be entitled to specific performance of the seller's obligation to deliver the *merx*.<sup>44</sup>

Although Peters admits that a contractual penalty would be an effective remedy in this context, the fragments by Hermogenianus and Paulus do not mention such an agreement. By contrast, *D 45 1 122 3* specifically mentions an undertaking to pay a penalty on breach.<sup>45</sup>

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<sup>43</sup> By contrast, *D 45 1 122 3*, specifically refers to a price having been fixed by the parties. *C 4 66 3* (dealing with the *ex lege* preferential right to transact) specifically refers to the owner being entitled to indicate that he would buy on the same terms as can be obtained from a third party. Peters' second argument for rejecting this second construction is less convincing. The prohibition in the texts of a sale to a third party leads Peters to conclude that the *pactum protimeseos* cannot function like the *Vorkaufsrecht* created by the German civil code, the *BGB*, whereunder nothing less than the sale to an outsider triggers a remedy which ultimately enables the holder to enforce delivery of the thing by the grantor (285). (See further par 4 1 1 *infra*.) Thus, as a sale to a third party is prohibited, Peters argues that nothing can trigger availability of the remedy of enforcement of delivery. Hermogenianus could, however, have meant that a lesser manifestation of a desire to sell, such as an offer to sell to an outsider, would trigger the remedy contemplated by him. Peters argues that, if this was so, an indication in the text of the terms of such an offer would be expected.

<sup>44</sup> ZimmErman *Obligations* 772 and authorities cited there. Cf *D 19 1 1 pr* (Ulpianus): "Si res vendita non tradatur, in id quod interest agitur, hoc est quod rem habere interest emptoris." Cf Kaser *Das Römische Privatrecht* 561-562.

<sup>45</sup> For the full text see n 24 *supra*.

Accordingly, for Peters, only the last possibility remains, namely that the *actio venditi* was directed at damages upon a sale in breach to a third party.<sup>46</sup> In my view, however, Peters has not clearly ruled out the possibility of the *pactum protimeseos* having functioned like a *lex commissoria*.

An overview of the position in Roman law reveals uncertainty regarding the construction of the *pactum protimeseos*.<sup>47</sup> The suggestion in the *Oryx* case that the holder of a *pactum protimeseos* had the same rights as an ordinary buyer in Roman law, including entitlement to delivery of the *merx* upon breach, is therefore open to doubt. The court appears to have placed much weight on its mistaken reading of *D 18 1 75* as granting the original seller the *actio empti* - the action of a buyer - on breach.<sup>48</sup> The court implied that the holder of the *pactum protimeseos* would thereby be entitled to enforce the grantor's duty to deliver just as a buyer could against his seller. The text however grants the seller the *actio venditi* - the action of a seller - simply because that is the only action with which the *pactum protimeseos*, as a *pactum adiectum* to a sales contract, could be enforced. The name of the action has no bearing on the relief that could be obtained in this instance.

### 3 3 Germanic Law

As has been indicated above, different conclusions were reached in the two leading cases on whether the feudal or Germanic law figure of contractual *naastingsrechte* displaced

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<sup>46</sup> Peters *Die Rücktrittsvorbehalte* 285. He suggests that a seller who sold at a lesser price than he otherwise would, because he believed that he would be able to buy back the thing could then claim the difference in price as damages. Cf also Floyd 1986 *THRHR* 253 261-262; Du Plessis *Die spesifieke nakoming van voorkoopregte en ander verwante regte in die Suid-Afrikaanse en Franse Reg* unpublished LLM dissertation, University of Stellenbosch (1997) 1-2.

<sup>47</sup> See also Laue *Begriff und Wesen des Vorkaufsrechts* 9; Floyd 1986 *THRHR* 253 261-262; Du Plessis *Spesifieke nakoming* 10.

<sup>48</sup> 905E-G.

the Roman law *pactum protimeseos* in Roman-Dutch law.<sup>49</sup> To understand the construction of the *naastingsrecht* or *ius retractus* of the Roman-Dutch sources, and to evaluate the reasons for its development, a brief investigation of Germanic law is required.

The term “Germanic law” refers to the legal rules of the Germanic tribes who lived in Western Europe after the fall of the Roman empire in the West prior to the reception of Roman law. Although these rules varied territorially, some common characteristics may be identified, such as the absence of the concept of ownership of land as an abstract, absolute right vesting in a specific person. Classical Germanic feudalism, applied in the Frankish areas, including the “Low Countries,” from the eighth century, denies the possibility that land could be owned – it could only be held in tenure.<sup>50</sup> The concept of tenure again, comprises a number of different juridical relationships with regard to land.<sup>51</sup> Around the thirteenth century, as a compromise between feudal and Roman principles, the concept of tiered ownership (superior and inferior ownership) came to be used to describe these different relationships.<sup>52</sup> Tenure thus came to be regarded as one of the different possible tiers of ownership.<sup>53</sup> “Ownership” was therefore more of a conglomerate of various rights or powers to use and exploit the thing than an abstract concept.<sup>54</sup>

According to some writers, the existence of preferential rights to buy in Germanic or feudal law confirms the theory that in ancient times ownership of land was not merely tiered, but collective.<sup>55</sup> After the development of individual ownership, relicts of the

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<sup>49</sup> *Supra* at 38.

<sup>50</sup> Gretton “Feudal System” in Reid *The Law of Property in Scotland* (1996) 50-62.

<sup>51</sup> Van der Merwe *Sakereg* 2<sup>nd</sup> edition (1989) 171-172.

<sup>52</sup> Gretton “Feudal System” 50-62.

<sup>53</sup> *Ibid*; De Blécourt & Fischer *Kort Begrip* 93.

<sup>54</sup> Schurig *Das Vorkaufsrecht* 27.

<sup>55</sup> Schurig *Das Vorkaufsrecht* 27 at n 75 and writers cited there. See Moorman van Kappen *Met open buydel* 13-14 and De Blécourt & Fischer *Kort Begrip* 97-98 for criticism and evaluation of this view.

ancient collective ownership manifested itself in various limitations on ownership in favour of certain classes of people, who may be identified with the co-owners of former times.<sup>56</sup> The rights of retraction existing in Germanic law are examples of such limitations. Known in German as *Näherrechte* and in Dutch as *naestingsrechte*,<sup>57</sup> they entitle those who are “closer” to a thing, for example by reason of family ties, to retract or “draw to themselves” the thing in the event of its sale to an outsider. Retraction may take place on payment of the agreed purchase price.<sup>58</sup> For the purpose of this discussion the term rights of retraction will be used.

The idea that family land should remain preserved for future family members was strengthened by the consideration that family farming was the most important income

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<sup>56</sup> Schurig *Das Vorkaufsrecht* 28; De Blécourt & Fischer *Kort Begrip* 101 *et seq*

<sup>57</sup> *Naestingsrechte* in Old Dutch.

<sup>58</sup> Laue *Begriff und Wesen des Vorkaufsrechts* defines the right of retraction as the right created by statute or custom for a certain class of persons, to appropriate sold land against performance of the obligations undertaken by the buyer (11). Note that no reference to the grantor is found in his definition. The right is directed at the land itself. There were various kinds of *ex lege* rights of retraction in Germanic law. Some were created or sanctioned by statute. See Gail *Practicarum Observationum* (1626) 19. Examples of rights of retraction (some developing after the reception) were those in favour of co-members of a knightage, in favour of members of the aristocracy on the sale to a non-aristocrat, in favour of Christians on the sale to a Jew, in favour of co-heirs or other co-owners, as well as in favour of neighbours. (Schurig *Das Vorkaufsrecht* 32-34; Gail *Practicarum Observationum* 19). Where ownership was divided into superior and inferior ownership, the feudal lord had a right of retraction upon the vassal alienating his rights in the land, as did the co-vassals (Schurig *Das Vorkaufsrecht* 33). All these types of rights were based on the holder of the right of retraction being “closer” to the land than outsiders. The construction of these rights of retraction were similar to that of relatives: it could be exercised even against third parties on payment of the purchase price (Schurig *Das Vorkaufsrecht* 34). Similar rights were also known in other early cultures. For example, in Judea of Biblical times, relatives were entitled in the order of their degree of relatedness to an owner of land to “redeem” the land on the sale thereof to an outsider by buying back the land (Ruth 3:12-13 and Ruth 4:1-11). See also Leviticus 25:25, 47-55, Numbers 35 and Deuteronomy 19:6 which suggest that such rights were regarded as endorsing a relative’s wider moral obligation to protect other family members and see to it that none was left destitute. Cf Guthrie *et al New Bible Commentary* 3<sup>rd</sup> edition (1970) 278, 282. See also Moorman van Kappen *Met open buydel* 13 at n 121. Rights of retraction are still widespread in Islamic countries (see Schurig *Das Vorkaufsrecht* 18).

source for the rural population and that voting rights depended on land possession.<sup>59</sup> An owner could thus only alienate his land if he first offered it for sale to his heirs who declined to buy. If he failed to offer, they could claim the land from the buyer against payment of the purchase price.<sup>60</sup>

This *ex lege* right probably developed from an outright prohibition to alienate land without the consent of the nearest heirs.<sup>61</sup> Heirs were regarded as having incomplete ownership of the land which they would inherit on the death of the owner. If the owner sold to an outsider, the heirs' incomplete ownership immediately waxed to full ownership.<sup>62</sup> On breach of this prohibition, the heirs as owners could have the alienation set aside and, as owners, obtain the land as if the seller had died; thus even against outsiders and without paying the purchase price.<sup>63</sup> However, an exception arose in terms of which an owner could, in the case of real necessity, alienate the land on condition that he first offered it to his nearest heirs. This exception became the general rule: the prerequisite of necessity disappeared. However the remedy of the heir in the case of breach was retained: he could claim the land, even from the third party, but now against

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<sup>59</sup> Moorman van Kappen *Met open buydel* 14; De Blécourt & Fischer *Kort Begrip* 97 *et seq*

<sup>60</sup> Schurig *Das Vorkaufsrecht* 31; De Blécourt & Fischer *Kort Begrip* 97 ff; Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht* 4.

<sup>61</sup> Schurig *Das Vorkaufsrecht* 31-32. Moorman van Kappen *Met open buydel* 14; De Blécourt & Fischer *Kort Begrip* 99.

<sup>62</sup> Schurig *Das Vorkaufsrecht* 31-32. De Groot calls this real right of the heirs *eigendomsverwacht*, a type of *gebrekkelijke eiendom* (Inl 2 3 10-2 3 11 & 2 47 6). Schurig refers to an *Erbenwartrecht* 29 & 30. See also Moorman van Kappen *Met open buydel* 14 who refers to the terms *Anwartschaftsrecht* in German and *droiture* in French. Cf however De Blécourt & Fischer *Kort Begrip* 99-100 who say that in the Frankish-Germanic period (±500-900) the family's consent was necessary to alienate immovables. If no consent was given, the alienation could be declared void by judicial decree. They makes no mention of an automatic right of relatives to claim the land for themselves on alienation.

<sup>63</sup> Schurig *Das Vorkaufsrecht* 31-32; Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht* 9.

payment of the purchase price.<sup>64</sup> As owner, the holder could thus simply ask for an order that the transfer to the third party be set aside.

The significance of this development is that the proprietary remedy<sup>65</sup> ascribed to the *ex lege* right of retraction, which allows the holder of the right of retraction to lay claim to the land, preceded the later construction of the *ex lege* right of retraction, which places a duty on the owner to make an offer to contract before selling. That explains why the remedy for breach of the right in its later form was not, as should be expected, an order to make an offer, but was directed at delivery of the land. This remedy cannot be equated with specific performance of the right of retraction. Rather, the idea that the holder's incomplete ownership waxed to full ownership accounts for the remedy of laying claim to the land.

Rights of retraction therefore differed from Roman *iura protimeseos* in a number of ways. The first was a real right, the latter not.<sup>66</sup> The source of rights of retraction was legislation or custom whereas *pacta protimeseos* were consensual agreements (although some *ex lege* rights of pre-emption did exist in Roman times).<sup>67</sup> Rights of retraction existed in favour of a group (for example, neighbours or family members) whereas the *ius protimeseos* vested in an individual. The object of a *ius protimeseos* could be movable or immovable. Rights of retraction only existed over land.<sup>68</sup>

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<sup>64</sup> Schurig *Das Vorkaufsrecht* 42 calls the right of retraction a *verdingliches obligatorisches recht*. The owner's duty to make an offer to contract stemmed from the heir's real right in the land. If this duty was breached the heir still had a real right to claim the land, but then incurred an obligation to fulfill the obligation that existed between the owner and third party. See also Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht* 9.

<sup>65</sup> See also Laue *Begriff und Wesen des Vorkaufsrechts* 10.

<sup>66</sup> Schurig *Das Vorkaufsrecht* 36, 49. Some writers speculate that the *ex lege* right of pre-emption of Roman law could have had real effect (De Zulueta 58 n 2, Floyd 1986 *THRHR* 253 261 n 84).

<sup>67</sup> See at n 25-26 *supra*.

<sup>68</sup> Laue *Begriff und Wesen des Vorkaufsrechts* 10-11. Laue (at 11) also considers that the event which triggered the right of retraction was the conclusion of a contract with a third party, whereas the Roman figure only required the desire to contract. ("...das römische...Vorkaufsrecht nach [heutige Meinung] nur

Rights of retraction created by juristic act were also recognised in feudal times before the reception.<sup>69</sup> Modelled on *ex lege* rights of retraction, they were created simultaneously with the transfer of the land in favour of the seller or a third party.<sup>70</sup> The buyer thus did not obtain unrestricted ownership. His ownership was regarded as limited by the agreement of retraction, and the right of retraction created a similar real right enforceable against everyone.<sup>71</sup> As these rights of retention apparently always applied to land, the element of publicity essential in modern law for real rights or the operation of the doctrine of notice did exist due to the formalities accompanying transfer of land.

The Germanic remedy described here immediately brings to mind the *Oryx* mechanism.<sup>72</sup> Both make an order to submit an offer superfluous, as they allow the holder to lay claim to the thing on a mere declaration of intention to exercise her right after the grantor's breach. The two figures differ in that the *Oryx* mechanism is no longer regarded as enforcement of a real right. The significance of the development described here is the recognition that the formulation of the *Oryx* remedy may be described as an accident of history. Its Germanic predecessor was not formulated in an attempt to strengthen the protection of the holder's interests, but rather as an attempt to water down the holder's limited ownership. The rejection of the concept of tiered ownership that provides the historical basis for the *Oryx* mechanism accounts for the difficulty which courts and commentators have in explaining the *Oryx* mechanism in terms of Romanist terminology.<sup>73</sup>

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*Kaufvertragswillen zur Voraussetzung.*") He admits, correctly, that the Roman law figure was not well defined (9, 11). What remedy the "desire to contract" gave rise to, is unclear.

<sup>69</sup> Schurig *Das Vorkaufsrecht* 34-35. Cf Gail *Practiarum Observationum* 19 (who merely refers to limitations on land which can be imposed by agreement as justification for rights of retraction flowing from statute).

<sup>70</sup> Schurig *Das Vorkaufsrecht* 35, 46.

<sup>71</sup> *Ibid*; Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht* 12.

<sup>72</sup> See ch 1 *supra* on the meaning of "*Oryx* mechanism."

<sup>73</sup> Cf Schurig *Das Vorkaufsrecht* 60. See also Van der Walt & Kleyn "Duplex Dominium: The History and Significance of the Concept of Divided Ownership" in Visser (ed) *Essays on the History of Law* (1989)

### 3 4 Roman-Dutch Law

Rights of retraction did not disappear as a result of the reception of Roman law in the Germanic territories – in fact some new forms developed.<sup>74</sup>

The family *naastingsrecht* was described as the *ex lege* right of blood relatives of a seller of land<sup>75</sup> to place themselves in the position of the buyer within a specified time period, if the buyer was not also a blood relative of the seller.<sup>76</sup> If the thing was already delivered to the buyer and if he had paid the purchase price, then the buyer had to deliver the thing to the *naaster* against compensation of the purchase price. If the thing had not yet been

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213 216 who conclude that, although the similarity between the modern concept of ownership and its Roman counterpart has been exaggerated, South African law conceives of ownership as a right which is in principle unrestricted and therefore absolute. See also Schulz *Classical Roman Law* (1951) 338. See, for example, Van der Merwe *Sakereg* 171-173, Schurig *Das Vorkaufsrecht* 20, 27 for the view that Roman ownership was in principle unrestricted and absolute. Cf Kaser *Das Römische Privatrecht* 400-403; Birks “The Roman Law concept of Dominium and the idea of absolute ownership” 1985 *Acta Juridica* 1.

<sup>74</sup> Schurig *Das Vorkaufsrecht* 36. Schurig shows that after the fall of the Western Roman Empire (in AD 476), and before the reception in Western Europe, the Germanic concept of rights of retraction had already penetrated Roman law. In the West, landowners resisted the Romanisation of land law after the reception (Moorman van Kappen *Met open buydel* 4-5). See also De Blécourt & Fischer *Kort Begrip* 102-3 for examples of types of rights of retraction which existed in the Netherlands. That the family right of retraction is sanctioned by the Bible appears to have contributed to its survival (Gail *Practicarum Observationum* 19).

<sup>75</sup> Or “incorporeal things” regarded as immovable like quitrent (*erfpacht*), or long leases. Moorman van Kappen *Met open buydel* 6; De Groot *Inl* 3 16 5.

<sup>76</sup> De Groot *Inl* 3 16 2: “een reg iemand toe-behoorende over eenig ontilbaer goed, als oock op den koper ende verkooper wanneer ‘t zelve goed verkocht werd, om te treden in des koopers plaetze.” (The phrase *oock op den koper ende verkooper* means that the right could be enforced against the third party buyer and the seller. Cf Van der Keessel *Praelectiones* on Gr 3 16 2.)

delivered the seller had the duty to deliver to the *naaster*. A court could also order delivery by the seller or third party.<sup>77</sup>

Details as to who exactly may retract or *naasten* and when and how this could be done, varied territorially.<sup>78</sup> In some areas the procedure of retraction (*naasting*) could take the form of a pre-emption (or *voorkoop*) procedure, in order to protect the buyer from the possibility of losing the thing at any time after the sale through *naasting*. This involved that the seller first had to publicly declare his intention to sell, whereupon the relatives had a certain period within which to buy, failing which the right of retraction was lost.<sup>79</sup> However, the seller could still sell without first publicizing his intention, in which case he had to publicize the sale giving his relatives the chance to retract the thing (thus through a *nakoop*-procedure).<sup>80</sup>

Some *ius commune* writers grappled with the nature of *naastingsrechte*. Gail for example, concludes that the action granted to the holder of a *naastingsrecht* is not a purely personal action, but is “written on the thing itself” (*in rem scriptam*) and thus follows the possessor wherever the goods go.<sup>81</sup> He notes that some writers dispute the real operation of such a personal action.<sup>82</sup> De Groot clearly sees *naastingsrechte* as real rights which may be enforced against the seller and the third party buyer.<sup>83</sup>

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<sup>77</sup> Van der Keessel *Praelectiones* on Gr 3 16 11.

<sup>78</sup> Moorman van Kappen *Met open buydel* 5; De Blécourt & Fischer *Kort Begrip* 101; Zimmermann “Kaufvertrag” 192. Many rights of retraction were introduced by legislation or created by local custom, which therefore differed from one area to the next (De Blécourt & Fischer *Kort Begrip* 101-102).

<sup>79</sup> Gail *Practicarum Observationum* 19; De Groot *Inl* 3 16 5. Cf 3 16 6.

<sup>80</sup> Moorman van Kappen *Met open buydel* 8. De Groot *Inl* 3 16 1 mentions *nakoop* as a synonym for *naasting*. So also De Blécourt & Fischer *Kort Begrip* 101.

<sup>81</sup> *Practicarum Observationum* 19.

<sup>82</sup> *Ibid.*

<sup>83</sup> *Inl* 3 16 5 and 3 16 16. See also Van der Keessel *Praelectiones* on Gr 3 16 16.

The important question is whether contractual arrangements creating preferential rights to transact also operated like the Germanic *ex lege* right of retraction. Four possibilities exist:

1. All contractual arrangements creating preferential rights to transact operated like Germanic rights of retraction and the Roman law *pactum protimeseos* disappeared.
2. All contractual arrangements creating preferential rights to transact were assigned the construction of the Roman law figure.
3. Contractual *naastingsrechte* and Roman law *pacta protimeseos* were available as alternative constructions.
4. The constructions influenced each other so that a mixed figure evolved.

In De Groot's time, *naastingsrechte* did not exist throughout the province of Holland.<sup>84</sup> A relative wishing to exercise a *naastingsrecht* had to allege and prove that such a right existed in the area where the immovable property was situated.<sup>85</sup> The variation in influence and operation of *ex lege naastingsrechte* might have resulted in a variation in the construction of contractual preference arrangements. As *ex lege naastingsrechte* did not exist throughout the province of Holland, it is more likely that the construction of such rights had a lesser influence on contractual arrangements creating preferential rights to transact there, than in areas where *ex lege naastingsrechte* were more prevalent.

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<sup>84</sup> De Groot *Inl* 3 16 3-3 16 5, 3 16 18. See also Van der Keessel *Th* 3 16 3 and Van Zurk *Codex Batavus* (1738) sv *Nakoop, Naesting, A. Pontgeld* par 2 and 3B. De Blécourt & Fischer *Kort Begrip* 382 point out that *naasting* existed in all territories where the intestate succession system known as *Skependomsreg* existed, but not where the system of *aasdomsreg* existed. In North-Holland the system of *Aasdomsreg* applied initially. After an attempt to replace it with *skependomsreg*, the *aasdomsreg* was reintroduced in 1599 (De Blécourt & Fischer *Kort Begrip* 382; Van der Merwe & Rowland *Die Suid-Afrikaanse Erfreg* 6<sup>th</sup> edition (1990) 22-23).

<sup>85</sup> De Groot *Inl* 3 16 5; Moorman van Kappen *Met open buydel* 10.

### 3 4 1 Writers from Holland

De Groot only considers *ex lege naastingsrechte* in his discussion *van naesting*.<sup>86</sup> The omission of the contractual figure might indicate that, in Holland, the construction of the contractual right of pre-emption differed from that of the *ex lege* right of retraction.

Voet, on the other hand, does discuss the contractual right of retraction (which he also calls a *ius retractus*) in conjunction with the family right of retraction.<sup>87</sup> However, he distinguishes the construction of the *ex lege* right of retraction from the contractual figure.<sup>88</sup> He specifically mentions that in the case of the family right of retraction the retracting party steps as completely into the place of the purchaser as if he and not the purchaser has bought the property, with the result that the tie between the vendor and the first purchaser is broken.<sup>89</sup> Thus he says, the exercise of the *ex lege* right of retraction is considered as one sale and one contract which the retracting party is considered to have himself entered into by ousting the purchaser and stepping into his place and transferring to himself the whole effect of the contract, so that fines and charges relating to alienation do not have to be paid again.<sup>90</sup> He distinguishes this construction from that applying to the contractual right of retraction. Perhaps this implies that the exercise of the contractual right of retraction brings about a second, separate contract, so that the holder may also have to pay fines and charges on alienation.<sup>91</sup> If this is what Voet means it

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<sup>86</sup> *Inl* 3 16 1 - 3 16 18.

<sup>87</sup> *Commentarius ad Pandectas* 18 3 9 *et seq.*

<sup>88</sup> 18 3 27 – 18 3 29.

<sup>89</sup> 18 3 27.

<sup>90</sup> *Ibid.*

<sup>91</sup> 18 3 29. Gane translates the last paragraph of this text as follows: “For the rest however it appears to be agreed by everyone that a retractor is not put under obligation for fresh *laudimia* or other like burdens whenever the retraction springs not from an agreement to sell back but from law or custom. That is because there is understood to be not a double but a single purchase only, and a single contract into which the retractor himself is deemed to have entered when he displaces the purchaser and steps into his place as such, transferring to himself the whole effect of the contract.” (Gane *The Selective Voet being the Commentaries on the Pandects* (1956)).

remains unclear when the separate contract comes into existence – would that be only on the acceptance of a subsequent offer by the grantor, or would a sale in breach and a unilateral act by the holder cause the contract to come into existence? In any event, Voet confines the remedy of “stepping into the place of the purchaser” to the *ex lege* right of retraction.

The method Voet prescribes for the exercise of the right of retraction mirrors that prescribed in the Codex where the quitrent holder wants to sell his quitrent right, namely that notice should be given of the intended sale, whereafter the holder (the owner in the case of the Roman *ex lege* right) has two months to declare his intention to buy.<sup>92</sup>

The only other comment Voet makes on the construction of the contractual right of retraction is that the grantor

“can in no way be compelled under that agreement to sell the thing, either by Roman law or by modern custom; but if he afterwards sells it to another party I have an action in respect of the damage which his breach of agreement has caused to me.”<sup>93</sup>

It is not certain whether his statement that the grantor cannot be compelled to sell the thing refers also to the situation after breach by the grantor or merely to the situation before the occurrence of the trigger event. As he does not limit the statement, both meanings are possible. Some judges have interpreted his statement that damages may be claimed after a sale to a third party, as only applicable when transfer to a *bona fide* third party had taken place.<sup>94</sup> There is no compelling reason to interpret the text in this way and the possibility that Voet means to disallow the holder the remedy of specific performance or an order that the grantor deliver the thing even before transfer cannot be excluded.

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<sup>92</sup> C 4 66 3 and Voet 18 3 10. See also Floyd 1986 *THRHR* 253 256.

<sup>93</sup> My translation of Voet 18 1 2.

<sup>94</sup> Ogilvie Thompson JA in *Owsianick supra* 319D-E and Van Heerden AJA in the *Oryx case supra* 907A.

Van Heerden AJA also relied on Van Leeuwen in support of his contention that the contractual right of retraction operated like the *ex lege naastingsrecht*.<sup>95</sup> Van Leeuwen does not discuss the remedies of the holder of a contractual right of retraction in detail. His definition of the contractual right of retraction includes an agreement that the purchaser is bound to resell at the option of the seller, as well as an agreement that, if the thing is sold to another, the original seller “on offering the same price, is preferred and retracts the sale.”<sup>96</sup> Elsewhere he defines a “*naastingsrecht*” by way of agreement as entailing that the purchaser shall return the property sold at the option of the vendor or within a certain time, at the same price; or that, in sale the vendor “must always be the nearest, should he so wish”.<sup>97</sup>

The implications of these definitions for the remedies of the holder are not explained. Van Leeuwen says it is doubtful whether handing back the *merx* to the seller constitutes a new sale, so that transfer duties must be paid again.<sup>98</sup> He reasons that the original sale from the holder to the grantor is rather confirmed when the *merx* is handed back as this is done in accordance with the original sale. He then states that “upon such retraction or giving back of the thing, the buyer is not liable to pay the duty; except that he must

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<sup>95</sup> *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd & Andere supra* 906C.

<sup>96</sup> Van Leeuwen *CF* 20 4: “Retractus conventionalis, de quo hic proprie, est pactum quo convenit, ut si venditor emptori pretium restituat, emptor venditori rem emptam revendere cogatur, vel si quando res empta iterum alteri vendatur, primus offerendo idem pretium praeferatur, venditionemque retrahat.” See also Van Leeuwen *RHR* 18 3.

<sup>97</sup> My literal translation of Van Leeuwen *RHR* 19 1: “Het regt van Naasting wt beding [sic], is daar by men bedingt, dat den Koper het verkofte goed, tot believen van den Verkoper, of ook wel binnen sekren tijd, voor den selven prijs, aan den verkoper wedrom sal moeten overdoen, of in het verkopen, den Verkoper altijd wedrom de naaste moet zijn, so hy wil.” As authority he refers to the Digest of Justinian. The second part of the sentence has been translated as “if the purchaser sell the property, the vendor shall have the option of repurchase” by Kotzé in Decker (ed) *Commentaries of Roman-Dutch Law* 2<sup>nd</sup> edition (1923). The implication that the contractual *naastingsrecht* is a type of option is not justified by the text.

<sup>98</sup> *RHR* 19 2.

reimburse the purchaser the original expenses incurred on that account.”<sup>99</sup> Van Leeuwen’s argument allows for the acceptance of a remedy like the *Oryx* mechanism, but his view on the holder’s remedies is unclear. That the holder may be entitled to delivery of the thing itself is perhaps implicit in the statement that “he is preferred and retracts the sale”.<sup>100</sup> Whether this means the same as in the case of an *ex lege* right of retraction, namely that the holder is to institute proper proceedings, after which the third party is bound to restore the thing to the holder,<sup>101</sup> or whether it simply means that the sale to the third party buyer may be cancelled so that the thing is restored to the grantor, is not clear. Accordingly Van Leeuwen does not provide clear authority for the view that the holder is entitled to stronger relief than restoration of the *status quo ante* by setting aside the transfer to a third party purchaser with notice.

Van der Keessel focuses his discussion on *ex lege* rights of retraction. He merely mentions the conventional *retractus* appended to a sale and does not discuss the remedies available to the holder.<sup>102</sup> His reference to the Digest of Justinian in this context suggests that he would construe the conventional *retractus* like the Romans did. Elsewhere, he emphasises that Grotius’s definition of the *ius retractus* as a right in respect of immovable property entailing that the holder is preferred upon a sale and steps into the place of the buyer, is limited to *ex lege* rights of retraction.<sup>103</sup>

It can therefore be deduced, especially from Voet, that the holder of a contractual right of retraction probably could not step into the shoes of a third party buyer on a sale in breach of his right. That was a remedy confined by Voet to *ex lege* rights of retraction. It is not

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<sup>99</sup> *Ibid.*

<sup>100</sup> *CF* 20 3 and *RHR* 19 2, where he speaks of *naasting*.

<sup>101</sup> *CF* 20 27. *Cf* Van der Keessel *Th* 3 16 11.

<sup>102</sup> Van der Keessel *Th* 3 16 1.

<sup>103</sup> Van der Keessel *Praelectiones* on *Gr* 3 16 2. See his discussion of the remedies of the *ex lege naaster* in 3 16 11. (The *naaster* steps into the place of the third party buyer. Before transfer to the buyer had taken place, the *naaster* may sue the seller for transfer. Had transfer taken place, a new transfer to the *naaster* must take place).

clear whether the holder could enforce delivery on breach either. Van Leeuwen appears to treat the contractual right of retraction as analogous to the one arising *ex lege*. What is undisputed is that the holder could claim damages. Thus the writers of Holland do not provide clear authority for an *Oryx* mechanism type remedy, nor for a remedy of specific performance in the form of an order to sell or make an offer, nor do they unanimously and clearly exclude such remedies.<sup>104</sup>

### 3 4 2 Other Dutch writers

All three judges in the two leading South African cases referred to Van Zutphen of Utrecht and Schrassert, who wrote on the law of Gelderland.<sup>105</sup> Botha JA also referred to the Frisian writer, Sande.<sup>106</sup>

The opinions of Sande<sup>107</sup> were treated with great respect by the writers of Holland and still carry much weight in South Africa.<sup>108</sup> Sande states that if an agreement has been made by a pact appended to a contract that the one party will not sell or lease the property to anyone but the other, a personal action for damages would arise out of such a pact on breach by the owner provided the other party had some interest why the owner should not alienate.<sup>109</sup> Damages are also payable where an owner had on transfer of his property

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<sup>104</sup> Cf also Floyd 1986 *THRHR* 253 263; Du Plessis *Spesifieke nakoming* 4-5. In his discussion of *D* 18 1 75, Groenewegen *De Legibus Abrogatis* merely refers one to his remarks on *C* 4 6 3, where he emphasises that immovables cannot be subjected to a real burden by contracting parties unless a written document of the transaction is executed before a magistrate. He makes no comment on *D* 45 1 122 3 or *D* 19 1 21 5. Van Bynkershoek *Quaestionum Juris Privati* 313 only discusses *ex lege* rights of retraction.

<sup>105</sup> *Owsianick supra* 320A-C, 321H-323D and *Oryx supra* 905H-906D.

<sup>106</sup> 323C-D.

<sup>107</sup> 1586-1638.

<sup>108</sup> *De Wet Die Ou Skrywers in Perspektief* 144.

<sup>109</sup> Sande *Tractatus de Prohibita Rerum Alienatione* 4 2 2. Sande appears to discuss the Roman law position stating that such a pact must be appended to a *bona fide* contract or strengthened by stipulation. However in the rest of his discussion he refers to sixteenth century writers.

made it a condition of the sale that the purchaser shall not alienate or sell to any one but him.<sup>110</sup> Sande makes no mention of a contractual *naastingsrecht* or a remedy aimed at delivery or transfer to the holder. The arrangement discussed by him is constructed rather like the Roman law *pactum protimeseos*.

Van Zutphen, who practised in Utrecht, wrote a chapter on *voorcoop* in his book on Dutch law.<sup>111</sup> He does not mention *ex lege naastingsrechte* in favour of relatives. He does refer to the question whether a co-owner has a *reg van voorcoop* (right of pre-emption) in respect of the other co-owners' share, but denies this unless local legislation has created such a right of pre-emption. The rest of his discussion is on rights of pre-emption created by agreement.

Like Voet, Van Zutphen holds that the grantor must give notice to the holder if he intends to sell the thing, upon which the holder has two months to declare whether he wants to buy the thing. If the holder fails to make a declaration within those two months, the right of pre-emption terminates. But he goes further than Voet and says that, if the seller (grantor) sells to a third party without any notice, the holder may attack (*immiteren*<sup>112</sup>) the contract of sale and retract (*retraheren*<sup>113</sup>) "the same".<sup>114</sup> It is not entirely clear whether "the same" (*het selve*) in this sentence is meant to refer to the preceding noun, namely the

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<sup>110</sup> 4 2 11 (referring to *D 18 1 75* and *D 19 1 21 5*). He apparently contemplates the interest of the owner to ward off unwanted third parties as near neighbours (4 2 12).

<sup>111</sup> Van Zutphen *Practycke der Nederlandsche Rechten van de Daghelijcksche soo Civile Is Criminele questien* (1645).

<sup>112</sup> From the Latin verb *immittere* meaning alternatively (1) to send in, cause or allow to go in, (2) to let loose, let go free and (3) to let go against, launch against, to attack, to incite against (Simpson *Cassell's Latin-English English-Latin Dictionary* 5<sup>th</sup> edition (1968) 287).

<sup>113</sup> From the Latin verb *retrahere* meaning, literally, to draw back and figuratively, to hold back or withdraw, to draw on again and to induce (Simpson *Cassell's Latin-English English-Latin Dictionary* 521).

<sup>114</sup> Van Zutphen *Practycke sv voorcoop* par 4. The original phrase reads that "...alsdan mach den ghene die de voorcoop competeert sijn selven het contract van vercoopinghe immitteren ende het selve voor de ghedane leveringe retraheren." Van Zutphen refers to the German writers, Berlichius, Carpzovius and Fabricius as authority.

contract of sale, or whether it refers to the *merx*. Grammatically, a reference to the contract of sale makes more sense. Presumably “retraction” therefore only means that the contract in breach of the holder’s right of pre-emption may be set aside. However, in later paragraphs the verb “retract” has as its object the sold goods.<sup>115</sup> If it means the same here, there is scope for an interpretation that the holder may claim delivery of the goods from the seller upon a sale to a third party. Alternatively it could mean that, like the infringing contract, the transfer to the third party may simply be set aside so that the goods revert to the grantor.

Van Zutphen does say that, had the goods been delivered to the purchaser, without notice to the holder, the sale cannot be rescinded. His reason is that the holder only has a personal action against the seller to sue the seller for damages and *interesse*. He does not limit this reasoning to the situation at hand, and the statement is open to the interpretation that the holder may only claim damages on breach.<sup>116</sup> However, he adds that, if the goods had been delivered to a buyer with knowledge of the right of pre-emption, the holder may retract and “revoke” (*revoceren*<sup>117</sup>) the goods.<sup>118</sup>

The critical question is the meaning of “retraction” and “revoke” in this context. Van Zutphen does not spell out whether this means the same thing as in the *ex lege* right of retraction, namely that the holder may step into the place of the purchaser and demand delivery to himself, on having taken certain prescribed steps. Neither does he say whether a new contract of sale comes into existence upon retraction. His statement that the buyer only has a personal right for damages may perhaps be reconciled with the statement that the buyer may retract the goods, by interpreting the latter to mean that the holder may have the transfer to the third party set aside, without being able to enforce

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<sup>115</sup> See paragraphs 6, 9, 11, 14 and 15.

<sup>116</sup> He cites Berlichius 2 40 56-57, Boër, Alexander, Carpzovius 2 32 8-10 and Fabricius 4 36 2 as authority.

<sup>117</sup> From the Latin verb *revocare* meaning to call back or to recall, recover or bring back something.

<sup>118</sup> Van Zutphen *Pracktycke sv voorcoop* 785-786 par 6. He refers to Berlichius *Conclusiones Practicabiles* 2 40 64 as authority.

delivery to himself. In that way the goods are in fact “recalled” or “drawn back” at the instance of the holder, but to the grantor. On the other hand he does use the verb *naesten* as a synonym for *retraheren*, which possibly implies that delivery to the holder may be enforced, as may be done by the holder of an *ex lege naastingsrecht*.<sup>119</sup>

Schrassert, writing on the law of Gelderland, discusses the question whether a provision in a partition agreement that the former co-owners will be preferred if the land be alienated, entitles a son of a party to the agreement to retract the thing with force on alienation.<sup>120</sup> The use of the verb *retraheren* in this context again raises the issue whether delivery of the thing may be claimed by the holder on a sale to an outsider.

He says that the agreement does not create a real right but a personal right for the *interesse* (damages) if the thing had been transferred to the third party buyer. But if transfer had not taken place so that the grantor still has possession, the holder may institute action for the fulfilment of the grantor’s promise to him, and for the sale to himself, and on a refusal, to vouch for the purchase price.<sup>121</sup> This text does not necessarily support the view that the holder could step into the shoes of the third party buyer on the sale. It may in fact provide support for the construction that an agreement of sale can be brought into being upon judicial action. Certainly, it conflicts with the view that only damages may be claimed upon a sale to a third party.

To summarise, Sande provides no authority for any other remedy than a claim for damages. It cannot be said with certainty whether Van Zutphen’s work provides support for the construction espoused in the *Oryx case*, as the learned judge argued. Neither is it totally clear what remedy exactly Van Zutphen has in mind. Schrassert, on the other

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<sup>119</sup> Paragraphs 11, 14 & 15.

<sup>120</sup> Schrassert *Practicae Observationes* (1736) 92.

<sup>121</sup> *Obs* 92 4: “Si vero traditio nondum secuta, sed possessio adhuc sit penes eum, agitur ad complementum promissionibus, adeoque ad venditionem sibi faciendam, oblato et in casu denegationis consignatio pretio.” He refers to Carpzovius (*Dict Const Def* 10 note 8 and 9) and to Christin (*Ad legum Mechlin* 11 2 5 *et seq*) for authority.

hand, clearly indicates that the holder may institute legal action for fulfilment of the promise to sell to him.

### 3 4 3 Other writers of the *ius commune*

Van Zutphen relies heavily on the German writer, Berlichius, as authority for his discussion of the holder's remedies. Both Berlichius and Van Zutphen rely on the German writer Gail.<sup>122</sup> Berlichius is also referred to in the two leading cases.<sup>123</sup> Accordingly the writings of Berlichius and Gail will be examined.<sup>124</sup>

Berlichius clearly distinguishes the contractual right of retraction from the *ex lege* figure.<sup>125</sup> Regarding the remedies of the holder of the contractual right he says that, if the seller (grantor) does in fact sell the goods without notice to the holder, the holder may attack (*immittere*) the contract of sale, and may retract (*retraheren*) the thing before delivery.<sup>126</sup> Had delivery taken place to a *mala fide* buyer, the holder can retract the sold goods "with force" from a pact of such a kind, and revoke the alienation.<sup>127</sup> However, if a

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<sup>122</sup> Van Zutphen *Practycke sv voorcoop* par 4, Berlichius *Conclusiones Practicabiles* (1670) 40 55.

<sup>123</sup> *Owsianick supra* 320A, 322D-H and the *Oryx* case *supra* at 906C.

<sup>124</sup> Pothier's discussion of promises to conclude a sale in the future seems to relate not to rights of pre-emption but rather to agreements to contract recognised in modern European but not South African law (Pothier *Treatise on the Contract of Sale* 6 1 1-6 1 3). Interestingly he states that the act which is the fulfilment of an obligation to conclude a contract of sale may be supplied by a judgment decreeing that, in default of the debtor's being willing to agree to a contract of sale, the judgment itself shall be equivalent to one. He prefers this view above the view that only damages may be obtained in the case of breach of a duty *quae in faciendo consistunt*, as the first view appears to be the one adopted in practice as more conformable to the integrity that ought to govern men in the performance of their promises.

<sup>125</sup> *Conclusiones Practicabiles* 40 53.

<sup>126</sup> *Ibid* 40 54.

<sup>127</sup> *Ibid* 40 64.

penalty was stipulated for on breach, the holder may not have the sale rescinded and retract the goods, but is limited to the stipulated penalty.<sup>128</sup>

Unfortunately, Berlichius does not spell out what retraction of the goods involves, that is, whether it refers merely to the holder being able to set aside the transfer so that the *merx* reverts to the grantor or whether it means claiming the goods for himself.

Gail does not discuss the remedies of the holder of a contractual right of retraction. He therefore provides no authority for Berlichius and Van Zutphen.<sup>129</sup> To this extent Botha JA may perhaps be right in saying that Van Zutphen wrongly imported the legal position applicable to the *ex lege naastingsrecht* to the contractual *right of retraction* (*voorcoopsreg*).<sup>130</sup>

Thus these writers do not clearly indicate what the exact remedy of the holder of a contractual right of retraction would be.

### 3 4 4 Modern legal historians

The construction of the contractual *naastingsrecht* in Roman-Dutch law or the *ius commune* has apparently not received as much attention as the *ex lege naastingsrecht* from modern legal historians,<sup>131</sup> but the conclusion in the previous section that no

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<sup>128</sup> *Ibid* 40 58.

<sup>129</sup> Van Zutphen *Pracktycke sv voorcoop* 4, Berlichius *Conclusiones Practicabiles* 40 55.

<sup>130</sup> 323C.

<sup>131</sup> See eg Zimmermann “Kaufvertrag”; De Blécourt & Fischer *Kort Begrip*; Moorman van Kappen *Met open buydel* and “Voorkeurs- of voorcoopsrecht” 1976 *NJB* 831; Fockema Andreae & Van Appeldoorn *Inleidinge tot de Hollandsche rechtsgeleerdheid beschreven bij Hugo de Groot met Aantekeningen vol II* 3<sup>rd</sup> edition (1926) on Gr 3 16, who all focus on *ex lege naastingsrechte*.

certainty exists as to the remedies of the holder of a contractual right of retraction in Roman-Dutch law, is supported by Floyd.<sup>132</sup>

Another writer who has investigated the historical development of preference contracts is the German writer, Schurig, who wrote a thesis on rights of pre-emption.<sup>133</sup> Schurig is more concerned with the historical reasons for the eventual formulation of the *BGB Vorkaufsrecht* and does not investigate the precise operation of the contractual right of retraction in the sixteenth, seventeenth and eighteenth centuries. His discussion focuses instead on the attempt, especially in the nineteenth century, to distinguish the *pactum protimeseos* from the Germanic institution and to adapt the latter to the system of Roman law.<sup>134</sup>

Schurig is nevertheless of the view that there is no reason to believe that the *pactum protimeseos* of Roman law did not exist in the earlier period. It could then be used as an independent contract as there was no longer a *numerus clausus* of contracts. However, the stronger, more effective right of retraction appears to have been more widely used in Germany.<sup>135</sup> That both existed followed not from juristic or economic need, but was the fortuitous result of historical events.<sup>136</sup> Schurig accepts that the Roman figure only gave rise to a claim to the preferential conclusion of a contract of sale, thus to a preferential offer to contract and not to a real right.<sup>137</sup> The Germanic right of retraction gave rise to a real right. He accepts that on the exercise of this right by unilateral declaration of the holder, a contract of sale (or relationship governed by the rules relating to sale) came into

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<sup>132</sup> 1986 *THRHR* 253 262-263, 256. His statement that there was a great degree of similarity between the *ex lege naastingsrecht* and the contractual right of retraction (255) is not justified by his later conclusions on the uncertainty surrounding the contractual figure (at 256 and 262-263).

<sup>133</sup> See n 27 *supra*.

<sup>134</sup> *Das Vorkaufsrecht* 38-45.

<sup>135</sup> 41.

<sup>136</sup> 59.

<sup>137</sup> 45, 49.

existence as if an offer to sell had been accepted.<sup>138</sup> He accepts that in the case of the Roman figure, an actual offer by the owner (to which the holder was entitled) and the acceptance thereof by the holder were necessary to bring a contract of sale into existence.<sup>139</sup>

### **3 4 5 Overview of the position in Roman-Dutch law and the *ius commune***

The investigation into the position after the reception reveals that the construction of contractual preference arrangements in Roman-Dutch law and the *ius commune* is not entirely clear. The possibility cannot be excluded that the Roman *pactum protimeseos* figure, which may have only given rise to a claim for damages, and possibly an order setting aside a sale to a third party, or of a transfer to a *mala fide* buyer, survived into this era. The “retraction” terminology used by some writers in the context of preference contracts, opens the possibility that the holder could also enforce delivery to himself on a sale to a third party, just like the holder of an *ex lege* right of retraction.

### **3 5 Early South African Law**

As no clarity exists on the construction of preference contracts in Roman-Dutch law, it is difficult to say what rules were received into South African law.

Botha JA in *Owsianick* decided that the Dutch law of *naasting* is not part of our law, and that there is no procedure known to our law whereby the holder may, on a sale in breach

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<sup>138</sup> 49, with no reference to authority at that page. He describes the conflicting arguments by nineteenth century historians on the legal nature of rights of retraction at 38-40.

<sup>139</sup> 45 at n 176, 49.

with his rights, demand that he be allowed to step into the buyer's place.<sup>140</sup> As was shown in chapter two, he was of the opinion that the holder of a contractual right of first refusal was only entitled to an interdict or damages on breach.<sup>141</sup>

Some of the early South African cases decided in the previous century, provide oblique support for Botha JA's contention by virtue of the courts' refusal to order the grantors to sell or transfer to the holders. Instead, damages or orders that the contract between the grantor and third party be declared void were mostly granted.<sup>142</sup> Of course, this may be the result of a reluctance to grant specific performance under English influence, and not necessarily reflect their understanding of the holder's rights.<sup>143</sup>

As has been pointed out in the previous chapter, in one case decided in the previous century, *Malan v Schalkwyk and Odendaal*,<sup>144</sup> the court was prepared to order that the contract with the third party was void and that the holder (the erstwhile seller) 'become

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<sup>140</sup> 323D-E. This conclusion is supported by Floyd 1986 *THRHR* 253 255 who relies on the same authority as Botha JA for his statement that neither the *ex lege* nor the contractual *naastingsrecht* was received into our law. Cf also Wessels *History of the Roman Dutch Law* (1908) 606.

<sup>141</sup> Par 2 1 1 *supra*.

<sup>142</sup> See, for example, *Joseph's Executor v Peacock* 1868 Buch 247, where the holder prayed for delivery and transfer of the thing tendering to pay the purchase price, which prayer the court *a quo* refused; instead ordering the payment of damages (which was claimed in the alternative). Unfortunately, the only issue which the court dealt with on appeal was the passive transmissibility of the right. In *Transvaal Silver Mines v Jacobs, Le Grange & Fox* 1891 5 SAR, the holders merely prayed for an order that the breaching contract to the *mala fide* third party be set aside, which was then ordered by the court. Cf also *Van Pletzen v Henning* 1913 AD 82; *McGregor v Jordaan* 1921 CPD 301; *Sher v Allen* 1929 OPD 137.

<sup>143</sup> In *Haynes v King William's Town Municipality* 1951 2 SA 371 (A) the tide began to turn away from this reluctance to grant specific performance towards the reaffirmation that a party is in principle entitled thereto, and that the court's discretion in this regard is a judicial one unfettered by rigid rules. This was confirmed in *Benson v SA Mutual Life Assurance Society* 1986 1 SA 776 (A) 783. See generally Van der Merwe *et al Contract* 276; Lubbe & Murray *Contract* 542 *et seq*; Joubert *Contract* 224 *et seq*; Christie *Contract* 606; Lambiris *Orders of Specific Performance and Restitutio in Integrum in South African Law* 125 *et seq*.

<sup>144</sup> 1 S 225 (decided in 1852).

entitled to and become possessed of the land' on payment of the original purchase price, as agreed in the preferential arrangement. This order is arguably analogous to the remedy applicable to the *ex lege* right of retraction, which Botha JA regarded as not part of our law.<sup>145</sup>

Moreover, it is submitted that *SA Breweries v Francis & Sons*,<sup>146</sup> which Botha JA relied upon for his conclusion that *naasting* is not part of modern law, does not exclude the possibility that the contractual Germanic *ius retractus* forms part of our law.

That case did not deal with a right of first refusal. A lease provided that the tenant would not mortgage any of the movables on the premises without the Breweries' (the lessor's) consent.<sup>147</sup> Another clause provided that whenever the lease shall terminate, the Breweries shall be entitled to purchase the movables at a price, failing agreement, to be determined by certain third parties. This clause was preceded by a *lex commissoria* in favour of the brewery, which also authorised the Brewery "to enter upon the premises and take possession of the whole."<sup>148</sup> The tenant purported to pass a notarial bond over the movables. The Breweries argued that the tenant's ownership of the movables was qualified by the conditions imposed.<sup>149</sup> The decision turned upon the fact that the bondholders did not know of this limitation. Bale CJ did however, during argument, state to counsel that the *ius retractus* was obsolete,<sup>150</sup> referring only to *Seaville v Colley*.<sup>151</sup> He did not answer counsel's contention that the comments in the *Seaville* case could only apply to a *ius retractus ex lege* and not to the conventional (contractual) *ius retractus*.<sup>152</sup>

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<sup>145</sup> See the discussion of this case in par 2 4 *supra*.

<sup>146</sup> *SA Breweries v Francis & Sons* 27 NLR 648 (decided in 1906).

<sup>147</sup> The lessor had sold the movables on the premises to the tenant.

<sup>148</sup> 650.

<sup>149</sup> At the time of the sale.

<sup>150</sup> 658.

<sup>151</sup> 9 Juta 39.

<sup>152</sup> 658.

Bale CJ's statement was clearly *obiter*. In the reasons for the court's decision he stated that, even if the *ius retractus* had not become obsolete, it did not apply in this case.<sup>153</sup>

The case of *Seaville v Colley*<sup>154</sup> referred to by Bale CJ, concerned the rule of Dutch law that a debtor sued by a cessionary of his creditor could discharge the debt by paying the cessionary the (lesser) sum for which the cessionary had obtained the claim.

The court, per De Villiers CJ, referred to this rule as the debtor's right of retraction.<sup>155</sup> It then referred to the *ius retractus* that existed in "the greater portion of Holland", entitling the nearest relatives of the seller of land, to step into the purchaser's place and demand a completion of the sale in their favour.<sup>156</sup> The court quoted Van Bynkershoek's statement that "every form of retraction, which is nowadays in use,...savours of the utmost unfairness, inasmuch as it robs the purchaser of his honestly acquired right in order to prop up a policy which is of far less importance than the enforcement of contracts."<sup>157</sup> De Villiers CJ then stated, that the law of retraction as applied to immovable property was not general throughout Holland and that he takes it for granted that it was never introduced in this country.<sup>158</sup>

From his example of such a *ius retractus* and the last part of the quotation from Van Bynkershoek, the judge clearly only meant to refer to the *ius retractus ex lege* as being obsolete. Van Bynkershoek would not have referred to a conventional *ius retractus* as reprehensible: such a *ius retractus* is also obtained "honestly". To deny its force would also deny the important policy of "the enforcement of contracts". Clearly, the case therefore does not concern contractual rights of retraction.

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<sup>153</sup> 659.

<sup>154</sup> *Supra*.

<sup>155</sup> 41. He stated that Voet also treated it as a branch of the law relating to *retractus* in 18 4 18.

<sup>156</sup> 41.

<sup>157</sup> 41, quoting from Van Bynkershoek *Quaestionum Juris Privati* 3 13.

<sup>158</sup> 42.

The court in *Seaville v Colley* furthermore referred to the presumption that every “law” introduced from Holland is still in force, unless it is inconsistent with South African usages, the best proof of which is found in unoverruled decisions.<sup>159</sup> In *Transvaal Silver Mines v Jacobs, Le Grange & Fox*,<sup>160</sup> decided five months before *Seaville* and not referred to in that case, the court held that the plaintiffs had “the right of pre-emption, i.e. a species of *retractus*.”<sup>161</sup> However, the construction of a right of pre-emption or of a *ius retractus* was not considered. Apparently it was merely taken for granted that the kind of *ius retractus* under consideration was received into South African law.<sup>162</sup>

### 3 6 Conclusion

An overview of the position in the Roman law reveals that no certainty exists regarding the construction of the *pactum protimeseos*. Van Heerden AJA’s suggestion in the *Oryx case* that the holder of a *pactum protimeseos* had the same rights as an ordinary buyer in Roman law, including entitlement to delivery of the *merx* upon breach, is doubtful at best.

The possibility cannot be ruled out with certainty that Roman-Dutch contractual preference arrangements gave rise only to a claim for damages or the setting aside of the sale to the third party. On the other hand, they could possibly have operated like the *ex lege* right of retraction. Neither can the possibility of both constructions being received into early South African law be excluded. The absence of a clearly defined, unified

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<sup>159</sup> 44.

<sup>160</sup> 1891 5 SAR.

<sup>161</sup> 116.

<sup>162</sup> 119. In *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 188 the court stated that a contract not to sell to a third party without giving the other contracting party an opportunity to purchase is analogous to a *jus retractus* or contractual right of *naasting*. In *Sher v Allen* 1929 OPD 137 141 the court also quoted Voet on the *ius retractus* arising from convention, indicating that the law relating to *iura retractus* may have been received into our law.

default regime for preference contracts in Roman-Dutch law may account for the plurality of constructions in South African law.

The *Oryx* mechanism has its roots in the Germanic (feudal) *ex lege* right of retraction, which allowed the holder to lay claim to the land on a sale in breach of his right. This was a proprietary remedy that developed from the view that the holder had incomplete ownership that automatically waxed to full ownership on breach. This concept of tiered ownership that forms the historical basis for the *Oryx* remedy, does not form part of our law. This accounts for the difficulty that courts and writers have in explaining and formulating this remedy in terms of Romanist obligation terminology, and the resultant resort to the language of fiction.

In view of the uncertainty in Roman, Roman-Dutch and South African law, courts should not, when considering the basic default rules of preference contracts, resort merely to argument based on historical authority and precedent. These can provide no ready made authoritative solutions, but only the raw materials from which solutions may be developed.

## 4 Comparative Perspective

The purpose of this comparative study is to establish whether a multiplicity of constructions<sup>1</sup> of preference contracts is also found in other jurisdictions. If such a multiplicity is recognised the field of application of each construction, that is, the prerequisites that must exist before a specific construction applies, will be considered. If one construction is portrayed as the only correct one to the exclusion of all others, or at least as the default construction which applies in the absence of a clear contrary intention, the reasons for doing so will be considered.

Three jurisdictions will form the focus of this study, namely Germany, England and the United States of America. One justification for this choice is that all three have been relied on in South African case law.<sup>2</sup>

South African courts have often quoted the English case, *Manchester Ship Canal Company v Manchester Racecourse Company*,<sup>3</sup> to support the proposition that the grantor has a duty to make an offer upon occurrence of the trigger event.<sup>4</sup> This has been used to counter the construction of the majority in *Owsianick v African Consolidated Theatres*

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<sup>1</sup> See chapter 1 *supra* for a working definition of the terms “construction” and “construct”.

<sup>2</sup> Language constraints also played a role in this choice, as did preliminary research to ascertain which jurisdictions present sufficient material to study on the basic construction of preference contracts. I will also refer to Austrian, Swiss, Scots and Canadian law at times.

<sup>3</sup> [1900] 2 Ch 352; [1901] 2 Ch 37.

<sup>4</sup> See *Van der Hoven v Cutting* 1903 TS 299; *Sher v Allan* 1929 OPD 137 142; *Cohen v Behr* 1947 CPD 942 946; *Hattingh v Van Rensburg* 1964 1 SA 578 (T); *Hirschowitz v Moolman* 1985 3 SA 739 (A); *Breytenbach v Stewart* 1985 1 SA 167 (T); *Soteriou v Retco Poyntons* 1985 2 SA 922 (A) 932; *Dithaba Platinum v Erconovaal* 1985 4 SA 615 (T). Cf the minority judgment by Botha JA in *Soteriou* at 936B where he distinguishes the *Manchester* case from the facts under consideration. In the latter case, the Appellate Division also relied on the English case of *Smith v Morgan* [1971] 2 All ER 1500.

(Pty) Ltd,<sup>5</sup> in terms of which preference rights creates merely a negative duty (*obligatio non faciendi*), so that no order to make an offer is available.<sup>6</sup>

German law was relied upon in support of the controversial *Oryx* mechanism.<sup>7</sup> As was pointed out above, many South African writers have criticised the court in *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd*<sup>8</sup> for not spelling out the precise construction of preference contracts and thus of the *Oryx* mechanism.<sup>9</sup> Several important questions affecting the operation of preference contracts remain uncertain as a result.<sup>10</sup> The closest the court came to explaining the legal nature of the *Oryx* mechanism was to refer to the German writer Larenz's explanation that the *Vorkaufsrecht* of the German civil code (*BGB*)<sup>11</sup> is a *Gestaltungsrecht*.<sup>12</sup> This, said the court, is a right to create a contract with the same contents as the contract concluded with the third party through a unilateral declaration of will.<sup>13</sup> The court left its discussion of German law at that. Since the concept of a *Gestaltungsrecht* to create a contract is not known to our case law, research into German law could be helpful to gauge whether that

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<sup>5</sup> 1967 3 SA 310 (A) *per* Botha JA.

<sup>6</sup> *Soteriou v Retco Poyntons supra* 932 *per* Nicholas JA for the majority.

<sup>7</sup> *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd* 1982 3 SA 893 (A) 907H.

<sup>8</sup> *Supra*.

<sup>9</sup> See chapter 1 *supra*. The court's failure to do so leaves the impression that a fiction has been introduced into our law, with all the resultant dangers flowing therefrom. *Hirschowitz v Moolman* 1985 3 729 (A) 763I-J; *Radesich* 1985 *De Jure* 407 409; see chapter 1 *supra*.

<sup>10</sup> So, for example, it is unclear what transactions or actions by the grantor or third parties would trigger the availability of the *Oryx* mechanism, and whether a contract of preference must always comply with the formalities prescribed by the Alienation of Land Act 68 of 1981. The court expressly left open these issues at 908F-G.

<sup>11</sup> *Bürgerliches Gesetzbuch*.

<sup>12</sup> 907H. See Larenz *Lehrbuch des Schuldrechts II.1* 13th edition (1986) 151. (The court in *Oryx* referred to the 12th edition.)

<sup>13</sup> 907H.

concept provides a sufficiently clear juridical explanation of rights of pre-emption, which may facilitate a coherent solution to the issues surrounding contracts of pre-emption.<sup>14</sup>

A study of American<sup>15</sup> law is also justified by the reliance in *Oryx*<sup>16</sup> and *Soteriou v Retco Poyntons (Pty) Ltd*<sup>17</sup> on the American writer Corbin. The court in *Oryx* quoted Corbin's statement that when the grantor accepts a third party offer without first offering to contract with the holder, this breach also has the effect of an offer to sell to the holder on the same terms which gives the holder a power of acceptance.<sup>18</sup> The quotation from Corbin contains no explanation why the breach suddenly conjures up an offer. Further investigation may reveal a coherent explanation.

As the literature on the basic construction of preference contracts is more extensive in German law than in English or American law, I will first consider German law.

## 4 1 German Law

German law indeed recognises a number of different types of preference contracts, or *Vorrechtsverträge* in the wide sense.<sup>19</sup> The only institution regulated in the *BGB* is the

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<sup>14</sup> For example those set out in n 10 *supra*.

<sup>15</sup> As in "from the United States of America."

<sup>16</sup> *Supra*.

<sup>17</sup> *Supra*.

<sup>18</sup> Corbin *Corbin on Contracts: A Comprehensive Treatise on the Working Rules of Contract Law Vol 1A Sections 152-274* (1963) § 261 (hereafter cited as *Corbin Corbin on Contracts Vol 1A*) p 473-4, quoted at 907H-908B: "When O [grantor] receives an offer from C [a third party], his acceptance of that offer without first offering it to B [holder] on the same terms is a breach for which B can recover damages, but it also has the effect of an offer to sell to B, giving him a power of acceptance. O's promise to make that offer is specifically enforceable, and if B gives notice of acceptance he consummates a contract to sell on the terms offered by C and accepted by O. He can get a decree for specific performance against both O and C, unless C has already received conveyance and is protected as an innocent purchaser for value."

<sup>19</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* (1965) 296; Wagner "Gestaltungen im Vorfeld des endgültigen Vertragsabschluss" 2000 *NotBZ* 69 76-77. Lorenz "Vorzugsrechte beim Vertragabschluss"

*Vorkaufsrecht*.<sup>20</sup> The other types are recognised because of the principle of freedom of contract.<sup>21</sup>

In a manner of speaking, the *Vorkaufsrecht* entitles the holder to “step into the shoes” of a third party with whom the grantor has contacted, albeit by causing a second contract to come into existence upon the holder's declaration exercising the *Vorkaufsrecht*.<sup>22</sup> Preference rights aimed at other types of contract than sale, for example lease, are also sometimes constructed analogously to the *Vorkaufsrecht*. The term *Eintrittsrechte*<sup>23</sup> has been used to describe a wide category of preference rights including *Vorkaufsrechte* and such similarly constructed rights, such as the *Vormietrecht* and *Vorpachtrecht*.<sup>24</sup> A sub-

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in FS Dölle *Vom deutschen zum europäischen Recht I* (1963) 103 uses the term *Vorzugsrechte* for the overarching category of preferential rights to transact.

<sup>20</sup> In §§ 463-473 *BGB* (previously §§ 504-514) and §§ 1094-1104 *BGB*. Several statutes create *Vorkaufsrechte*, for example in favour of lessees or communities. The primary rights and duties of the parties in these other forms of *Vorkaufsrechte* are the same as that of the contractual *Vorkaufsrecht* (Hahn “Rechtsgeschäftliche Vorkaufsrechte im Rahmen von Grundstückskaufverträgen” 1994 *Mitteilungen der Rheinischen Notarkammer* 193 194).

<sup>21</sup> Hueck “Erwerbsvorrechte im Gesellschaftsrecht” in Paulus *et al* (eds) *Festschrift für Karl Larenz* (1973) 749 752.

<sup>22</sup> See § 464 *BGB* (previously § 505) and commentaries thereon, such as Grunewald in Westermann (ed) *Erman Bürgerliches Gesetzbuch* 10<sup>th</sup> edition (2000) (hereafter cited as *Erman* (Grunewald)) § 505; Westermann in Westermann (ed) *Münchener Kommentar zum Bürgerlichen Gesetzbuch 3.I Schuldrecht Besonderer Teil* (§§ 433-606), *VerbrKG, HausTWG, MHG* 3<sup>rd</sup> edition (1995) (hereafter cited as *Münchener Kommentar* (Westermann)) § 505 RdNr 1; Huber in Mertens (ed) *Bürgerliches Gesetzbuch mit Einführungsgesetz und Nebengesetzen Kohlhammer-Kommentar begründet von Hs Th Soergel & W Siebert 3: Schuldrecht II* (§§ 433-515) *AGB-Gesetz, AbzG, EAG, EKG, UN-KaufAbk* 12<sup>th</sup> edition (1991) (hereafter cited as *Soergel & Siebert* (Huber)) § 505 RdNr 3. See also Schurig *Das Vorkaufsrecht im Privatrecht* (1975) 19 and Larenz *Lehrbuch des Schuldrechts* § 44 III. In this respect, the *Vorkaufsrecht* is similar to the *Oryx* mechanism.

<sup>23</sup> Literally, “step-in rights.”

<sup>24</sup> Röser *Ankaufsrecht, Vorhand, Einlösungsrecht und Option: Ein Beitrag zur Lehre von den gesetzlich nicht geregelten Anrechten zum Kauf* (1938) 23. These rights are not specifically regulated in the *BGB* but contract drafters and commentators have tended to construe them like the *Vorkaufsrecht*. See Nipperdey “Über Vorhand, Vorkaufsrecht und Einlösungsrecht” 1930 *Zeitblatt für Handelsrecht* 300 302ff; Röser

type of *Eintrittsrechte* which are wider than *Vorkaufsrechte*, are the *Einlösungsrechte*<sup>25</sup> which are triggered by the conclusion of any type of contract aimed at alienation of the object, such as sale, exchange and donation.<sup>26</sup>

Apart from *Eintrittsrechte* in the above sense, German law also knows contracts that create a *Vorhand*<sup>27</sup> for the holder. Any agreement that obliges the grantor to first give the holder an opportunity to contract before the grantor contracts with a third party falls into this group of contracts. This is of course the way in which preference agreements are usually worded in South Africa.<sup>28</sup> In Germany, such wording, which prohibits the grantor from first contracting with a third party, excludes the application of the *Vorkaufsrecht*.<sup>29</sup>

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*Ankaufsrecht* 23; BGH decision of 25.11.1987 reported in 1988 *Wertpapier Mitteilungen* 92 (in respect of a *Vorpachtrecht*). So for example, a *Vormietrecht* is understood as the right of the holder to unilaterally create a lease contract upon the owner concluding a contract of lease with a third party (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 297; Michalski “Der Mietvorvertrag” 1999 *Zeitschrift für Miet- und Raumrecht* 141 146). However, this term is sometimes used to denote the rights to take over a contract between the grantor and the third party, such as a long-term contract for the supply of energy or goods. See for example *Soergel & Siebert* (Huber) Vor § 504 RdNr 18 (now § 463); Bassenge *et al* (eds) *Palandt Bürgerliches Gesetzbuch* 60<sup>th</sup> edition (2001) (hereafter cited as *Palandt*) Vorbem § 504 RdNr 12 (now § 463).

<sup>25</sup> Literally, “rights to redeem”.

<sup>26</sup> See, for example, *Soergel & Siebert* (Huber) § Vor 504 RdNr 19 (now § 463); Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 302; Röser *Ankaufsrecht* 21. It has also been used in an even wider sense to refer to any conditional right to create a contract or obligation by unilateral declaration, where the condition need not necessarily be the conclusion of a contract with a third party (Roser 21-22). See however *Münchener Kommentar* (Westermann)§ 504 RdNr 6 (now § 463) who uses the term *Einlösungsrechte* to include *Vormiet-* and *Vorpachtrechte* as well.

<sup>27</sup> Literally, “forehand”, figuratively, “preference”.

<sup>28</sup> See par 2 1 1 *supra* and par 7 3 *infra* where some typical formulations encountered in the case law are set out.

<sup>29</sup> RG SeuffA 74, 232 (30.5.1919) 284 and RG SeuffA 81, 360 (17.9.1929) 361 which emphasise that the contract with a third party is a necessary prerequisite (precondition) for a *Vorkaufsrecht*. See also RG 169, 65 (30.03.1942) 69 where the court refused to treat an agreement that if the grantor wants to sell, the holder shall have a *Wiederkaufsrecht*, as a *Vorkaufsrecht* as the “exercise of the right is not made dependant on the prior conclusion of a contract with a third party” (my translation); Hueck “Erwerbsvorrechte” 752;

Why this is so will appear from the closer investigation of each institution hereunder. That the customary wording of South African preference contracts would indeed put them into the scope of *Vorhand* and not *Vorkaufsrecht* contracts means that the different types of *Vorhand* contracts of German law must be carefully considered. A key outcome to be pursued is a verdict on which sub-type of *Vorhand* contract is to be regarded as the default construction, that is, the construction which should apply where the contract contains a cryptic formulation which does not exhaustively regulate the parties' primary rights, duties and remedies. As has been pointed out above, such very cryptic drafting is apparently common practice in South Africa.

The discussion hereunder will focus on the normal constructions of the various types of preference contracts. German law recognises that the parties may deviate from the normal construction, including the *BGB* rules on the *Vorkaufsrecht*.

## **4 1 1 The *Vorkaufsrecht***

### *4 1 1 1 Basic construction*

The *Vorkaufsrecht* is a deliberate creation of the drafters of the *BGB*. It does not correspond to either the Roman law *ius protimeseos* or the Germanic *ius retractus*, although it certainly bears a marked resemblance to the latter institution.<sup>30</sup>

One distinctive characteristic is that the right can only be exercised upon a completed valid contract with a third party.<sup>31</sup> Three major practical reasons swayed the drafters of

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Michalski 1999 *Zeitschrift für Miet- und Raumrecht* 141 146; Weber "Der Optionsvertrag" 1990 *Juristische Schulung* 249 251. See also Bappert & Wagner *Rechtsfragen des Buchhandels* 2<sup>nd</sup> edition (1958) 155, par 20.4 who specifically distinguish the *Vorrechtsvertrag* generally used in the publishing industry (which amounts to a *Vorhand*) from the *Vorkaufsrecht* on this basis.

<sup>30</sup> Schurig *Das Vorkaufsrecht* 59-60.

the *BGB* to limit the trigger event to a contract of sale with a third party. Firstly, it was felt that before conclusion of a contract with a third party, there is no certain basis for the decision of the holder whether to exercise the right.<sup>32</sup> In other words, the terms on which the holder may acquire the object was considered to be too unclear if anything short of conclusion of a contract triggers the right.<sup>33</sup> The drafting commission accordingly rejected proposals that the grantor should be obliged to make an offer to the holder before he has contracted with a third party.<sup>34</sup> Secondly, as long as no binding contract with the third party has been concluded, the holder is not in danger of losing her *Vorkaufsrecht* (through transfer to a *bona fide* third party) and should therefore not be forced to decide about the exercise of her right before that point.<sup>35</sup> Thirdly, if some circumstance short of a binding contract could force the holder to decide about the exercise of her right, there is a danger of the grantor faking an offer which the grantor knows the holder would not accept. This would force the holder either to buy the property at such exorbitant terms or to waive the *Vorkaufsrecht* by failing to exercise it.<sup>36</sup>

Accordingly, the grantor is not obliged to refrain from contracting with a third party until he has first offered to contract with the holder. In other words, there is no *obligatio non faciendi*, which is seen as characteristic of rights of pre-emption in South African law.

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<sup>31</sup> § 463 *BGB* (previously § 504 *BGB*). See also *Erman* (Grunewald) § 504 RdNr 8 (now § 463) and the authorities in n 29 *supra*.

<sup>32</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 16; Schurig *Das Vorkaufsrecht* 56 with reference to *BGB Motive II* 345 *et seq.*

<sup>33</sup> That is, if a “manifestation of a desire to sell” would trigger the right, which does not amount to a contract with or offer to a third party, it would be disputable on what terms the holder would be entitled to contract with the grantor. Some vague standard such as “reasonable terms” would then be required, which would invariably lead to disputes.

<sup>34</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 16-17; Schurig *Das Vorkaufsrecht* 56; *Soergel & Siebert* (Huber) § 504 RdNr 17 (now § 463) with reference to *Protokolle II* 96 *et seq.* See also BGHZ 115, 355 (decision of the *Bundesgerichtshof* of 11.10.1991) 338 *in fine*; Hueck “Erwerbsvorrechte” 752, 755; Michalski 1999 *Zeitschrift für Miet- und Raumrecht* 141 146.

<sup>35</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 19, with reference to *Protokolle II* 96 *et seq.*

<sup>36</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 19; Schurig *Das Vorkaufsrecht* 56; Weber 1990 *Juristische Schulung* 249 251.

Contracting with a third party without first having given the holder the opportunity to do so is not breach of a *Vorkaufsrecht*. Instead, it is a neutral trigger event or condition for the holder's right to become operative.<sup>37</sup> Any agreement worded to the effect that there is a duty to refrain from selling to a third party unless the holder has first been given a chance to contract, therefore excludes the *Vorkaufsrecht*.<sup>38</sup>

Because of this distinctive characteristic, the term *Vorkaufsrecht* is somewhat of a misnomer. As the holder's right arises, or becomes operative, only after the sale to a third party, it is rather like the *nacoopsrecht* discussed in the previous chapter, which could be translated as *Nachkaufsrecht*.

A second distinctive characteristic of the *Vorkaufsrecht* is that the holder may bring a contract into existence by unilateral declaration without any further declaration of will by the grantor being required.<sup>39</sup> It thus gives the holder a conditional power to create a

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<sup>37</sup> Although the Austrian Civil Code (art 1072 ABGB) seems to suggest the existence of an *obligatio non contrahendo cum tertii*, a number of Austrian writers and some courts have also accepted that there is no breach if the grantor only offers to the holder after conclusion of the third party contract. Their view results from influence from the *BGB Vorkaufsrecht* and has been described as *contra legem* by Schurig *Das Vorkaufsrecht* 53. See for example 1964 *Evidenzblatt* 239 240 where Austria's highest court followed Klang and Ehrenzweig's opinion that the offer to the holder can be made before or after conclusion of the contract with the third party. The court's statement is based on the view that making the offer after conclusion of the third party contract is not breach. (The statement in the text should not be taken to mean that no binding contract can exist pending fulfilment of a suspensive condition to which the contract is subject. Contracts are valid and binding even before fulfilment of the condition. See Westermann in Säcker (ed) *Münchener Kommentar zum Bürgerlichen Gesetzbuch I Allgemeiner Teil* (§§ 1-240) *ABG-Gesetz* 4<sup>th</sup> edition (2001) (hereafter cited as *Münchener Kommentar* (Westermann) § 158 RdNr 39)).

<sup>38</sup> RG Seuff A 81, 360; RGZ 154, 355; Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 300, 302.

<sup>39</sup> § 464 *BGB* (previously § 505). In *Oryx*, the court focused on this second characteristic, which came to be known as the *Oryx* mechanism, but equated it to a remedy for breach of the right of pre-emption, which it is not in the case of a *Vorkaufsrecht*, as there is no question of breach until after the holder has exercised the *Vorkaufsrecht* in response to the contract concluded with the third party.

contract.<sup>40</sup> This contract will have the same terms as those agreed with the third party, unless the parties have agreed otherwise in the preference contract.<sup>41</sup> If the grantor refuses to transfer the object of the right to the holder, the holder can pray directly for performance in terms of the contract of sale that was created by unilateral declaration.

#### 4 1 1 2 *Explanation of legal nature*

The legal nature of the *Vorkaufsrecht* is not determined by the *BGB* and has always been controversial.<sup>42</sup>

A tempting juridical explanation is that the agreement granting the *Vorkaufsrecht* is in fact a conditional offer or conditional option, where the condition is the conclusion of a contract with a third party.<sup>43</sup> The terms of the offer are the terms on which the grantor agrees to contract with a third party. These terms become fixed upon the fulfilment of the condition. The unilateral declaration of the holder that brings a contract of sale into existence, is simply the acceptance of the offer.<sup>44</sup>

However, the *BGB* contains some rules on the *Vorkaufsrecht* which are arguably inconsistent with a conditional option construction. One is an express provision that whereas an agreement granting a *Vorkaufsrecht* in respect of land must comply with the formalities prescribed for a sale of land, the holder's unilateral declaration may be form-

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<sup>40</sup> RG SeuffA 81, 360 361 (“...Das Vorkaufsrecht im Sinne des BGB [gibt] dem Berechtigten eine durch Verkauf bedingte Befugnis...”).

<sup>41</sup> § 464 *BGB*.

<sup>42</sup> See all the major commentaries on §§ 504 *et seq* *BGB* (now §§ 463 *et seq*).

<sup>43</sup> As a conditional option, the operation of the option is postponed until fulfilment of the condition, but the option contract binds the parties thereto in the interim. See §§ 158-160 *BGB*; *Münchener Kommentar* (Westermann) § 158.

<sup>44</sup> This is supported by *inter alia* Schurig *Das Vorkaufsrecht* 89ff and Weber 1990 *Juristische Schulung* 249 250. Cf *Erman* (Grunewald) § 504 RdNr 5 (now § 463) (“The *Vorkaufsrecht* is an option” (my translation)).

free.<sup>45</sup> As acceptance of an offer must also comply with formalities, a number of writers and courts have rejected the view that the holder's unilateral declaration is an acceptance of an offer embedded in the initial agreement.<sup>46</sup> Instead of merely accepting that the legislator has chosen to deviate from the normal formalities requirements set by itself,<sup>47</sup> they have come up with all sorts of other theories as to the legal nature (a coherent explanation of the construction) of the *Vorkaufsrecht*.

One rather contrived explanation is that the initial agreement is in fact a doubly conditional contract of sale that already complies with the formalities requirements.<sup>48</sup> The first condition is the conclusion of a contract with a third party and the second the holder's unilateral declaration that it wants to buy on the terms agreed with the third party. As the holder's declaration is therefore not the acceptance of an offer, it need not comply with the formalities legislation. Opponents of the "doubly conditional sale"

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<sup>45</sup> § 464(1) *BGB* (previously § 505 (1)).

<sup>46</sup> Cf *Erman* (Grunewald) § 504 RdNr 7 (now § 463).

<sup>47</sup> This would be a sensible deviation as the purpose of the formalities requirements is met if the preference contract and contract with the third party are in writing as the terms on which the holder would contract with the grantor are then clear and both parties are warned about these terms. The relevance for South African lawyers of this debate is that where a specific clause can amount to a *Vorkaufsrecht* type preferential right, there are arguments both ways as to whether the holder's declaration must be in writing or not. What is true is that any construction which includes the second distinctive element of the *Vorkaufsrecht* (the contractual power or *Oryx* mechanism) should accept that the initial preference agreement must comply with the formalities, as no further expression of consent to contract with the holder is required from the grantor before the contract of sale comes into existence.

<sup>48</sup> This is the predominant view of the courts (*Münchener Kommentar* (Westermann) § 504 RdNr 7; Mader in Honsell (ed) *J von Staudinger's Kommentar zum Bürgerliches Gesetzbuch mit Einführungsgesetz und Nebengesetzen 2: Recht der Schuldverhältnisse §§ 433-534* 13<sup>th</sup> edition (1995) (hereafter cited as *Staudinger* (Mader)) Vorbem zu §§ 504 ff RdNr 25; *Erman* (Grunewald) § 504. This construction is preferred by writers such as *Soergel & Siebert* (Huber) Vor § 504 RdNr 7-9 (now § 463). The doubly conditional sale construction is especially contrived as it ignores the express provision of § 464 according to which the sale between the grantor and holder comes into existence upon the exercise of the *Vorkaufsrecht* by the holder (and not at an earlier stage). For further criticism see Medicus *Schuldrecht II Besonderer Teil: Ein Studienbuch* 9<sup>th</sup> edition (1999) § 83 p 79ff; Larenz *Lehrbuch des Schuldrechts* § 44 III.

construction argue that the second condition is a clear admission that the *essentialia* of a contract of sale do not exist at all at conclusion of the preference contract. The holder does not necessarily want to buy from the grantor at all at that stage. The holder of a right of pre-emption often has an interest in remaining free to decide whether she wants to contract or not at the time the grantor decides to contract. This "choice" or "option" to contract is of the essence of an option and not of a contract of sale. This criticism suggests a further objection against the conditional option construction. Just as the holder does not want to buy at the conclusion of the preference contract, so the grantor does not want to sell at that stage, which is the essence of an offer.<sup>49</sup> A reply that in any conditional option the grantor does not want to sell until the condition occurs is unconvincing. Where the condition is an uncertain future event not dependent on the cooperation or will of the grantor, the grantor must perforce now intend to sell in the knowledge that she will have no control over the fulfilment of the condition. On the other hand, commercial reality knows and needs options subject to conditions over the fulfilment of which the grantor has some control. An example would be an agreement that if the owner of a piece of land should ever start using a piece of land for dock purposes, which was previously used for racecourse purposes, his neighbour would have an option to buy it at R200 000.<sup>50</sup> German writers point out that the economic need to recognise contracts subject to at least partly potestative conditions ("mixed conditions"), means that a blanket objection to potestative conditions as inconsistent with a serious intention to be bound (an *essentiale* for any contract) is redolent of a formalistic *Begriffsjurisprudenz* approach.<sup>51</sup> A more functional approach is to consider the reasons for the unacceptability of potestative conditions and test any specific potestative condition against such reasons before rejecting it as inconsistent with an intention to be contractually bound. Only potestative conditions which cause liability to be dependent on the mere *ipse dixit* of a party are objectionable simply because such a contract could

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<sup>49</sup> Laue *Begriff und Wesen des Vorkaufsrechts nach BGB* (1905) 20.

<sup>50</sup> Cf the facts of *Manchester Ship Canal Company v Manchester Racecourse Company supra*. Another example would be an option of purchasing any premises that might be designated for the purposes of a dairy on the south side of a certain road (cf *Ryan v Thomas* (1911) 55 Sol Jo 364.)

<sup>51</sup> Cf *Soergel & Siebert* (Huber) Vor § 504 RdNr 10; *Münchener Kommentar* (Westermann) § 158 RdNr 60.

never be enforced by a court against that party as long as he insists that he does not want to be bound. Therefore the condition that the grantor concludes a contract with a third party is not an objectionable potestative condition.<sup>52</sup> A court could enforce it against a grantor who insists that he does not want to be bound by simply pointing to the fact that a contract with a third party has been concluded. The same applies even where the condition is agreed to be an "overt act manifesting a serious desire to sell." The declaration of exercise by the holder is not an objectionable suspensive condition for the same reason.<sup>53</sup>

If the contract creating a *Vorkaufsrecht* is a conditional option or doubly conditional sales contract, it is a *sui generis* one as the *BGB* implies certain terms into such a contract which are specific to the *Vorkaufsrecht* contract (hereinafter *Vorkaufsvertrag*). One example is the grantor's duty to notify the holder that the condition has been fulfilled, after which the holder has two months in the case of immovables and one week in respect of other things to exercise the right.<sup>54</sup> Another example is the provision that the holder may exercise the *Vorkaufsrecht* as long as he is able to perform all the main obligations of the third party and as long as a money value can be placed on any subsidiary duties undertaken by the third party which the holder cannot perform.<sup>55</sup>

Perhaps this *sui generis* nature that negates a simple subsumption of the *Vorkaufsrecht* under the genus "option" or "sales contract", explains why Larenz and others are satisfied with the explanation that the *Vorkaufsvertrag* simply creates a *Gestaltungsrecht* for the

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<sup>52</sup> In BGHZ 72, 385, the court described such a condition as a mixed condition. Cf *Münchener Kommentar* (Westermann) § 158 RdNr 60.

<sup>53</sup> In any event, even if the second condition under the conditional sale construction is regarded as a purely potestative condition in the form of the holder being willing to buy, it does not prejudice anybody, as it would normally be the holder who seeks enforcement of the *Vorkaufsrecht* contract and not the grantor. Therefore there is no prospect of a denial by the holder that he wishes to buy.

<sup>54</sup> § 469 *BGB* (previously § 510).

<sup>55</sup> § 466 *BGB* (previously § 507).

holder to establish a contract by unilateral declaration.<sup>56</sup> *Gestaltungsrechte* are all those rights that allow a party by unilateral declaration to establish, alter or terminate bilateral juristic relationships like contracts.<sup>57</sup> An example of another type of *Gestaltungsrecht* is the right to terminate an existing contract by unilateral declaration, whether upon notice or after breach. The *Vorkaufsrecht*, as the right to create a bilateral juristic relationship by unilateral act, is said to be analogous to a declaration to terminate a contract upon breach. Such a declaration of cancellation not only terminates an existing obligation, but also gives rise to a bilateral juristic relationship with bilateral rights and duties, or at least changes the existing obligation.<sup>58</sup>

The main criticism against this theory is that nothing is gained by the categorisation of a *Vorkaufsrecht* as a *Gestaltungsrecht*, as it does not explain where the *Gestaltungsrecht* comes from.<sup>59</sup> The *Gestaltungsrecht* theory is said to be abstract, vague and meaningless.<sup>60</sup> The obvious response to this criticism is that the *Gestaltungsrecht* is simply the result of an implied term in the preference contract, which arises *ex lege* on the basis of statutory interpretation of the *BGB*. Alternatively, it can be explained as the result of an implied term derived from the normal grounds for implying such term, for example consensus and efficiency.<sup>61</sup> No other explanation of the origin of other types of

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<sup>56</sup> BGHZ 102, 240; BGHZ 32, 375 383; Larenz *Lehrbuch des Schuldrechts* § 44 III; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 268.

<sup>57</sup> See Larenz *Lehrbuch des Schuldrechts* § 44 III; BGHZ 102, 240; Medicus *Schuldrecht II* § 83; Dietl *et al Wörterbuch für Recht, Wirtschaft und Politik II* (1983) sv *Gestaltungsrecht*. Secker's article "Lehre von Gestaltungsrechte" in *Festschrift für R Koch* (1903) 23 *et seq* is the *locus classicus*.

<sup>58</sup> Larenz *Lehrbuch des Schuldrechts* § 44 III. For example, it gives rise to the duty of mutual restitution.

<sup>59</sup> Schurig *Das Vorkaufsrecht* 66-67 agrees that it can be a *Gestaltungsrecht*, but prefers the conditional option construction as it explains that the *Gestaltungsrecht* is a power of acceptance arising from the offer embedded in the preference agreement. Cf Röser *Ankaufsrecht* 24-25. See also Laue *Begriff und Wesen des Vorkaufsrechts* 22-23, who states that merely supplying more examples of analogous rights does not explain the creation of a contract by unilateral declaration.

<sup>60</sup> *Soergel & Siebert* (Huber) Vor § 504 RdNr 9.

<sup>61</sup> See further par 6 2 on the determinants of *ex lege* implied terms. The preference contract itself is also the source of the subsidiary obligations of the grantor, such as the duty to inform the holder of a contract

*Gestaltungsrechte* exists anyway and it is all that is needed. Therefore the *Vorkaufsvertrag* can be seen as a special type of contract which gives rise to a *Gestaltungsrecht* for the holder.<sup>62</sup>

South African law does not know the concept of a *Gestaltungsrecht*, but the concept of a contractual power is similar.<sup>63</sup> The Supreme Court of Appeal has recognised that parties may agree that one may have the power to (unilaterally) amend the contents of the

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concluded with a third party. Röser's criticism that the *Gestaltungsrecht* theory does not deal with these subsidiary obligations is therefore unfounded (*Ankaufsrecht* 25).

<sup>62</sup> Schurig *Das Vorkaufsrecht*'s rebuttal to this defence of the *Gestaltungsrecht* construction (at 72-73) is that contractual freedom grants parties the power to establish (only) *obligations* between parties within the system of the law of obligations. He states that the contractual establishment of an "abstract *Gestaltungsrecht*" which has nothing to do with the underlying contract conflicts with this system. However, this criticism can be met by the reminder that the preference contract is indeed the "underlying contract" in which the parties can be taken to have agreed on a *Gestaltungsrecht*. Therefore the *Gestaltungsrecht* has something to do with the underlying contract. Neither can it be said that no present obligation is established by the "underlying contract" (*Vorkaufsvertrag*): the duty to inform the holder of the conclusion of a third party contract exists from conclusion of the *Vorkaufsvertrag*. Neither is it true to suggest that the system of the law of obligations only allows the creation of obligations. Contractual freedom also allows the creation of *Gestaltungsrechte*, such as the right to accept an offer that must be left open due to the existence of an option contract, even where the grantor purports to retract the offer. (Although offers are generally irrevocable in German law anyway, the concept of an option contract is known as well. See generally Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 227 *et seq*; Linneborn *Das Optionsrecht* (1936)). If Schurig means to say that such a *Gestaltungsrecht* has to be agreed on expressly in the underlying contract before it can be said to have "anything to do with" the underlying contract, consistency would require that he also expects parties to a preference contract to agree expressly that an option is granted. This last point perhaps shows up the fact that the *Vorkaufsrecht* is a deliberate construction of the legislator, and perhaps not one which parties would naturally agree upon were it not for lawyers educated about the existence and construction of the *Vorkaufsrecht*. (Parties would normally rather agree on the *Vorhand* where they intend that the grantor must prefer the holder).

<sup>63</sup> See especially Cockrell "Second-guessing the exercise of contractual power on rationality grounds" 1997 *Acta Juridica* 27; Hahlo & Kahn *The South African Legal System and its Background* (1968) 81-82. Cockrell defines a "power" in Hohfeldian terms as the ability to alter the existing legal condition of another for better or worse.

contract.<sup>64</sup> Of course, it is also recognised that a party may be granted a right to unilaterally cancel a contract. The remedy of cancellation upon breach, which is exercised extra-judicially, is such a power. An offeree has the power to accept an offer. Perhaps it has conceptual value to recognise a concept that encompasses all such powers for South African law. *Gestaltungsrecht* is not easily translatable. It has been translated as dispositive right.<sup>65</sup> The use of the term right in this context may be misleading, as it appears to refer to a personal right, which entitles one to a performance and implies a corresponding duty to perform. If one must identify a corresponding duty to perform for the grantor of the *Gestaltungsrecht* it is simply to allow the holder of the right to exercise the *Gestaltungsrecht*, that is to establish, vary or terminate the contract between the parties. Accordingly, the term contractual power is preferable.

I agree that the *Gestaltungsrecht* theory is a sufficient explanation of the *Vorkaufsrecht*. However, no cogent criticism can be brought against the conditional option theory either.<sup>66</sup> It is probably helpful to regard the *Vorkaufsvertrag* as a conditional option contract with special subsidiary rules. It provides a coherent understandable explanation of the holder's power as a power of acceptance of an offer, a concept well known to contract law.<sup>67</sup>

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<sup>64</sup> *NBS Boland Bank v One Berg River Drive CC* 1999 4 SA 928 (SCA). See also Lubbe "Kontraktuele diskresies, potestatiëwe voorwaardes en die bepaaldheidsvereiste" 1989 *TSAR* 159.

<sup>65</sup> Romain *et al* *Wörterbuch der Rechts- und Wirtschaftssprache Teil II Deutsch-Englisch* 3<sup>rd</sup> edition (1994) 364.

<sup>66</sup> Admittedly, it does not explain the statutory *Vorkaufsrechte* (Larenz *Lehrbuch des Schuldrechts* § 44 III; *Münchener Kommentar* (Westermann) § 504). They are indeed only *Gestaltungsrechte*. However, it is a coherent explanation of contractual *Vorkaufsrechte*, apart from the fact that the detailed default rules relating to the *Vorkaufsrecht* were chosen as a matter of policy by the legislator and do not flow from the legal nature of the *Vorkaufsrecht*. See at n 54 and 55.

<sup>67</sup> Two other theories with only marginal support, namely the *Vorvertrag* and *Ermächtigung* theories will not be discussed in depth here. According to Laue, the only proponent of the *Ermächtigung* theory, the holder is granted the power or authority to contract with himself on the grantor's behalf on the conclusion of a third party contract (*Begriff und Wesen des Vorkaufsrecht* 15 ff). Accordingly, it does not add much to the *Gestaltungsrecht* theory. According to the *Vorvertrag* theory the grantor undertakes a duty to contract with the holder in future. When the grantor contracts with a third party, it has the effect of an offer by the

#### 4 1 1 3 *Field of application*

As has been stated earlier the *Vorkaufsrecht* does not apply where the agreement is worded in such a way that the grantor must first allow the holder an opportunity of contracting before the grantor contracts with a third party.<sup>68</sup>

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grantor (cf Schurig *Das Vorkaufsrecht* 62-63; Laue *Begriff und Wesen des Vorkaufsrechts* 18-19). Both theories amount to fictions and are not coherent explanations of the holder's power to create a contract by unilateral declaration. See also *Staudinger* (Mader) Vorbem zu § § 504 ff RdNr 29. A number of commentators like *Staudinger* (Mader) Vorbem zu § § 504 ff RdNr 28-30, *Münchener Kommentar* (Westermann) § 504 RdNr 7 and *Soergel & Siebert* (Huber) Vor § 504 RdNr 7 and *Medicus Schuldrecht II* § 83 p 79-80 downplay the importance of the effort to seek a coherent juristic explanation of the *Vorkaufsrecht* construction. They imply that the juristic construction should not be seen as influencing the practical consequences of the *Vorkaufsrecht*, but is merely a way to order the *Vorkaufsrecht* as simply and logically as possible into contract law doctrine. They emphasise that the specific questions surrounding the *Vorkaufsrecht* should not be decided on the basis of any theory or terminological categories, but rather on the basis of the *ratio legis* and the balance of interests (see especially *Soergel & Siebert* (Huber) Vor § 504 RdNr 9 and OLG Karlsruhe NJW-RR 90, 935). However, some writers like Larenz *Lehrbuch des Schuldrechts* § 44 III maintain that a coherent explanation has practical consequences, such as the prevention of wrong decisions, and that the legal order cannot be fully and correctly understood in the absence of such systematic components. The fact that the system should be open to change does not mean that the systematic ordering of the legal system becomes worthless. See also Schurig *Das Vorkaufsrecht* 16.

<sup>68</sup> Can the interpretation that the *Vorkaufsrecht* is excluded simply because the contract speaks of a duty to offer before contracting with a third party be questioned as a literalistic approach? Should the agreement not be construed like a *Vorkaufsrecht* in any event? In 1930 *Juristische Wochenschrift* 3766 the Reichsgericht had to construe the following clause: "At the termination of this contract the publisher may only grant the right to collect subscriptions to another firm, if the holder rejects the takeover of such collection at the terms offered by the other firm or if the holder has not declared itself willing to take over the collection at such terms within 8 days of being informed of such terms." (My translation.) On the face of it this intends that before the grantor may contract with a third party it would first grant the holder the opportunity to do so, a classical *Vorhand* situation. The *Landesgericht* interpreted the clause as a negative duty, namely that the grantor has no enforceable duty to inform the holder of terms offered by a third party firm, but that the grantor may simply not contract with a third party firm if the grantor had not so informed

As the *Vorkaufsrecht* is the only preferential right to transact governed in the *BGB*, it applies as the default construction where an agreement, will or statute simply states that one party will have the *Vorkaufsrecht* in respect of a certain property.

One variation to the *BGB* implied terms, which still cause the agreement to retain the two distinctive characteristics of *Vorkaufsrechte*, is an agreement that the holder will have the *Vorkaufsrecht* to buy the property at a specified price. In that case, the grantor will still have no duty to refrain from contracting with a third party until the holder has been given an opportunity to contract. The holder will also still have the power to bring the contract of sale into existence at conclusion of a third party contract.

Another possible variation of the *BGB Vorkaufsrecht* is an agreement that the holder will already have a *Vorkaufsrecht* upon the grantor manifesting a desire to sell. In such a case an interpretation that no *obligatio non faciendi* is intended is still possible. In other words it could still be intended to be a *Vorkaufsrecht* in the sense that the manifestation of a desire to sell is not a breach, but merely a neutral trigger event which entitles the holder to bring the contract of sale into existence by unilateral declaration. Only if the

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the holder or where the holder declared itself willing to contract on the terms of which it was informed (3767). Thus the holder's remedy was limited to damages and the continuation of the present relationship, but not an order that the grantor inform it of the terms offered by a third party. On appeal the *Reichsgericht* called this negative construction "impossible" and "contrary to the true will of the parties". In this the court was influenced by its presupposition that the parties intend that the holder should have the right to step into a contract with a third party. Accordingly, said the court, the parties must have intended according to good faith to also give the holder the means by which he could exercise this right. Therefore he must be informed of a third party offer. Accordingly the court read in a *Vorkaufsrecht* construction. The problem with the court's reasoning is that it never justifies its presupposition that the parties intend the holder to step into the shoes of a third party. This presupposition is clearly based on the court's view that the *Vorkaufsrecht* is the only possible construction. It never mentions the *Vorhand* construction. The court simply decided that the provisions of the *Vorkaufsrecht* should be applied to the present case. The court simply ignored the wording of the agreement and found that the parties intend that the holder should have the right to step into a contract concluded with a third party.

grantor thereafter fails to perform the contract of sale, can breach be spoken of. In terms of the option construction, the condition would be the manifestation of a desire to sell. If the parties did not agree on the price at which the holder may create a contract, the *BGB* default rules dealing with any contract where no price is mentioned, will apply.<sup>69</sup>

#### 4 1 2 The *Vorhand*

The holder is granted a *Vorhand* when the grantor agrees to give the holder the preference above other interested parties in respect of an intended transaction.<sup>70</sup>

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<sup>69</sup> The terms which a third party offers and which the grantor is willing to accept is the starting point. However, where he just plans to sell and no third party offer exists, one should first enquire whether a market value exists, which could be applied on the basis of a tacit term. See § 453 *BGB* and § 269 *BGB* according to which it should be the market price at the debtor's, that is, the holder's place of business or residence. If no tacit agreement exists as to the price, the grantor has the power to set a reasonable price. This is the implication of § 315 and § 316 *BGB*. If the price set by the grantor is unfair, the holder may apply to have it substituted by the court's determination (§ 315(3) *BGB*).

<sup>70</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 296; Schurig *Das Vorkaufsrecht* 93; Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 310; Röser *Ankaufsrecht* 18 *et seq*; Lorenz "Vorzugsrechte" 118, *Staudinger* (Mader) 515-516; Larenz "Die rechtliche Bedeutung von Optionsvereinbarungen" 1955 *Der Betrieb* 209-211; Larenz *Lehrbuch des Schuldrechts* § 44 IV (p 156-157); Medicus *Schuldrecht II* § 83 RdNr 164; *Soergel & Siebert* (Huber) Vor § 504 RdNr 14 (now § 463); *Münchener Kommentar* (Westermann) § 504 RdNr 4 (now § 463); *Münchener Kommentar* (Westermann) § 159 RdNr 59; *Palandt* Vorbem zu § 504 RdNr 11 (now § 463); *Erman* (Grunewald) § 504 RdNr 5 (now § 463); Michalski 1999 *Zeitschrift für Miet- und Raumrecht* 141 147 (who uses the term *Anmietrecht* to denote a *Vorhand* in respect of a lease contract and *Vormietrecht* as a preferential right to lease structured like a *Vorkaufsrecht* (146-147); Hueck "Erwerbsvorrechte" 749-767; Weber 1990 *Juristische Schulung* 249 252-253; Westermann & Klingberg "Vorkaufsrechte im Gesellschaftsrecht" in Westermann & Rosener (eds) *Festschrift für Karlheinz Quack zum 65. Geburtstag* (1991) 545 552; Wolf "Rechtsgeschäften im Vorfeld von Grundstücksübertragungen und ihre eingeschränkte Berkundungsbedürftigkeit" 1995 *DNotZ* 179 192; RG SeuffA 74, 282 (decision of the Reichsgericht of 30.05.1919); RG SeuffA 81, 360 (decision of the Reichsgericht of 17.09.1927) 362; 1942 *Höchstrichterliche Rechtsprechung* 345 (decision of the OLG München of 07.07.1941); 1930 *Juristische Wochenschrift* 3766 (decision of the Reichsgericht of 05.11.1929). See also LG Offenburg 1989 *Die AG* 134 and OLG Karlsruhe 1990 *Wertpapier Mitteilungen* 725 (discussed by Westermann & Klingberg "Vorkaufsrechte im Gesellschaftsrecht", especially at 556,

Although *Vorhand* contracts can take a number of different forms,<sup>71</sup> the common denominator in most *Vorhand* contracts is an agreement that the grantor should not contract with a third party before giving the holder a chance to do so.<sup>72</sup> This group of preference contracts has also been called *Vorrechtsverträge* in the narrow sense.<sup>73</sup> As is the case in South Africa, the terminology used by parties, courts and writers are sometimes misleading and inconsistent.<sup>74</sup> For convenience's sake, I will refer to *Vorhand* contracts.

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from which it appears that the shares were subject to an *Ankaufsrecht*); BGHZ 83, 313-319 (31.03.1982). In the publishing industry the *Vorhandvertrag* is often called an *Optionsvertrag*. See for example, Bappert & Wagner *Rechtsfragen des Buchhandels* 155, par 20.4; Haberstumpf & Hintermeier *Einführung in das Verlagsrecht* (1985) 115-120 (§ 1 RdNr 44); Schrickler Bappert & Maunz: *Verlagsrecht* 3<sup>rd</sup> edition (2001) (hereafter cited as Bappert & Maunz (Schrickler) *Verlagsrecht*) 132; Brandi-Dohrn *Der urheberrechtliche Optionsvertrag: Urheberrechtliche Abhandlung des MPI, Heft 6* (1967). Apart from the *Vorkaufsrecht*, Austrian writers also identify *Vorrechtsverträge* which have been interpreted as creating an obligation to make an offer when the grantor desires to sell, as opposed to when there is a third party involved (Faistenberger *et al* *Gschnitzer: Österreichisches Schuldrecht: Besonderer Teil und Schadenersatz* 2<sup>nd</sup> edition (1988) 61).

<sup>71</sup> Allerkamp "Vorvertrag, Option und Vorhand" 1981 *Mitteilungen der Rheinischen Notarkammer* 55 62 says the term *Vorhand* is extremely vague as a number of very different agreements are understood thereby. See also Michalski 1999 *Zeitschrift für Miet- und Raumrecht* 141 147 who states that it could mean a number of things from a mere duty to inform the holder of the offers of third parties, or the grantor's intention to alienate, to a duty to make an offer. See also *Soergel & Siebert* (Huber) Vor § 504 RdNr 14 (now § 463); *Staudinger* (Mader) Vorbem zu §§ 504 *et seq* (now § 463). In its decision of 15.02.1991, the *Oberlandesgericht Hamburg* confirmed that there are various types of *Vorhand*, including the duty to refrain from contracting with third parties without an undertaking to make an offer should he decide to sell (as discussed by Kramer "Zur Unterscheidung zwischen Vorvertrag, Festofferte and Optionsvertrag – Formbedürftigkeit" 1991 *Entscheidungen zum Wirtschaftsrecht* 547-548).

<sup>72</sup> This is the common denominator in all *Vorhand* contracts except for the *Verhandlungsvorhand* which prohibits the grantor from contracting with a third party unless she has first given the holder a chance to negotiate (not necessarily to contract) with her.

<sup>73</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 298. *Vorrechtsverträge* in the wide sense would include *Vorkaufsrechte*.

<sup>74</sup> In the following cases a *Vorhand* was clearly intended yet the court used different terminology (as indicated between brackets after each case): BGHZ 9, 237 (17.04.1953) ("an option contract which creates a preference (*Vorrecht*) to conclusion of a publishing contract" (my translation)); BGHZ 126, 226-245

*Vorhand* clauses take different forms, but are often formulated as follows where they give a preference in respect of a sale: If the grantor wishes or plans to sell a specified object, he shall first offer it for sale to the holder.<sup>75</sup> The exact duty of the grantor may be expressed or understood in various ways. The grantor can undertake a duty to make an

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(*Vorkaufsrecht*). As only the unlawfulness of the price agreed upon and not the construction was in issue, the terminology did not make a difference on the facts.); 1942 *Höchstrichterliche Rechtsprechung* 345 (decision of the *Oberlandesgericht München* of 07.07.1941) (*Ankaufsrecht*). Parties have called a preference contract creating a *Vorhand* a *Wiederkaufsrecht*, for example in RG 169, 65, where it was agreed that if the grantor wants to alienate the land, the holder shall have a *Wiederkaufsrecht*. The term *Vorrecht* (preference) is wide enough to include *Vorkaufsrechte* in the sense used in the *BGB* and is therefore unsuitable to refer to *Vorhand* arrangements only. There is some uncertainty about the precise meaning of the term *Ankaufsrecht* (see especially Röser *Ankaufsrecht* 15-19; Hense "Anmerkung zur Entscheidung des OGHBrZ betreffende Ankaufsrecht" 1951 *Deutsche Notar-Zeitschrift* 124-129). Although some writers use it to denote a *Vorhand* (see for example *Soergel & Siebert* (Huber) Vor § 504 RdNr 15 (now § 463)), it mostly refers to an arrangement which South African law would call an option (Larenz 1955 *Der Betrieb* 209 211; Hueck "Erwerbsvorrechte" 752; Weber 1990 *Juristische Schulung* 249 250; cf Westermann & Klingberg "Vorkaufsrechte im Gesellschaftsrecht" 552; *Staudinger* (Mader) Vorbem zu §§ 504ff RdNr 35 *et seq* (now § 463)). Röser regards it as a right to an offer or acceptance of an offer by the other party (15-16) which he distinguishes from an option. He sees the *Vorhand* as an *Ankaufsrecht* conditional upon the grantor wishing to sell (*Ankaufsrecht* 18-19). Due to this uncertainty the term *Ankaufsrecht* will not be used to denote the *Vorhand*. Parties also sometimes use the term *Vorkaufsrecht* when it is clear that they do not mean the *BGB Vorkaufsrecht* but rather the *Vorhand* (Lorenz "Vorzugsrechte" 104; Hueck "Erwerbsvorrechte" 752; Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 335). The term *Erwerbsvorrecht* is wide enough to encompass *Vorkaufsrechte* and other preferential rights aimed at obtaining an object (used in this sense by Hueck "Erwerbsvorrechte" 755). In the publishing industry, preference contracts are mostly called *Optionsverträge* in the wide sense even though they are not constructed like an option or conditional option at all. See the authorities cited in n 70 *supra in fine*. Although Brandi-Dohrn *Der urheberrechtliche Optionsvertrag* 13 also uses the term "option contract in the wide sense", he does refer to the granting of a *Vorhand* in its definition. The term *Vorerwerbsrecht* is used as a synonym for *Vorhand* (and distinguished from the *Vorkaufsrecht*) in Heidenhain & Meister (eds) *Münchener Vertragshandbuch Band I: Gesellschaftsrecht* 5<sup>th</sup> edition (2000) 876, § V.112.

<sup>75</sup> Some authors incorrectly define *Vorhand* exclusively in respect of sales contracts, for example Nipperdey "Vorhand, Vorkaufsrecht und Einlösungsrecht" 1930 *Zentralblatt für Handelsrecht* 300.

offer to the holder upon the occurrence of the trigger event, mostly formulated as the grantor's wish to contract.<sup>76</sup> (This form of *Vorhand* will hereinafter be referred to as an *Angebotsvorhand*.)<sup>77</sup> This could for example be formulated as a duty to inform the holder of any third party offer to allow the holder to decide whether he wants to contract on the same terms.<sup>78</sup> Alternatively, the grantor has no duty to offer, but instead has a duty to inform the holder of his intention to contract and then to accept the holder's offer if that is the highest offer available (hereinafter *Annahmeverhand*).<sup>79</sup> Alternatively, the holder could merely be entitled to a *non facere*. In terms of this construction the grantor has no duty to offer or to accept the holder's offer on the occurrence of a stipulated event, but must refrain from contracting with a third party if he had not first offered to contract with the holder.<sup>80</sup> The weakest form of *Vorhand* is the so-called *Verhandlungsvorhand*, which only obliges the grantor to give the holder the chance to negotiate with the grantor before contracting with a third party.<sup>81</sup> These four types are the main constructions found in the case law.

A number of commentators do not discuss all these forms of preference contract. Many only speak of one form.<sup>82</sup> A number discuss only two forms, the *Verhandlungsvorhand*

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<sup>76</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 300; Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 300; Röser *Ankaufsrecht* 19.

<sup>77</sup> *Angebotsvorhand* literally means "offer preference (*Vorhand*)". As an example of the use of this terminology see Wagner 2000 *NotBZ* 69 77; "Vorhand: Verhandlungsvorhand; Angebotsvorhand; Beurkundungsbedürftigkeit" 1999 *DNotl-Report* 25-26

<sup>78</sup> Hueck "Erwerbsvorrechte" 752.

<sup>79</sup> Röser *Ankaufsrecht* 19; Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 303; Delp *Der Verlagsvertrag* 6<sup>th</sup> edition (1994) 64. *Annahmeverhand* literally means "acceptance preference (*Vorhand*)". This term is not known to the case law and literature but has been created by analogy to the known term of *Angebotsvorhand* to distinguish it from the latter institution.

<sup>80</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 304.

<sup>81</sup> See for example 1993 *Betriebsberater* 2222. (decision of the *Bundesfinanzgericht* of 18.10.1993); Allerkamp 1981 *Mitteilungen der Rheinischen Notarkammer* 55 62; Wagner 2000 *NotBZ* 69 77; "Vorhand: Verhandlungsvorhand; Angebotsvorhand; Beurkundungsbedürftigkeit" 1999 *D Notl-Report* 25-26.

<sup>82</sup> *Palandt* § 504 RdNr 11 (now § 463). Larenz *Lehrbuch des Schuldrechts* § 44 IV p 157; Larenz 1955 *Der Betrieb* 209 210; Hertel "Rechtsgeschäfte im Vorfeld eines Projektes" 1983 *Betriebs-Berater* 1824 1825.

and the *Angebotsvorhand*.<sup>83</sup> Some mention the *Annahmeverhand* as well.<sup>84</sup> Many do not mention the construction in terms of which the holder is merely entitled to a *non facere*.<sup>85</sup> However, many do, especially in works on publishing and copyright law.<sup>86</sup>

All these constructions differ from the *Vorkaufsrecht* in that a completed contract concluded with a third party is not necessarily required for the holder's claim to arise.<sup>87</sup> In fact, conclusion of a third party contract without granting the holder the chance to contract or at least to negotiate with the grantor beforehand is a breach of the *Vorhand*, whereas it would be perfectly legitimate in the case of a *Vorkaufsrecht*.<sup>88</sup> Neither does breach of the *Vorhand* entitle the holder to create a contract extra-judicially by unilateral declaration.<sup>89</sup> No contract between the grantor and holder exists in the absence of an offer and acceptance to each other,<sup>90</sup> although in some types of *Vorhand* courts are

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Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 300 specifically denies that the *Vorhand* can also be an obligation to inform the holder of the intention to alienate and to invite him to negotiations. He recognises only the *Angebotsvorhand* construction.

<sup>83</sup> Wagner 2000 *NotBZ* 69 77; "Vorhand: Verhandlungsvorhand; Angebotsvorhand; Beurkundungsbedürftigkeit" 1999 *D Notl-Report* 25-26; Soergel & Siebert (Huber) Vor § 504 RdNr 14 & 15 (now § 463); Staudinger (Mader) Vorbem zu §§ 504ff RdNr 40 (now § 463). *Münchener Kommentar* (Westermann) § 504 RdNr 4 (now § 463) regards the *Verhandlungsvorhand* as the default construction and recognises that parties could intend an *Angebotsvorhand* as well. Allerkamp 1981 *Mitteilungen der Rheinischen Notarkammer* 55 62 mentions these two possibilities plus the fact that a *Vorhand* sometimes refer to an option. However, he refers to no example of the latter case, nor any other authority.

<sup>84</sup> Röser *Ankaufsrecht* 19; Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 303.

<sup>85</sup> Röser *Ankaufsrecht* 18 *et seq* who defines the *Vorhand* as the right to the creation of an obligation conditional upon the intention of the grantor to create a similar obligation with a third party. See also the authorities in notes 81 - 83.

<sup>86</sup> For example Bappert & Wagner *Rechtsfragen des Buchhandels* 156 par 20.5; Brandi-Dohrn *Der urheberrechtliche Optionsvertrag* 1; Schack *Urheber- und Urhebervertragsrecht* 2<sup>nd</sup> edition (2001) 434 par 973. Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* recognises all four types.

<sup>87</sup> Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 300; Larenz *Lehrbuch des Schuldrechts* § 44IV p 157.

<sup>88</sup> *Ibid.*

<sup>89</sup> Hueck "Erwerbsvorrechte" 765; Erman (Grunewald) § 504 RdNr 5 (now § 463).

<sup>90</sup> Hueck "Erwerbsvorrechte" 765.

willing to order the grantor to make an offer or to accept the holder's offer if that is the highest offer available.

As the *Vorhand* is not mentioned in the *BGB*, it is not surprising that the *Vorkaufsrecht* is by far the more familiar institution.<sup>91</sup> However, *Vorhand* agreements are still used in practice.<sup>92</sup> *Vorhand* clauses are found *inter alia* in publishing contracts, contracts dealing with sale or lease of land, as well as in company statutes and agreements between shareholders.<sup>93</sup> The question arises why parties would rather use language excluding the

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<sup>91</sup> No German student to whom I have spoken (including doctoral and *Habilitation* students who have written both state exams) knows about the existence of the *Vorhand*. Most student textbooks that provide an overview of the whole of German private law, such as Medicus *Grundwissen zum Bürgerlichen Recht* (2000) contain no reference thereto. As the *Vorhand* is not well known and discussed in depth in commentaries on the *BGB*, it is not too surprising that a notary like Allerkamp 1981 *Mitteilungen der Rheinischen Notarkammer* 55 62 recommends the use of a *Vorvertrag* or option rather than a *Vorhand*, due to the vagueness (*Unbestimmtheit*) surrounding the *Vorhand* (apart from the fact that he feels that it generally does not bind the grantor sufficiently). The numerous statutory *Vorkaufsrechte* are also constructed like the *BGB Vorkaufsrecht* which would likely influence lawyers and to an extent non-lawyers acquainted with these statutory rights to think of all preferential rights to transact along the lines of the *Vorkaufsrecht* construction. Cf Hahn 1994 *Mitteilungen der Rheinischen Notarkammer* 193 194.

<sup>92</sup> In respect of case law since 1990, see 1994 *GRUR* 53-57 (decision of the *Landesgericht* Düsseldorf of 26.06.1990); 1993 *Betriebs-Berater* 2367-2370 (decision of the *Oberverwaltungsgericht*, Nordrhein-Westfalen of 23.04.1993). Cf. EFG 1999, 619-621 (decision of the *Finanzgericht* Berlin of 04.02.1999); OLGR-Bremen, Hamburg, Schleswig 1997, 66-68 (decision of the *Oberlandesgericht* Schleswig of 18.10.1996); EFG 1991, 103 (decision of the *Finanzgericht*, Saarland 05.10.1990); 1997 *OLGR-München* 134 (decision of the *Oberlandesgericht* München of 04.12.1996); 1993 *Betriebs-Berater* 2222 (decision of the *Bundesfinanzhof* of 18.08.1993). In respect of articles and commentaries since 1990 see Weber 1990 *Juristische Schulung* 249; “Vorhand: Verhandlungsvorhand; Angebotsvorhand; Beurkundungsbedürftigkeit“ 1999 *D Notl-Report* 25-26; Westermann & Klingberg “Vorkaufsrechte im Gesellschaftsrecht” 552. All the major commentaries on the *BGB* contain a short paragraph on *Vorhand*. See for example *Erman* (Grunewald) § 504 RdNr 5 (now § 463); *Palandt* § 504 RdNr 11 (now § 463); *Münchener Kommentar* (Westermann) § 504 (now § 463).

<sup>93</sup> Hueck “Erwerbsvorrechte” 752; Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 335; Röser *Ankaufsrecht* 19. They are found mostly in *GmbH* statutes (*Gesellschaft mit beschränkter Haftung* – company with limited liability) (Hueck “Erwerbsvorrechte” 752), but also in *KG* statutes (*Kommanditgesellschaft*) (Hueck “Erwerbsvorrechte” 753). Often preferential rights to buy shares are

*BGB Vorkaufsrecht* and so create a *Vorhand* contract? This could simply be due to ignorance of the limited field of application of the *Vorkaufsrecht*, coupled with the fact that it is naturally expected by most non-lawyers that the holder of a preferential right to transact must have the chance of contracting *before* a sale to a third party.<sup>94</sup>

However, it has been argued that there are also substantive reasons why parties would sometimes knowingly prefer to oblige the grantor to offer to contract with the holder before contracting with a third party instead of formulating their agreement in the *Vorkaufsrecht* mould. One reason to prefer the *Vorhand* construction is that the costs and effort of negotiating and drafting a valid contract between the grantor and third party becomes wasted if the holder of a *Vorkaufsrecht* does in fact exercise his right.<sup>95</sup> In the case of land, for example, a written and signed contract must be presented to the holder to force a decision on the exercise of the *Vorkaufsrecht*. As a rule, every buyer wants to be

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linked to a consent requirement. That is, a shareholder requires consent to transfer her shares, but the consent cannot be withheld if none of the holders are prepared to buy the shares at the price at which the grantor is able to sell to another (Hueck "Erwerbsvorrechte" 752-753).

<sup>94</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 18. Cf Röser *Ankaufsrecht* 13 and Schurig *Das Vorkaufsrecht* 56. The *Vorhand* construction has also been described as the one parties would most naturally intend in a decision reported in 1942 *Höchstrichterliche Rechtsprechung* 345 346. The court said it may be assumed that the parties intended that the holder would be given the preference (*Vorhand*) if the grantor decides to sell, without conclusion of a prior contract between the grantor and a third party. The *Vorhand* construction existed in German law before promulgation of the *BGB* (Schurig *Das Vorkaufsrecht* 59).

<sup>95</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 18; Hueck "Erwerbsvorrechte" 752. To solve the problem of costs, the contract with the third party could provide that the seller would initially pay the costs connected with the drafting of the contract (and valuation fees where applicable) but that the buyer must refund the seller in respect thereof on demand. In that case, the buyer would probably trust that the seller would only demand a refund upon the holder of the *Vorkaufsrecht* having failed to exercise his right, and the drafter would be happy to receive payment from the seller. The holder is of course bound to this obligation of the buyer on the exercise of his *Vorkaufsrecht*. Cf BGHZ 131, 348 where the court held that the holder who exercised his *Vorkaufsrecht* also incurs the obligation to pay the agent's fee, where the contract with the third party provided that such fee is payable by the buyer. Of course, this solution might still not please a grantor who does not want to incur any costs in connection with the sale.

assured of a binding waiver of another's preferential right to sale before concluding a contract with the owner.<sup>96</sup> It is of course possible for the holder to waive his *Vorkaufsrecht* before conclusion of a sale. However, the holder of a *Vorkaufsrecht* may refuse to do so before seeing the concluded contract, for example out of fear that the grantor would in the end contract with the third party on better terms than the offer submitted to the holder. Apart from the effort and costs of concluding a legally valid contract, the buyer who has concluded the contract must then wait for two months for the holder's decision, knowing that she might lose the opportunity to buy other suitable properties which might come up for sale in the meantime. Some buyers might be scared off by this prospect.<sup>97</sup> An owner who realises this in advance,<sup>97</sup> would perhaps rather want to formulate the preferential right in such a way that he could force the holder to decide whether to exercise her right before a sale with a third party is concluded. Then the holder need merely be informed of the material terms on which the owner is prepared to contract. In such a case, the *Vorhand* formulation would suit the grantor better.

Publishing contracts invariably contain a *Vorhand* rather than a *Vorkaufsrecht*.<sup>98</sup> This is because the publisher as holder of the preference wants to be the first to see the author's next work and wants to have the first opportunity to negotiate with the holder. Because

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<sup>96</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 18; Röser *Ankaufsrecht* 34; Schurig *Das Vorkaufsrecht* 56.

<sup>97</sup> See also Tew "Rights of First Refusal: The 'Options' That Are Not Options, But May Become Options" 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-17. The *Vorkaufsrecht* also creates a risk for the third party of offering more than is necessary to entice the *Vorkaufsrecht* holder not to exercise his right.

<sup>98</sup> See Bappert & Maunz (Schricker) *Verlagsrecht* § 1 RdNr 40; Schack *Urheber- und Urhebervtragsrecht* § 29 RdNr 973; Haberstumpf & Hintermeier *Verlagsrecht* 116 § 13; Delp *Der Verlagsvertrag* 64-66; Schmitt *Die Schaffensfreiheit der Künstler in Verträgen über künftige Geisteswerke* (1978) § 32 p 181; Reh binder *Urheberrecht: Ein Studienbuch* 10<sup>th</sup> edition (1998) § 47 RdNr 344; Bappert & Wagner *Rechtsfragen des Buchhandels* 154-155; Brandi-Dohrn *Der urheberrechtliche Optionsvertrag* 13. In the publishing industry, *Vorhand* agreements are rather referred to as options in the wide sense in order to distinguish them from options in the narrow sense. The latter refers to an actual option to conclude a publishing contract in respect of a future work. It could therefore be seen as an option conditional upon the creation of and decision to publish a new work.

publishing contracts require agreement on a number of material terms apart from the author's remuneration, for example the print-run (amount of copies to be published), it is economically inefficient to require a third party contract to be concluded before the holder's preferential right comes into being. No third party publisher would be prepared to negotiate all such details in the knowledge that another, the holder of the preferential right, could exercise a preferential right to publish the work.<sup>99</sup>

Interestingly, one sometimes finds both a *Vorhand* clause and a *Vorkaufsrecht* in a contract. The effect of such a combined formulation is that the *Vorhand* obliges the grantor to first offer to the holder before contracting with a third party. If the grantor fails to do so, the *Vorkaufsrecht* clause grants the holder the right to create a contract by unilateral declaration.<sup>100</sup>

In the absence of such a combined clause, the question remains what the primary rights and duties of the parties to *Vorhand* contracts are. As was pointed out above, German law recognises that the juristic construction of *Vorhand* contracts is not always the same. The exact construction depends on the concrete organisation of the contract by the parties and is therefore rather a matter of interpretation. As was mentioned, four main types of *Vorhand* agreements can be identified. In the order of the most restrictive to least restrictive on the grantor's freedom to deal with her property or other resources, they are:

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<sup>99</sup> The existence of a preemptive right may deter potential publishers from making offers because it reduces their expected return from the costs they incur in negotiating and making an offer.

<sup>100</sup> See for example, the contract considered by the Finanzgericht des Saarlandes on 05.10.1990. reported in 1990 *Steuerentscheidungen* 441. See also *Soergel & Siebert* (Huber) Vor § 504 RdNr 15 (now § 463); *Münchener Kommentar* (Westermann) § 504 RdNr 4 (now § 463). See clauses 16 and 17 of the suggested lease contract in Hoffmann-Becking and Schippel (eds) *Beck'sches Formularbuch zum Bürgerlichen, Handels- und Wirtschaftsrecht* 5<sup>th</sup> edition (1991) 181 § III.D.2 and clause 8 of the suggested pool contract in Heidenhain & Meister (eds) *Münchener Vertragshandbuch Band I: Gesellschaftsrecht* 5<sup>th</sup> edition (2000) 872-873 § V.112, discussed at 876.

1. The *Angebotsvorhand*, which entitles the holder to an offer by the grantor when the grantor wishes to conclude the main contract (for example, when the grantor wishes to sell). In other words it creates an enforceable conditional duty to make an offer.
2. The *Annahmeverhand*, which entitles the holder to acceptance of his offer by the grantor when the grantor wishes to conclude the main contract. In other words it creates an enforceable conditional duty to accept the holder's offer if that is the highest offer available.
3. Preference contracts that only place a negative duty on the grantor not to contract with a third party as long as the holder is prepared to contract on the same terms as the third party.
4. Preference contracts that oblige the grantor to give the holder a chance to negotiate before finally contracting with a third party.

The discussion hereunder will focus on the basic rights, duties and remedies of the parties as well as the juristic construction of each type (that is the explanation of the legal nature of each type). The field of application of each type will also be considered. Finally, I will consider whether one type is regarded as the default type where the wording of the agreement is cryptic and vague enough to encompass more than one type.

#### *4 1 2 1 A duty to make an offer (Angebotsvorhand)*

This form of *Vorhand* applies where the contract shows an intention to place an enforceable duty on the grantor to offer to contract with the holder, when the grantor

wishes to contract at all.<sup>101</sup> It could therefore be described loosely as a conditional duty to make an offer, the condition being the grantor's wish to contract.

#### 4 1 2 1 1 The trigger event

In the majority of *Vorhand* clauses, the condition, or trigger event, is not precisely defined. A number of writers formulate the default trigger event as an expression of a desire to alienate. However, most say that in the case of a *Vorhand* to buy a mere expression of a desire to sell is not enough.<sup>102</sup> Something more is required, such as the commencement of serious negotiations with a third party.<sup>103</sup> That which precedes such negotiations, for example a valuation of the object by an expert or a general sounding out whether there would be any interested parties at all, should not be a trigger event. Larenz attempts to narrow down the trigger event by stating that the expression of desire to contract can appear either from a declaration to the holder or from an action which can be regarded as “the initiation of the accomplishment of the decision to alienate.”<sup>104</sup> Henrich suggests that one must ask whether an independent person would interpret the grantor's actions as showing a willingness, here and now, to contract with a specific person. If so, the grantor cannot say that he did not want to bind himself.<sup>105</sup> Although this is probably the most precise definition to be found in the literature, it is still bound to lead to disputes, as will the attempt to distinguish between “serious negotiations” and “non-serious negotiations.”

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<sup>101</sup> RGZ (1886) 16, 155, 158; Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 300-301; Wagner 2000 *NotBZ* 69 77.

<sup>102</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 339; Larenz 1955 *Der Betrieb* 209 210; Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 301; Larenz *Lehrbuch des Schuldrechts* 157 § 44 IV.

<sup>103</sup> *Ibid.*

<sup>104</sup> In the words of Larenz 1955 *Der Betrieb* 209 210 (my translation). See also Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 301.

<sup>105</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 340.

In German law, the grantor cannot wipe out the trigger event by declaring that she has now decided not to contract at all.<sup>106</sup>

#### 4 1 2 1 2 Duties of grantor at trigger event

If the grantor manifests the necessary intention, a duty to make an offer arises. What must be in the offer? At least the material terms on which the grantor is prepared to contract. It has been argued that the grantor should also be forced to inform the holder of the name of the interested third party.<sup>107</sup> The most important reason is that it protects the holder who has an interest in warding off unwanted third parties.<sup>108</sup> At what price must the grantor offer to contract with the holder, if this was not agreed in the preference contract? Some writers say that the offer must be reasonable.<sup>109</sup>

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<sup>106</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 340.

<sup>107</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 349; decision of the *Reichsgericht* reported in 1930 *Juristische Wochenschrift* 3766.

<sup>108</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 349. This is termed an *Abwehrinteresse* by German writers as opposed to an *Erwerbsinteresse*, an interest in obtaining the object of the right. The holder's primary interest could be to ward off unwanted third parties (as is often the case in shareholder preference contracts, franchise agreements and contracts between neighbours and relatives). Another argument is that "preference" is said to mean priority under equal terms. A realisation of such priority is only possible when the holder knows that he has competition who is offering the same terms as the grantor. Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 349-350; decision of the *Reichsgericht* reported in 1930 *Juristische Wochenschrift* 3766. An analysis of certain consequences of preference contracts according to whether the holder's interest is an *Abwehr-* or *Erwerbsinteresse* has been suggested by Burkert "Die Reichweite des § 506 BGB" 1987 *NJW* 3157.

<sup>109</sup> Larenz *Lehrbuch des Schuldrechts* 157 § 44 IV; *Erman* (Grunewald) § 504 (now § 463) states that it depends upon the interpretation of each agreement whether this is required. Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 348 at n 348 states that § 315 *BGB* requires the grantor to make a fair offer.

Where the preference contract provides that the holder may take over the highest offer made by a third party, the grantor also has an enforceable duty to inform the holder of the offers received from third parties.<sup>110</sup>

#### 4 1 2 1 3 Exercise of the right by the holder

The questions which arise here are:

1. must the holder's declaration that he exercises the preference right comply with formalities legislation set for the main contract,
2. within what time period must the holder make the declaration, and
3. must the holder prove a willingness and ability to perform all the terms of the contract?

If the grantor indeed offers to contract with the holder, the normal rules for acceptance applies.<sup>111</sup> Where the grantor is in breach of the obligation to make an offer, the holder need not make a formal declaration of intention to exercise the preferential right.<sup>112</sup> However, a failure to demand performance of the grantor's duty within a reasonable time may be taken as a waiver of the preferential right.<sup>113</sup>

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<sup>110</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 348, 355.

<sup>111</sup> The preference contract or grantor's offer may specify a time limit. (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 350 - 350). If not, the holder must exercise the right within a reasonable time. Röser *Ankaufsrecht* suggests an analogous application of § 469 *BGB* (previously § 510) relating to the *Vorkaufsrecht*, that is two months for land and one week for other objects. The formalities legislation must also be complied with (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 321, 347, 354; Hueck "Erwerbsvorrechte" 766; Larenz 1955 *Der Betrieb* 209; Röser *Ankaufsrecht* 53).

<sup>112</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 353.

<sup>113</sup> *Ibid.*

To validly exercise and enforce the right, the holder must show that she is willing and able to perform all the terms offered by the grantor or agreed with the third party,<sup>114</sup> except a term included by *mala fide* collusion to avoid the preferential right.<sup>115</sup> An inference of such *mala fide* collusion can only be made where the grantor has no personal or economic interest in the inclusion of such a term.<sup>116</sup>

#### 4 1 2 1 4 Remedies for breach

What remedies are available on breach of the grantor's duty to make an offer on fulfilment of the condition?

Firstly, the holder may pray for an interdict upon the threatened sale to a third party.<sup>117</sup>

Per definition, the *Angebotsvorhand* creates an enforceable duty to make an offer. The holder can therefore claim an order that an offer be made.<sup>118</sup> This is an effective prayer due to § 894 *Zivilprozessordnung* which creates a fiction that a declaration of will prayed for is regarded as made upon the judgment granting the prayer. For this reason, the holder may in the same action claim an order that an offer be made, and an order that the grantor perform the main contract. The contract comes into existence on the first prayer

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<sup>114</sup> Hueck "Erwerbsvorrechte" 367.

<sup>115</sup> 1988 *Wertpapier Mitteilungen* 92 (decision of the *Bundesgerichtshof* of 25.11.1987).

<sup>116</sup> *Ibid.*

<sup>117</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 355.

<sup>118</sup> Larenz *Lehrbuch des Schuldrechts* § 44 IV. Cf Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 356. Floyd "Die Voorkoopreg" 1986 *THRHR* 253 269 n 164 wrongly states that an order to make an offer is not known to German law. He relies on Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 356 n 60 who does state that Italian writers generally do not recognise such an order. However, in the same footnote Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* also cites some German authorities in favour of his statement in the text that the holder can claim either the making or acceptance of an offer.

and the holder's confirmation that she accepts that offer.<sup>119</sup> The duty to make an offer does not become impossible to perform after the grantor has contracted with a third party. Although the intention is that the grantor must make an offer *before* contracting with a third party, the offer can still be made thereafter.<sup>120</sup> Of course, where the grantor has transferred the object of an *Angebotsvorhand* to a *bona fide* third party, a claim for specific performance makes no sense as performance of the main contract has become impossible.<sup>121</sup> In the case of an *Angebotsvorhand* to sell, performance of this contract and the main contract does not become impossible where the grantor has already bought from a third party in breach of the preference contract.<sup>122</sup> The grantor could therefore be ordered to conclude a further contract with the holder and once again take delivery of the goods.<sup>123</sup>

The holder may also claim for damages upon breach by the grantor.<sup>124</sup> The *quantum* would be assessed according to the holder's interest in obtaining performance of the main contract.<sup>125</sup> However, the holder may not claim damages if the grantor can show that the holder would not have exercised his right even if the grantor had made an offer to the holder timeously.<sup>126</sup>

#### 4 1 2 1 5 Extinction of preference

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<sup>119</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 356-357 and 186-187; *Staudinger* (Mader) Vorbem zu §145ff RdNr 67; *BGHZ* 98, 130 134; *BGH* 1986 *NJW* 2820 2821. *Contra* Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 301 who states that the holder need only pray for performance of the main contract.

<sup>120</sup> Cf Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 356.

<sup>121</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 365.

<sup>122</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 366.

<sup>123</sup> *Ibid.*

<sup>124</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 365 *et seq.*

<sup>125</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 367.

<sup>126</sup> *Ibid.*

If a proper offer is made and the holder rejects it or fails to accept it within the time stated in the offer, or within a reasonable time, the grantor is free to contract with a third party on those terms. Some writers argue persuasively that the *Vorhand* should not terminate through mere non-exercise thereof, but only once the grantor actually contracts with a third party at the terms offered to the holder.<sup>127</sup> The purpose of this rule is to prevent the grantor from ridding himself of his duty through a fake offer which he knows the holder would not accept, and thereafter selling to a third party at terms more beneficial to the holder. It would be difficult to prove such collusion between the grantor and a friend.<sup>128</sup>

The normal rules on termination of obligations apply to the *Vorhand*, so that it also terminates by, for example, waiver.<sup>129</sup>

#### 4 1 2 1 6 Legal nature

Many authors regard the *Angebotsvorhand* as a conditional *Vorvertrag*, that is a contract which obliges one or both of the parties to enter into another (the main) contract.<sup>130</sup> More

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<sup>127</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 363. Cf also Haberstumpf & Hintermeier *Verlagsrecht* 117 § 13; Brandi-Dohrn *Der urheberrechtliche Optionsvertrag* 62 et seq; Bappert & Maunz (Schrickler) *Verlagsrecht* § 01 RdNr 43 who argue that the holder's failure to buy from the grantor at the terms offered only terminates the right if he intimates an intention not to exercise the right at all, regardless of the terms offered. If the refusal was instead motivated by the specific terms offered, the grantor who has not in fact sold after the first offer, must offer again before she may contract with a third party on better terms.

<sup>128</sup> *Ibid.*

<sup>129</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 363 et seq.

<sup>130</sup> Larenz 1955 *Der Betrieb* 209 210; Allerkamp 1981 *Mitteilungen der Rheinischen Notarkammer* 55 62f; Michalski 1999 *Zeitschrift für Miet- und Raumrecht* 141 147; Wagner 2000 *NotBZ* 69 77. On *Vorverträge*, see generally Weber 1990 *Juristische Schulung* 249 252. Lorenz "Vorzugsrechte" grudgingly accepts the description of a *Vorhand* as a unilateral *Vorvertrag* as correct but not very helpful (105, 112). Cf BGH EWiR 565-566 which distinguishes the *Vorvertrag* from the *Vorrechtsvertrag* on the basis that the latter obliges the grantor to offer the object for sale if he should decide to sell, whereas a *Vorvertrag* obliges one or both parties to conclude another contract. According to Henrich *Vorvertrag, Optionsvertrag,*

specifically, it is a (potestatively) conditional, unilaterally binding *Vorvertrag*.<sup>131</sup> Most writers accept that as a *Vorvertrag*, the preference contract should also comply with the formalities set for the main contract.<sup>132</sup> However others advocate that the applicability of formalities legislation should depend on the purpose of each piece of legislation involved, although it is accepted that in respect of land the formalities legislation should apply.<sup>133</sup>

#### 4 1 2 2 *A duty to accept the holder's offer (Annahmeverhand)*

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*Vorrechtsvertrag*, the legal nature of preference contracts structured like the *Vorhand* is controversial in most jurisdictions. Preference contracts have been regarded as *Vorverträge* by some Italian and Swiss commentators (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 57, 68; Lorenz “Vorzugsrechte” 115), although they are there also often regarded as contracts *sui generis* (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 58). Lorenz “Vorzugsrechte” maintains that the theory of *Vorverträge* plays no role in Swiss law (115; cf Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht nach dem schweizerischen Zivilgesetzbuche* (1918) 27). Their legal nature in France is also disputed (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 37-38). The view that it is a conditional unilateral promise to contract, similar to a conditional option, is widely held but criticised on the basis that the will to contract is an essential element of a promise to contract and therefore cannot be a condition (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 37). Therefore they are often held to be contracts *sui generis* (Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 37). French law does not recognise the *Vorvertrag* concept in the sense in which this term is used in Germany (Lorenz “Vorzugsrechte” 121, Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 22 *et seq.*). The *Vorverträge* of German law include what South African law would call *pacta de contrahendo* as well as bilaterally binding agreements to agree, provided the latter are sufficiently certain to enforce them. On *Vorverträge* generally, see Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 1 *et seq.*

<sup>131</sup> Lorenz 1955 *Der Betrieb* 209 210; Allerkamp 1981 *Mitteilungen der Rheinischen Notarkammer* 55 62 *et seq.*; Michalski 1999 *Zeitschrift für Miet- und Raumrecht* 141 147; Wagner 2000 *NotBZ* 69 77; Lorenz “Vorzugsrechte” 105.

<sup>132</sup> See the authorities cited by Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 321; Röser *Ankaufsrecht* 39; Wolf 1995 *DNotZ* 179 193; Soergel & Siebert (Huber) Vor § 505 RdNr 14 (now § 464); Allerkamp 1981 *Mitteilungen der Rheinischen Notarkammer* 55 62; “Vorhand: Verhandlungsvorhand, Angebotsvorhand; Beurkundungsbedürftigkeit” 1999 *DNotl-Report* 25-26.

<sup>133</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 322.

A preference contract could also oblige the grantor to notify the holder of the intention to sell or, in addition, of the terms on which the grantor is prepared to contract with a third party and to accept the holder's offer if that is the best offer available when the holder makes the offer.<sup>134</sup>

The following clause is an example of a preference agreement that has been construed as an *Annahmeverhand* by a German court:

If the lessor terminates the contract by notice, and a third party offers a higher rent than the rent agreed in this contract, the lessee will have a preference to lease (*Mietsvorrecht*) in respect of this new offer, which right the lessee must exercise within 10 days of receipt of notice of the better offer.<sup>135</sup>

The court held that the contract only gives the lessee the right to be informed of a better offer. The grantor is not obliged to make an offer to the lessee on the same terms. If the lessee does make a similar or better offer than the third party the grantor has a duty to accept the lessee's offer.

This type of *Vorhand* obviously benefits the grantor in that the notice to the holder does not bind the grantor. If the owner receives a higher offer from a third party after such notice to the holder, the grantor may answer the holder's offer on the same terms with a notice of the higher offer. As the holder's offer is not the best offer available, the owner is not obliged to accept it.<sup>136</sup> The grantor's freedom to contract is thus not impaired to the same extent as under an *Angebotsvorhand*. The grantor's interest in obtaining the best possible terms when dealing with her property is served better by the *Annahmeverhand* than by the *Angebotsvorhand*.

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<sup>134</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 303. See Delp *Der Verlagsvertrag* 64 for a drafting suggestion for such a contract.

<sup>135</sup> OLG 17, 26 (my translation).

<sup>136</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 304.

In German law it is generally accepted that the *Annahmeverhand* is a potestatively conditional unilaterally binding *Vorvertrag*, as it creates a duty for the grantor to enter into a future contract.<sup>137</sup> The condition is the grantor's wish to contract and the fact that the holder's offer is the best available offer when made.

Apart from the main construction of the *Annahmeverhand* the rules relating to the *Angebotsvorhand* discussed in the previous section, apply *mutatis mutandis* to the *Annahmeverhand* as well.<sup>138</sup>

4 1 2 3 A duty not to contract with a third party if the holder is prepared to contract on the same terms (“bare preference *Vorhand*”)

This form of *Vorhand* only imposes an *obligatio non faciendi* on the grantor. The grantor may not contract with a third party unless the holder has first been given a chance to contract and has failed to accept this opportunity.<sup>139</sup> It could accordingly be described as a *pactum de non contrahendo cum tertii*.<sup>140</sup> The grantor is neither obliged to make an offer to nor to accept an offer by the holder under any circumstances. It can be described as a mere duty to prefer the holder above third parties, without a duty to contract with the holder being added to that preference. A “preference” implies a negative: the non-selection of others, but does not necessarily intimate when and how a selection must take place. Accordingly, this form of *Vorhand* grants the holder merely a preference without adding a duty to contract.<sup>141</sup> As such it can be described as a “bare preference *Vorhand*”

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<sup>137</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 304.

<sup>138</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 303, 309 *et seq.*

<sup>139</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 304 *et seq.*

<sup>140</sup> See Michalski 1999 *Zeitschrift für Miet- und Raumrecht* 141 144 at n 89 and 143 n 30.

<sup>141</sup> BGH 22, 347 (decision of 14.12.1956); Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 304-305. Most writers on publishing law understand the *Vorhand* (generally known as *Optionsvertrag*, but sometimes referred to as a *Vorrechtsvertrag*) as such. See for example Ulmer *Urheber- und Verlagsrecht* 3rd edition (1980) 397 § 94; Reh binder *Urheberrecht* 270 par 344. Some realize that this is the default construction, whereas parties can agree on a different construction (eg Brandi-Dohrn *Der urheberrechtliche*

in order to distinguish it from the other forms. Upon breach of the preference, the holder is not entitled to the conclusion of a contract, but only to damages and an interdict prohibiting conclusion of a contract with a third party unless the holder has first been granted an opportunity to contract (*Unterlassungsanspruch*).<sup>142</sup>

Accordingly this type of preference contract has two distinct characteristics. Firstly, nothing short of contracting with a third party amounts to breach by the grantor. Secondly, the holder cannot enforce transfer of the object of the preferential right.

This type of preference agreement is used extensively in publishing contracts. The default construction of preference agreements in publishing contracts is that the author as grantor is not obliged to make an offer to the publisher as holder upon the author's decision that

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*Optionsvertrag* 13). For the (unmotivated and shortly stated) view that the *BGB* provisions on the *Vorkaufsrecht* should apply to the *Optionsvertrag* generally found in publishing contracts, see Bappert & Maunz *Verlagsrecht: Kommentar zum Gesetz über das Verlagsrecht vom 19.6.1901* (1952).

<sup>142</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 350. There is some authority on publishing contracts to the effect that the holder may claim either damages or *Naturalrestitution* (restitution) against the third party, that is, that the contract with a third party be set aside. Some writers state that the publisher as holder can then also require conclusion of such a contract, but that this remedy is meaningless as normally the third party would have obtained the intellectual property rights to the artistic work by that stage. See Bappert & Maunz *Verlagsrecht* (1952) § 1 RdNr 45 with reference to BGH NJW 1962, 1197; RGZ 108, 58. Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* does not mention an interdict prohibiting the performance of a contract already concluded, presumably because the maxim *prior est tempore, potior est iure* does not apply to competing personal rights under German law. § 879 *BGB* makes this principle applicable to *real* rights on the basis of the maxim that no-one can transfer more than he himself possesses. See Baur & Stürner *Sachenrecht* 17<sup>th</sup> edition (1999) § 17 B II; Quack (ed) *Münchener Kommentar zum Bürgerlichen Gesetzbuch 6 Sachenrecht (§§ 854-1296), WEG, ErbbauVO, SachenRBeG, SchuldRÄndG* 3<sup>rd</sup> edition (1997) § 879 RdNr 12; Kruger (ed) *Münchener Kommentar zum Bürgerlichen Gesetzbuch 2 Schuldrecht Allgemeiner Teil (§§ 241-432)* 4<sup>th</sup> edition (2001) 13-14 (Einleitung RdNr 19); *Palandt* § 879. In South Africa, by contrast, courts apply the maxim, *prior est tempore, potior est iure* to personal rights unless it is inequitable in the circumstances. See for example, *Krauze v Van Wyk* 1986 1 SA 158 (A); *Wahloo Sand BK en Andere v Trustees, Hambly Parker Trust en Andere* 2002 2 SA 776 (HHA).

the work is ready for publication.<sup>143</sup> Neither is the author obliged to accept any offer from the publisher. However, a publisher who holds a *Vorhand* may sue for the submission of the author's work and for information on any third party offers.<sup>144</sup> Any offer made by the publisher in response need not be accepted by the author.

The formalities requirements and the rules relating to the price at which the holder may contract are irrelevant to this type of contract. There is also no question of a trigger event which allows the holder to exercise her right. If the grantor in fact contracts with a third party, it is rather a matter of breach.

#### *4 1 2 4 A duty to negotiate with the holder before contracting with a third party (Verhandlungsvorhand)*

A grantor of a preferential right may sometimes only grant the holder the right to negotiate before a contract is concluded with a third party. This could include the right to “have the last word” before the seller makes his decision in order to allow the holder to make or increase an offer. Normally the expression *das letzte Wort geben* (to give the last word) would be interpreted in this way, that is, the grantor is free to sell to whomever she pleases at whatever terms she pleases as long as the holder had the last opportunity to negotiate.<sup>145</sup> Such a *Vorhand* is termed a *Verhandlungsvorhand* (“negotiation *Vorhand*”) by some commentators.<sup>146</sup>

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<sup>143</sup> Bappert & Wagner *Rechtsfragen des Buchhandels* 157; Ulmer *Urheber- und Verlagsrecht* 3<sup>rd</sup> edition (1980) 397 § 94.

<sup>144</sup> Bappert & Maunz (Schrickler) *Verlagsrecht* § 1 RdNr 44. See also Bappert & Wagner *Rechtsfragen des Buchhandels* 157.

<sup>145</sup> RG HRR 933, 913.

<sup>146</sup> “Vorhand: Verhandlungsvorhand; Angebotsvorhand; Beurkundungsbedürftigkeit“ 1999 *D Notl-Report* 25-26; Wagner 2000 *NotBZ* 69 77; *Soergel & Siebert* (Huber) Vor § 504 RdNr 14 (now § 463); *Staudinger* (Mader) Vorbem zu §§ 504ff RdNr 40 (now § 463); *Münchener Kommentar* (Westermann) § 504 RdNr 4 (now § 463); Wolf 1995 *DNotZ* 179 192.

This is the weakest form of *Vorhand* and obviously does not have much commercial value for the holder, as the holder's only remedy is an interdict (*Unterlassungsanspruch*), which would very likely sway the grantor not to contract with the holder in any event.<sup>147</sup>

#### 4 1 2 5 Which type of *Vorhand* is the default construction in German law?

As was pointed out above, many writers discuss only the *Angebotsvorhand* and do not even mention the *Vorhand* that places a mere *obligatio non faciendi* on the grantor. However, Henrich (whose book remains the most comprehensive study of *Vorhand* contracts) argues cogently that the bare preference contract should be regarded as the normal or default construction where the *BGB Vorkaufsrecht* is excluded by the wording of the contract, in cases where the preference contract contains no mechanism for determination of the price upon exercise of the preferential right. In this he is supported by a decision of the *Bundesgerichtshof*, the highest German court, in a decision given in 1956.<sup>148</sup> In that case a clause in a publishing contract that “the author would first offer new manuscripts to the publisher” was construed as merely placing a duty on the author to *first* offer to contract with the publisher before contracting with anyone else. The court decided that the grantor also complies with this duty if he does not immediately name the terms on which he is prepared to contract, but waits upon the offer of the publisher as holder. If the author is unhappy with the terms offered by the publisher, he is not forced to conclude a publishing contract. He may however only offer that work to another publisher if the latter offers him better terms than the offer made by the holder. The mere fact that the author shows a desire to sell his work for publishing, does not, therefore,

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<sup>147</sup> As the *Verhandlungsvorhand* only entitles the holder to negotiate, it need not comply with formalities legislation. See the authorities in the previous footnote.

<sup>148</sup> BGH 22, 347. Various writers on publishing also favour this construction as the default construction in cases where the “option clause” does not predetermine the terms of the eventual publishing contract. See for example Brandi-Dohrn *Der urheberrechtliche Optionsvertrag* 13; Bappert & Wagner *Rechtsfragen des Buchhandels* 157 par 20.6 *et seq*; Schack *Urheber- und Urhebervertragsrecht* (2001) 434 par 973.

entitle the holder to an offer that it should publish the work nor to acceptance of the publisher's offer if that is the best offer available.

The main argument for regarding this type of preference contract as the default type is that the parties are more likely to intend such a construction as it has important advantages as against the other two types.<sup>149</sup>

The main advantage of this type of contract is that the grantor is left freer. He need not fear that any negotiation with an interested party might be interpreted as a trigger event so that he could thereupon be forced into a contract with the holder. The grantor can calmly sound out the market and obtain the best offer.<sup>150</sup> A preference contract is a compromise between being absolutely bound to sell and the freedom not to do so.<sup>151</sup> Therefore it is in the interest of the grantor to construct the preference contract as loosely as possible, and this is what he would most likely agree to.<sup>152</sup> Therefore the grantor would generally rather intend to conclude this type of contract than the *Angebots-* or *Annahmeverhand*.<sup>153</sup> The holder of a preferential right to buy realises full well that she may never get the opportunity of obtaining the object of the right. One could therefore expect that the holder should be satisfied with an agreement in terms of which the grantor would remain

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<sup>149</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 305. In the case of a testamentary preferential right, the argument as to the intention of the future owner remains relevant as she must agree to accept the disposition (adiate) subject to the preferential right before the property will be transferred to her.

<sup>150</sup> Cf Westermann & Klingberg "Vorkaufsrechte im Gesellschaftsrecht" 556.

<sup>151</sup> Cf Schurig *Das Vorkaufsrecht* 37.

<sup>152</sup> Cf also Röser *Ankaufsrecht* 52, albeit in a different context. If the holder required more of the grantor the holder had the possibility of agreeing with the grantor on an option. See BGH 25.11.1987 1988 *Wertpapier Mitteilungen* 92-95 where the court construed a *Vormietsrecht* (that is, constructed like a *Vorkaufsrecht*) to place as little a burden as possible on the grantor's freedom to deal with his property, *in casu*, to agree any terms in which it has a personal or economic interest with the third party, even if this means that the holder cannot exercise the *Vormietsrecht*. The court suggested that if the parties had wanted to secure the holder's right to conclude the main contract, they would have agreed on an option contract (95).

<sup>153</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 305.

owner of the object, as long as it is not sold to a third party. A balancing of interests requires that nobody be given more than his interest demands.<sup>154</sup> Arguably the holder's interest, even if it is primarily aimed at obtaining the object, is served sufficiently well by the bare preference *Vorhand*. That the grantor of a right of pre-emption is not necessarily obliged to enable "exercise of the right" in the sense of obtaining the property, appears from the fact that the grantor may alter, damage or destroy the object as she pleases as long as it has not been sold to a third party, and may also freely agree to donate or exchange the object.<sup>155</sup>

Moreover, the *Angebotsvorhand* has a number of disadvantages. The question whether the trigger event has occurred and the terms on which the offer should be made are likely to lead to protracted disputes.<sup>156</sup> The negative or bare preference *Vorhand* eliminates disputes on these issues. Henrich also points out that in countries like Italy and England which accept the revocability of an offer, the grantor who has made an offer to the holder

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<sup>154</sup> Schurig *Das Vorkaufsrecht* 77.

<sup>155</sup> See RGZ 101, 101; BGHZ 49, 8; BGH WM 57, 1164; *Erman* (Grunewald) § 504 RdNr 8 (now § 463); *Soergel & Siebert* (Huber) § 504 RdNr 5 (now § 463); *Münchener Kommentar* (Westermann) § 504 RdNr 18 (now § 463).

<sup>156</sup> See *supra* at n 33. The solution advanced by Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 is not very satisfying. To say that once the grantor wishes to sell, he should make an offer on the same terms as a third party offer to him, is not very satisfying. Why should a court order the grantor to make such an offer upon entering into serious negotiations with the third party if the grantor has not shown that this offer is acceptable to him, that is, before a contract had been concluded between the grantor and third party? Cf Röser *Ankaufsrecht* who only speaks of a duty to inform the holder of a third party offer if and when the grantor is willing to accept that offer (52). On his construction it would be rather difficult to enforce the grantor's "obligation to offer" to the holder, as the grantor would always be able to say that the third party offer is not acceptable. Although Röser describes the *Vorhand* as a conditional duty to make an offer, his construction is in effect closer to Henrich *Vorvertrag*, *Optionsvertrag*, *Vorrechtsvertrag*'s construction of the default type. If no offer was made, Nipperdey 1930 *Zeitblatt für Handelsrecht* 300 proposes that the parties should possibly be held to have intended that the offer must be made at the market price, especially in the case of *Wertpapiere* and shares. This recommendation could be followed, but has a small field of application. Nipperdey's fall back solution is § 315 *BGB*, according to which the grantor is free to set a price according to a fair assessment (300). Of course, this also leads to uncertainty.

is allowed to revoke the offer upon proof that she no longer wishes to sell at all,<sup>157</sup> which is also the accepted view in South Africa.<sup>158</sup> This widely held view that a grantor who no longer wishes to sell at all should not be forced to do so, is another reason to treat the “negative *Vorhand*” as the normal type of preference contract in German law, as the *Angebots-* or *Annahmeverhand* would force the grantor to make an offer or acceptance which would be irrevocable under German law.<sup>159</sup>

A prevalent justification in favour of the *Angebotsvorhand* construction as the normal construction is that the obligation created by the preference contract is a relationship of trust and that according to *Treu und Glauben* the grantor is bound to enable the holder to exercise his right. This begs the question that the holder has a right to contract and not just a right to be preferred above others. Moreover, if there was a duty to enable the holder to eventually acquire the thing, this could arguably be used to argue that the grantor should be liable for damages if the object should perish due to his fault before occurrence of the trigger event.<sup>160</sup> However, the parties clearly do not intend to place such a burden on the grantor.<sup>161</sup> The grantor should be free to deal with his property as he pleases within the law. Only his capacity to freely alienate the object is limited by the preference contract.

Henrich therefore dismisses the view that the parties normally intend that the grantor could be forced to make an offer to the holder before contracting with a third party as not properly heeding the true intention of the parties.<sup>162</sup> He regards the root of the error as doctrinal lines of reasoning which take the well-known institutions of *Vorvertrag* and

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<sup>157</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 348.

<sup>158</sup> *Wissekerke v Wissekerke* 1970 2 SA 550 (A).

<sup>159</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 340. This results from the principle that an offer to contract is irrevocable for the period in which it may be accepted (Allerkamp 1981 *Mitteilungen der Rheinischen Notarkammer* 55 56.)

<sup>160</sup> As Röser *Ankaufsrecht* argues at 70.

<sup>161</sup> Cf however Du Plessis *Spesifieke Nakoming* 44 who states that, according to French law, the grantor of a *pacte de préférence* is not allowed to deal with the object in such a manner as to affect the holder’s rights.

<sup>162</sup> *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 306.

*Vorkaufsrecht* as its point of departure without considering the true intention of the parties.<sup>163</sup> As was pointed out before, the majority of German writers who mention *Vorhand* do not even mention this bare preference or *obligatio non contrahendo cum tertii* construction. Therefore they do not counter Henrich's policy arguments that the latter should be the normal default construction.<sup>164</sup> Perhaps this omission is due to Henrich's work being the only in depth study of *Vorhand* contracts that is not focused solely on publishing law,<sup>165</sup> as well as to the absence of references to works on publishing law in the general commentaries and articles on *Vorhand* contracts.

According to Henrich, the *Angebotsvorhand* must be the default construction in two situations. Firstly, where the parties have fixed the terms of the future contract or provided for a mechanism for its determination<sup>166</sup> in the preference contract, and, secondly, in the case of a preferential right to sell.<sup>167</sup>

In the first instance, the grantor has no interest to sound out the market for a better offer. Therefore, the parties are likely to have intended that the holder may obtain the object on the occurrence of the trigger event. Accordingly the grantor should have an enforceable

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<sup>163</sup> *Ibid* 306.

<sup>164</sup> All the major commentaries on the *BGB* normally contain only a few paragraphs, if that, on *Vorhand* contracts, and concentrate largely on the discussion of *Vorkaufsrechte*, which are more widely used. Moreover, their discussion on *Vorhand* contracts do not mention the works on publishing law, perhaps because such agreements are known as "options in the wide sense" and not as *Vorhand* agreements in the publishing industry. The same applies to works on the law of obligations, such as Larenz *Lehrbuch des Schuldrechts* 14<sup>th</sup> edition (1987).

<sup>165</sup> Röser's work also studies the *Vorhand* contract in more depth than is usual.

<sup>166</sup> Cf *Soergel & Siebert* (Huber) Vor § 504 RdNr 15 (now § 463) who require an ascertainable price for the *Vorhand* (understood as an enforceable duty to make an offer) to apply. The price would be ascertainable if it is determined as the estimated value or the market value or where the determination is left to a third party or to one of the parties themselves. Where the price is left open, they construct it as a *Verhandlungsvorhand*. They do not mention the possibility of the bare preference *Vorhand* construction.

<sup>167</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 307.

duty to make an offer in such cases.<sup>168</sup> This accords with the widely espoused view that where the terms of the eventual publishing contract are predetermined in the preference contract to such a degree that the publisher (the holder) need only make a declaration to create the main contract, the preference contract can be regarded as an option contract in the narrow sense, that is, in the sense this term bears in South African law.<sup>169</sup> In other words, the publisher has a right to contract upon fulfilment of the condition, namely the author's decision to have his work published.<sup>170</sup>

In the case of a preferential right to sell, the grantor is not the owner of the object of the right. Accordingly, the argument that the grantor should be left as free as possible to deal with her property does not apply. The owner as preferential right holder is specifically interested in being granted the opportunity of selling to the grantor. This provides support for classifying that type of preference contract as an *Angebotsvorhand*.<sup>171</sup> It is submitted that there is more justification for treating this type of preferential right as an *Annahmeverhand*. The holder of the right would mostly be a trader with a usual price, so that it can be argued that by implication, the parties agree that the grantor would buy any supplies needed at the holder's usual price which can be easily determined, unless the grantor can show that there is a better price available from a third party supplier.

It should be noted that Henrich's policy arguments in favour of the "bare preference" *Vorhand* as the default construction centre on the first characteristic element of the "bare

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<sup>168</sup> Interestingly, Lorenz "Vorzugsrechte" 120 feels that only where the preference contract fixes the terms of the future contract may the holder's right be secured by an "endorsement" or *Vormerkung* in the land register. This implies that where the terms are not "fixed" by the preference contract, the holder has no right to obtain transfer of the land and is only entitled to a *non facere*.

<sup>169</sup> See for example, Bappert & Wagner *Rechtsfragen des Buchhandels* 157 par 20.6 *et seq*; Brandi-Dohrn *Der urheberrechtliche Optionsvertrag* 60-61.

<sup>170</sup> German writers on publishing law distinguishes this option contract in the narrow sense from the "option contract in a wide sense" as the "bare preference *Vorhand*" is called by these writers.

<sup>171</sup> The fact that the potential buyer as grantor also has an interest in being free to sound out the market for the best price, militates against Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag*'s argument that this situation creates an *Angebotsvorhand*. This matter will be considered further in chapter 7 *infra*.

preference” *Vorhand*, namely that nothing short of contracting with a third party amounts to breach by the grantor. He does not specifically address the policy arguments in favour of the second element, namely, that the holder does not ever have a remedy by which he can enforce transfer of the object of the preferential right. It appears that he regards this second element rather as a logical consequence of the first. The argument would be that as the grantor is never obliged to make or accept an offer he can never be forced to do so by a court. The grantor's *obligatio non faciendi* is, like all such obligations, enforceable only by an order that the grantor refrain from doing something. On the other hand, Henrich's opponents accept that the holder should be entitled to enforce transfer of the object without discussing the policy arguments for allowing this.

#### **4 1 3 A comparison of the various types of preference contract in German law**

The five different types of preference contract discussed above can be compared using the following criteria:

- 1 Can the holder enforce performance of the main contract at any stage?
- 2 If so, at what stage?
- 3 If the holder can enforce performance of the main contract, in what manner is this to be done?

The answers to these questions can be tabulated as follows.

Type of contract	Specific performance of main contract?	At what stage?	In what manner?
<i>Vorkaufsrecht</i>	Yes	Conclusion of a contract with a third party.	Unilateral declaration plus prayer for performance of the main contract
<i>Angebotsvorhand</i>	Yes	Manifestation of a desire to contract, <i>inter alia</i> by entering into serious negotiations with a third party	Combined prayer that the grantor make an offer and that the grantor perform the main contract (same effect as <i>Vorkaufsrecht</i> , one extra prayer involved)
<i>Annahmeverhand</i>	Yes	Manifestation of a desire to contract, <i>inter alia</i> by entering into serious negotiations with a third party party, unless there is a better third party offer available.	Submission of a valid offer to the grantor plus a combined prayer that the grantor must accept that offer and perform the main contract.
<i>Bare preference Vorhand</i>	No	Not applicable	Not applicable
<i>Verhandlungsvorhand</i>	No	Not applicable	Not applicable

Accordingly, the bare preference *Vorhand* grants less power to the holder and more freedom to the grantor.

The *Angebots-* and *Annahmeverhand* grant the holder the most power in the sense that the holder is able to enforce performance of the main contract even before conclusion of a contract with a third party. The trigger event occurs at an earlier stage than under the *Vorkaufsrecht*.

The *Vorkaufsrecht* grants a more streamlined remedy to the holder, as performance of the main contract may be prayed for directly upon the occurrence of the trigger event. The order to make an offer under the *Angebotsvorhand* appears somewhat clumsy and laboured.<sup>172</sup> At least it need not be prayed for in a separate action, but can be prayed for together with an order for performance of the main contract.

The different types of preference contracts can also be compared with reference to the reasons for the introduction of the *Vorkaufsrecht* and the reasons for the continued recognition of the *Vorhand* in practice, to evaluate whether each institution fulfils a role in practice which the others cannot fulfil.

It will be recalled that the *BGB* drafters deliberately chose to limit the trigger event to a contract with a third party for three reasons.

Firstly, it was felt that if anything short of a valid contract would trigger the holder's right to obtain performance of the main contract, the terms on which the holder may enforce performance of the main contract would be too unclear. This is indeed a valid point of criticism against the *Angebots-* and *Annahmeverhand* as was pointed out above. Where the trigger event is anything short of an option granted to a third party, disputes are likely

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<sup>172</sup> Schurig *Das Vorkaufsrecht* 53.

to arise about the terms on which the holder may contract. However, this criticism is not applicable against the bare preference *Vorhand*.

The *BGB* drafters could also have added that in the case of the *Angebots-* and *Annahmeverhand* it is often uncertain whether the trigger event has occurred, again causing a likelihood of disputes. By contrast, the conclusion of a contract with a third party is a more definite trigger event. No such likelihood of disputes is possible in the case of the bare preference *Vorhand* however.

The reasons why parties would still use the *Vorhand* instead of the *Vorkaufsrecht* have already been discussed.<sup>173</sup>

To conclude, we have established that

1. German law recognises a number of different constructions which may apply according to the different contexts in which preference contracts may be used, the relative bargaining power of the parties, the purpose of the holder and the wording chosen for the preference clause. Each of these constructions has some commercial justification.
2. according to Henrich, the default *Vorhand* construction amounts to an *obligatio non faciendi*, which corresponds with the *Hartsvivier* construction and Botha JA's construction. However, where the price is set in the preference contract, the default construction is the *Angebotsvorhand* construction, where the grantor can in one court action obtain specific performance of the substantive contract.

This suggests the following hypotheses for South African law. Firstly, a multiplicity of types of preference contract should be recognised. Secondly, there are two types of preference contract where the wording imports a duty to contract with the holder before

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<sup>173</sup> Par 4 1 2 *supra*.

contracting with a third party. The first is a right to conclude the main contract on the fulfilment of a condition, usually the wish to buy. This would be the applicable default construction where the preference contract determines the terms of the main contract. The second type is a mere right to be preferred above third parties if the grantor should contract, which creates no right to contract.

These hypotheses will next be considered critically against the position in England and the USA.

## **4 2 English law**

The most important textbooks on English contract law contain at best only short paragraphs on rights of pre-emption and first refusal. These textbooks define a right of pre-emption or right of first refusal as an agreement to give the purchaser the right to buy at a figure to be agreed should the landowner wish to sell.<sup>174</sup> They add that it is an undertaking to make an offer in certain specified circumstances at the price at which the owner is in fact prepared to sell.<sup>175</sup> Although they do not discuss the remedies of the holder, the implication is that the normal rules on specific performance apply. This means that a claim for damages is the primary remedy, but the court can order the grantor to make an offer to sell in a proper case.<sup>176</sup> It is therefore possible for the holder to obtain an order that the grantor contract with the holder, and ultimately, an order for specific performance of that contract. An order to transfer property subject to a right of pre-emption upon payment of the purchase price was given in cases in such as *Lord Carrington v Wycombe Railway Co*<sup>177</sup> and *Birmingham Canal Company v Cartwright*.<sup>178</sup> The grantor was ordered to make an offer in *Banstead Urban District Council v*

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<sup>174</sup> Guest *et al* (eds) *Chitty On Contracts: Volume 1 General Principles* 28<sup>th</sup> edition (1999) par 2-117 (at 141); Treitel *The Law of Contract* 10<sup>th</sup> edition (1999) 54.

<sup>175</sup> *Ibid.*

<sup>176</sup> See *Castle Barnsley's Land Options* 2<sup>nd</sup> edition (1992) 186 - 187.

<sup>177</sup> 1868 3 Ch App 377 379, 384.

<sup>178</sup> 1879 11 Ch D 421.

*Wilkinson*.<sup>179</sup> In *Lyle & Scott v Scott's Trustees; Same v British Investment Trust Ltd*<sup>180</sup> the grantors were declared bound to implement an article in the articles of association of the company, which obliged shareholders desirous of selling their shares to inform the secretary in writing of their desire, upon which other shareholders would be invited to purchase the shares. The remedy is therefore seen either as an order to make an offer or an order to perform the main contract, which apparently came into existence extra-judicially. It has been said that the right of pre-emption mutates into an option at the point where the power to compel a disposal arises.<sup>181</sup>

It is important to note that the preference contracts in all these cases indeed either specify the essential terms of the main contract, contain a mechanism for the determination of such terms or indicate otherwise that the holder is granted a right to contract upon the occurrence of a certain event as opposed to a mere preference. This is in fact the case in many decisions on rights of first refusal and rights of pre-emption decided under English law. Accordingly, in Henrich's scheme of preference contracts they should indeed fall under the *Angebotsvorhand* construction, which creates an enforceable right to contract, and not under the bare preference *Vorhand* construction.<sup>182</sup> Therefore these cases do not exclude the application of the bare preference *Vorhand* construction where a contract contains no such indication of a right to buy.

In the following cases the preference contract set a definite price for the exercise of the holder's right: *Banstead Urban District Council v Wilkinson*<sup>183</sup> (£2100), *Gardner v Coutts*<sup>184</sup> (£3000), *Pritchard v Briggs*<sup>185</sup> (£3000). In the following cases, the right to

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<sup>179</sup> 1962 *Estates Gazette* 155 157.

<sup>180</sup> 1959 AC 763.

<sup>181</sup> *Pritchard v Briggs* 1980 Ch 339 (CA); *Castle Barnsley's Land Options* 178 ("At the point where the power to compel a disposal arises, the right of pre-emption mutates into an option").

<sup>182</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* argues that these features communicate the intention to grant a conditional right to contract as opposed to a mere right to be preferred above others. See par 4 1 2 5 *supra*.

<sup>183</sup> *Supra*.

<sup>184</sup> 1968 1 WLR 179.

contract was granted "at a price to be agreed" coupled with a mechanism or standard for ascertaining the price failing agreement: *Lyle & Scott v Scott's Trustees; Same v British Investment Trust Ltd*,<sup>186</sup> (to be fixed by auditor failing agreement), *Murray v Two Strokes Limited*<sup>187</sup> (to be fixed by a valuator failing agreement), *Lord Carington v Wycombe Railway Co*<sup>188</sup> (to be fixed by arbitration according to the Land Clauses Consolidation Act of 1845<sup>189</sup>), *Fraser v Thames Television*<sup>190</sup> ("on terms to be negotiated on the understanding that it would not be in excess of what would be deemed to be a fair fee").<sup>191</sup>

In the following cases, the price was not predetermined, but the preference contract contained some other indication that an enforceable conditional right to buy as opposed to a bare preference is created. In *Manchester Ship Canal Co v Manchester Racecourse Co*<sup>192</sup> the holder only sought (and obtained) an injunction against transfer to a third party purchaser.<sup>193</sup> The case therefore has no direct bearing on the question whether the holder

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<sup>185</sup> *Supra*. In this case the court stated that the "will of the grantor turns [the right of pre-emption] into an option by deciding to sell and thereby binding the grantor to offer it for sale to the grantee." As an option, it then becomes an interest in land, which is a change in the nature of the right to which the court saw "no insuperable objection in logic or in principle" (423). In effect the court sees the right of pre-emption as a conditional option; a construction justifiable by the fact that the parties agreed on a specified price at which the holder may buy on fulfilment of the condition.

<sup>186</sup> 1959 AC 763.

<sup>187</sup> 1973 All ER 357-368.

<sup>188</sup> *Supra*.

<sup>189</sup> Cf Lord Hailsham of St Marylebone *Halsbury's Laws of England Vol 8(1)* 4<sup>th</sup> edition (1996) 335 par 381.

<sup>190</sup> 1984 1 QB 44.

<sup>191</sup> In *Miller v Lakefield Estates Limited* 1989 1 EGLR 212, the preference contract provided that if the co-owners could not agree on the price within a certain period, the property had to be auctioned and the proceeds divided. In this case therefore, the right of first refusal could not be enforced by way of an order to make an offer or to transfer the property. In the absence of agreement on the price, the right of first refusal would fall away and the property had to be auctioned. The court correctly refused an order that one co-owner was entitled to buy the property at a reasonable price.

<sup>192</sup> 1900 2 Ch 352; 1901 2 Ch 37.

<sup>193</sup> 1901 2 Ch 42, 51.

could enforce transfer to itself upon conclusion of a third party contract. In any event, no true right of first refusal was created. The clause provided that if the land should ever cease to be used for racecourse purposes or if it should be proposed to be used for dock purposes, the Racecourse Co would give to the Canal Co the first refusal of the land.<sup>194</sup> The court *a quo* had difficulties with this language,<sup>195</sup> but could not declare the agreement void for vagueness as it formed part of an Act of Parliament.<sup>196</sup> Instead the court *a quo* admitted that giving effect to the agreement might require a certain expansion of the language used.<sup>197</sup> Although the appeal court did not refer to these difficulties of construction, it confirmed that the clause could have more than one meaning<sup>198</sup> whereas no objection on the basis of uncertainty could be entertained as the agreement had statutory validity.<sup>199</sup>

The type of agreement featured in the *Manchester Ship Canal Co* case differs from a right of first refusal in that the condition for the exercise of the holder's right is not merely the wish to sell, but rather the occurrence of some other event. The duty to make an offer would arise if the land should be used for dock purposes even if there was no third party purchaser on the scene.<sup>200</sup> Therefore this is not a right of first refusal or right of pre-emption in the sense of a duty to prefer the purchaser above others, but a right to be made a fair and reasonable offer on the stated event irrespective of whether the grantor wishes to sell or not. In effect, the court construed the preference contract as a conditional option.<sup>201</sup> As it was part of a statute, the court could not decide that the absence of an agreed price or mechanism for determination thereof made the option

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<sup>194</sup> 1900 2 Ch 353; 1901 2 Ch 38.

<sup>195</sup> 1900 2 Ch 360-363

<sup>196</sup> 1900 2 Ch 360-361; 1900 2 Ch 50.

<sup>197</sup> 1900 2 Ch 363.

<sup>198</sup> 1901 2 Ch 46-47.

<sup>199</sup> 1901 2 Ch 50.

<sup>200</sup> 1900 2 Ch 47.

<sup>201</sup> See *Castle Barnsley's Land Options* 159 where similar agreements are constructed as conditional options to purchase.

contract void for vagueness.<sup>202</sup> In view of the peculiar set of facts in the *Manchester Ship Canal Co* case, it is unfortunate that this case and especially the statement that "refusal implies an offer"<sup>203</sup> has exercised so much influence on South African cases dealing with totally different clauses, with no legislative power.<sup>204</sup> The minority in *Soteriou v Retco Poyntons (Pty) Ltd*<sup>205</sup> per Botha JA realized this distinction and rejected the argument that "refusal" necessarily imports an enforceable duty to make an offer.

The preference contract in *Birmingham Canal Co v Cartwright*<sup>206</sup> in effect mirrors the *BGB Vorkaufsrecht*. This explains why it was not construed like the bare preference *Vorhand* of German law. Instead, the court granted an order that there must be an inquiry as to the price at which the mines were sold to the third party and on payment of the price, the grantor must transfer the mines to the holder's successor.<sup>207</sup> In this case, the "trigger event" was defined as a contract of sale with a third party. The clause provided that if the grantor "should sell or agree to sell" the adjoining mines, the grantor should at the same time offer the holder the mines and give the holder the first refusal for one month at the same price as the grantor should have agreed to sell the mines.<sup>208</sup> Accordingly, there was no duty to refrain from contracting with a third party before granting the holder an opportunity to contract. This was therefore clearly not a contract to give the holder the first chance to contract, but rather a conditional option, the

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<sup>202</sup> As was the case in *Ryan v Thomas* 1911 55 Sol Jo 364, in which a similar agreement was declared void for vagueness for the failure to mention a price. In that case the condition on which the holder would have had a first option was also not the grantor's wish to contract, but rather the designation of any land for the purpose of a dairy on the southern side of a road.

<sup>203</sup> 1900 2 Ch 364. See also 1901 2 Ch 49.

<sup>204</sup> See for example the majority judgment in *Soteriou v Retco Poyntons (Pty) Ltd supra per* Nicholas JA at 932G. Cf the attempt by Botha JA in his dissenting judgment in *Soteriou v Retco Poyntons (Pty) Ltd supra* 936D to distinguish *Manchester Ship Canal Co* by reason of the difference in wording of the clauses.

<sup>205</sup> *Supra*.

<sup>206</sup> 1879 11 Ch D 421.

<sup>207</sup> 435.

<sup>208</sup> 421.

condition being a sale to a third party and the terms being the terms agreed with the third party.

The case of *Smith v Morgan*<sup>209</sup> contains a preference contract with no price, no mechanism for determining the price, nor a condition other than the desire to sell. Neither is it a *Vorkaufsrecht*. This case therefore appears to fall under the bare preference *Vorhand* construction in Henrich's typology. Yet the court gave a declaration that, should the grantor have wished to sell the land, she was legally bound to offer the land for sale first to the holder at a price at which she was in fact willing to sell. Does this mean that in English law, all preference contracts give rise to a duty to make an offer which is enforceable by court order? It is submitted that *Smith v Morgan* does not justify that conclusion. The court's declaratory order is not inconsistent with the mere preference or bare preference *Vorhand* construction. The court did not declare anything on the holder's remedies where the grantor manifests an intention to sell. One cannot draw the conclusion that the court would have ordered the grantor to make an offer in such a case. To say that the grantor is legally bound to make an offer is not inconsistent with the negative *Vorhand* construction. Making an offer is the only way in which the grantor may legally be free to sell to another in terms of the bare preference *Vorhand* construction. This case is therefore not inconsistent with the constructions accepted in the *Hartsrivier* and *Owsianick* cases<sup>210</sup> and the similar construction of the bare preference *Vorhand* of German law.<sup>211</sup>

A case which is admittedly inconsistent with these “negative covenant” constructions, is *Kling v Keston Properties Ltd.*<sup>212</sup> The court granted specific performance of the contract

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<sup>209</sup> 1971 1 WLR 803.

<sup>210</sup> *per* Botha JA.

<sup>211</sup> In any event, in his dissenting judgment in *Soteriou v Retco Poyntons (Pty) Ltd supra* 936G, Botha JA emphasised that the clause in *Smith v Morgan supra* differed substantially from the clause considered by the court in that the clause in *Smith v Morgan supra* contained an express reference to an offer to be made which was lacking in the latter.

<sup>212</sup> 1984 44 PCR 212.

which it decided came into existence by the exercise of the right of pre-emption. The right of first refusal agreement provided simply that in the event of the grantor wishing to sell the garage on long lease [*sic*], the holder will have the option to buy it first on terms no less favourable than have been available to other garage buyers or prospective garage buyers when the grantor intend actually to sell it. Arguably this formulation on the terms of the "option" is not as certain as in the other cases cited above, which provide for either a specified price or appraisal or arbitration. However, the court relied heavily on a statement in *Pritchard v Briggs*<sup>213</sup> that a right of pre-emption turns into an option when the grantor decides to sell. It is undoubtedly correct that a preference contract which fixes a price for the main contract, such as the one considered in *Pritchard v Briggs* is in fact a conditional option contract. The court did not note this distinction on the facts. It is arguable, in any event, that the preference clause in *Kling v Keston Properties Ltd* attempts to lay down a price for the main contract which could be interpreted as the market price for any garage in that building at that time.

Accordingly, there is no case in English law which clearly excludes the bare preference *Vorhand* construction in respect of preference contracts containing no arrangement as to price or any other indication that a conditional right to contract is granted.

In fact, the author of *Barnsley's Land Options*, acknowledges that two species of rights of first refusal or right of pre-emption exist, as he mentions two possible formulas for such rights.<sup>214</sup> Firstly, the "normal formula" that the grantor must offer the land of the holder at the stated price or other appropriate figure, should she desire to sell. Secondly, the alternative formula, which merely obliges the grantor to notify the holder of the desire to sell, and leaves the holder to make a suitable offer to buy, which the grantor is free to accept or decline.<sup>215</sup>

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<sup>213</sup> *Supra*.

<sup>214</sup> *Castle Barnsley's Land Options* 157-158. This work apparently contains the most extensive "academic" discussion on rights of first refusal and rights of pre-emption to be found in English law.

<sup>215</sup> The pre-emption clause in the Scottish case of *Roebuck v Edmunds* 1992 *Scots Law Times* 1055 was interpreted similarly to the bare preference *Vorhand* of German law. It provided that "It shall not be in the

The latter formula resembles the *Hartsrivier* construction<sup>216</sup> and the bare preference *Vorhand* construction advocated by Henrich. In effect it only creates an *obligatio non faciendi*. Unlike the *Annahmeverhand* it does not oblige the grantor to accept the holder's offer if it is the highest offer available.

To conclude, the English cases on rights of pre-emption referred to in South African case law do not support a uniform construction of all rights of pre-emption as creating an enforceable duty to make an offer upon the grantor manifesting an intention to sell. English drafters of preference contracts generally provide for a mechanism for determining the terms of the main contract upon the exercise of the right. Such drafting justifies the conclusion that the parties intend the holder to be entitled to contract on those terms. On the other hand, it is recognised that preference contracts could also be drafted so as to free the grantor from the obligation to make an offer to the holder or to accept the holder's offer, as long as the grantor does not contract with a third party on terms not rejected by the holder.

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power of our said disponees and their foresaids [sic] to sell or dispose of the subjects hereby disposed or any part thereof to a third party until they shall first have made a written offer of the same or such part to us...or our successors...at the price and on the conditions on which they may be willing to sell or may conditionally have sold the same...to a third party and we... shall be bound to intimate in writing acceptance or rejection of the offer within fourteen clear days....” The court refused an offer that the holder may buy at the price agreed with a third party where the grantor acknowledged that the transfer to the third party should be set aside. In effect, only the *status quo ante* was restored. The court relied on Halliday *Conveyancing Law and Practice* and withdrawal of a similar claim by the holder in *Matheson v Tinney* (OH) 1989 *Scots Law Times* 535. It argued that pre-emption clauses should be strictly construed and that the clause does not go beyond a duty *not to convey* the property to another without a prior offer to the holder. The court saw no legal basis for a positive obligation to convey the property to the holder in the case of breach. On the other hand, *Matheson v Tinney* (OH) 1989 *Scots Law Times* 535 537 contains an *obiter* statement that “A clause of pre-emption does not prohibit alienation [so as to contravene a statute of 1746] but simply gives the superior or the disponent an option to purchase if the vassal or disponent decides to sell.”

<sup>216</sup> Recognised in *Hartsrivier Boerderij (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T). See par 2 1 2 *supra*.

### 4 3 American law

American case law on rights of first refusal and rights of pre-emption reveals several controversies surrounding the default regime.<sup>217</sup> However, one point on which most courts and writers agree is that such rights are enforceable by specific performance, and grantors have frequently been ordered to convey the object of the right of pre-emption to the holder thereof, in other words, to perform the main contract.<sup>218</sup>

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<sup>217</sup> Flannigan "The Legal Construction of Rights of First Refusal" March-June 1997 *Canadian Bar Review* 1 (on American law). For examples, see also Stutzman and Day "Protecting the Preemptor: Real Property Rights of First Refusal in Light of *Gyurkey v Babler*" 1983 *Idaho Law Review* 277 279 ff; Daskal "Rights of First Refusal and the Package Deal" 1995 *Fordham Urban Law Journal* 461; Platt "The right of first refusal in involuntary sales and transfers by operation of law" 1996 *Baylor Law Review* 1197; Siviglia "Helpful Practice Hints: Rights of first refusal" 1994 *New York State Bar Journal* 56; Conine "Property provisions of the operating agreement - interpretation, validity, and enforceability" 1988 *Texas Tech Law Review* 1263; Karen *et al* (eds) 49 *American Jurisprudence 2d Landlord and Tenant* (1995) § 392 ff.; Karen *et al* (eds) 47 *American Jurisprudence 2d Judicial Sales* (1995) § 168; Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-19 *et seq*, 7-65 *et seq*. Unfortunately, treatises on contract law do not discuss these institutions comprehensively. *Corbin on Contracts Vol IA* §§ 261, 261A & 1197 and *Vol 3* §§ 11.3 & 11.4 contains the most extensive discussions amongst the contract law treatises, but does not mention all the controversies discussed by Flannigan. That "rights of first refusal" do not have a clear default regime is borne out by the following comment by Siviglia 1994 *New York State Bar Journal* 56 "Some agreements merely state that one party will have a 'right of first refusal,' but standing alone, that term has little, if any, meaning. Certainly, in this sparse form, it is an invitation to dispute."

<sup>218</sup> See *inter alia* Corbin *Corbin on Contracts: A Comprehensive Treatise on the Working Rules of Contract Law Vol 5A Sections 1122-1251* (2001 Fall Cumulative Supplement) (hereafter cited as *Corbin Corbin on Contracts Vol 5A*) § 1197 p 377 and cases there cited; Holmes *Corbin on Contracts: Formation of Contracts Vol 3* revised edition (1996) § 11.3 p 480 *et seq* & § 11.4 and cases there cited; Karen *et al* (eds) 71 *American Jurisprudence 2d Specific Performance* (1973) § 146; Karen *et al* (eds) 18A *American Jurisprudence 2d Corporations* (1985) § 586, p 445; *Restatement of American Law - Property* § 395; *Barling v Horn* (1956, Mo) 296 SW 2d 94; *Wilson v Brown* (1936) 5 Cal 2d 425; *Robinson v Drew* 144 A67, 83 NH 459 (1928); *Mobil Exploration & Producing North America Inc v Graham Royalty Ltd* 910 F 2d 504 (8th Cir 1990); *Daniels v Anderson* 162 Ill 2d 47, 204 Ill Dec 666, 642 NE 2d 128 (1994); *Abraham Investment Co v Payne Ranch Inc* 968 SW 2d 518 (Tex App Amarillo 1998); Cross "The ties that bind:

At what point has the grantor been ordered to do so? Firstly, if the grantor purports to retract an offer made to the holder. The same applies where the grantor has given notice to the holder of a third party offer which the grantor is willing to accept and subsequently attempts to retract it.<sup>219</sup> Secondly, where the grantor manifests a desire to accept a good faith offer received from a third party, without having given the requisite notice to the holder.<sup>220</sup> Such desire is most clearly manifested where the grantor has contracted with a third party or has granted the third party an option. However, a lesser manifestation, namely the listing of the property for sale, was regarded as sufficient in a case where the preference contract predetermined the terms of the main contract.<sup>221</sup> This echoes the *Angebotsvorhand* construction of German law. One legal writer states that any evidence that the grantor is willing to contract is sufficient to justify specific enforcement of the promise to offer the land on the terms which the grantor contemplates accepting from a third party.<sup>222</sup>

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preemptive rights and restraints on alienation that commonly burden oil and gas properties” 1999 *Texas Wesleyan Law Review* 193 211. Sometimes it is said that the grantor has a duty to make an offer. (See for example Corbin *Corbin on Contracts Vol 1A* § 470). However, this “duty” is not enforced by an order that the grantor will make an offer. Rather the holder may sue directly for performance of the main contract where the grantor has failed to make an offer on occurrence of the trigger event. Cf also the definition of a right of first refusal by Mitchell “Can a Right of First Refusal be Assigned?” 2001 *University of Chicago Law Review* 985 which implies an enforceable right to purchase triggered when the grantor decides to sell.

<sup>219</sup> Such a notice is seen as an operative offer. At that point the right of first refusal “ripens” into an option (Daskal 1995 *Fordham Urban Law Journal* 461 467).

<sup>220</sup> Stutzman & Day 1983 *Idaho Law Review* 277 278; Corbin *Corbin on Contracts Vol 1A* § 261 p 481 (with reference to *Brenner v Duncan* 27 NW 2d); Holmes *Corbin on Contracts: Formation of Contracts Vol 3* § 11.4 p 488; 49 *American Jurisprudence 2d Landlord and Tenant* (1995) § 393; *Mercer v Lemmens* 230 Call App 2d 167 171. This is also the usual formulation of first refusal agreements. See for example *Sager v Rogers* 1987 WL 6718 at 2 (Tenn Ct App 1987); *Miller v Le Sea Broadcasting Inc* 87 F3d 2241 7th Cir 1996; *Dalton v Balum* 76 ALR 3d 1134 1136 and cases there cited.

<sup>221</sup> *Long v Wayble* 48 Or App 851, 618 P2d 22.

<sup>222</sup> Holmes *Corbin on Contracts: Formation of Contracts Vol 3* § 11.4 p 493, with no reference to case law. Holmes also argues that listing real property with a broker should entitle the holder to buy at the listed price as this does not prejudice the grantor, who would normally ask more than they expect to get for the

There are some limitations on this “right to specific performance.” Firstly, some cases emphasise that the primary remedy for breach of contract remains damages where this sufficiently compensates the holder.<sup>223</sup> Secondly, courts also take into account hardship to the third party when deciding whether to grant specific performance or damages.<sup>224</sup> Thirdly, there is some authority that the holder cannot obtain specific performance upon a lesser manifestation of a desire to contract than conclusion of a third party contract, unless the first refusal agreement specified the price at which the right of first refusal may be exercised.<sup>225</sup>

Unfortunately, the juridical explanation of the holder's enforceable right to obtain specific performance upon a manifestation of a desire to contract is incoherent. The following passage from *Miller v Le Sea Broadcasting Inc*<sup>226</sup> containing the normal explanation to be found in case law and academic literature, shows up this incoherence:

“A right of first refusal is the weakest of options; technically it is not an option at all.... It is merely a pre-emptive right, although it becomes an option when the grantor decides to sell on the terms offered by the third party; at that point the holder of the option has the right to buy the property; a right that is a true option.”<sup>227</sup>

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property (§ 11.4 p 494). He admits that the grantor is inconvenienced when he wishes to “test the market” without being bound to sell to the holder at a listed price.

<sup>223</sup> *Miller v Le Sea Broadcasting Inc supra*. In this case there was evidence that the holder intended to sell the property to a third party for a specified sum and damages was awarded to compensate for the holder's loss of profit instead of specific performance as prayed.

<sup>224</sup> *First National Exchange Bank v Roanoke Oil Co* 1938 169 VA 99, 192 SE 76.

<sup>225</sup> 49 *American Jurisprudence 2d Landlord & Tenant* §439, p 374, especially the discussion of *Ohio Oil Co v Yacktman* (1<sup>st</sup> Dist) 36 Ill App 3d 255, 343 NE 2d 544. Cf also *Holmes Corbin on Contracts Vol 3* 492 n 13 § 11.4.

<sup>226</sup> *Supra* at 226.

<sup>227</sup> The same explanation is to be found in *inter alia* *Corbin Corbin on Contracts Vol 5A* § 1197, p 377 and § 261, p 474; Stutzman & Day 1983 *Idaho Law Review* 277-278; Daskal 1995 *Fordham Urban Law Journal* 461 467; Rosenoer “Acquiring Rights in Tomorrow's Software: First Refusal and First Negotiation Rights under Californian Law” 1990 *The Computer Lawyer* 13; Tew 1989 *Eastern Mineral Law Institute*

The court added later that "[a]lthough a right of first refusal is not an option, it is awfully close."<sup>228</sup>

No understandable explanation is usually given as to why the right of pre-emption suddenly turns into an option. Often the right of pre-emption is said to "ripen"<sup>229</sup> or "mature"<sup>230</sup> into an option. These terms undoubtedly have explanatory value in the agricultural industry, but they do not mean much in contract law. The juridical construction of rights of first refusal therefore appears to be no more than a fiction. The same criticism applies to an "explanation" that the third party's offer "becomes, in essence, the seller's offer to the pre-emptor by operation of the right of first refusal."<sup>231</sup>

That the right of first refusal is regarded as changing into an option on the occurrence of the trigger event suggests that it should be regarded as a conditional option. One author indeed argues that rights of first refusal are conditional options.<sup>232</sup> Many courts have also used "conditional option" terminology.<sup>233</sup> So for example in *Brenner v Duncan*, the court held that the "condition of the option" did occur when the land was sold to a third party.<sup>234</sup> Many courts simply use "option" terminology when referring to rights of first

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*Procedures* 7-1, and the numerous cases cited by these authors. It is also encountered in some Louisianan decisions. See for example Wheat "Clarifying the Nature of Louisiana's Right of First Refusal in the Transfer of Immovables" 1987 *Louisiana Law Review* 899 901-902. This construction has also been accepted in Canadian law. See Flannigan March-June 1997 *Canadian Bar Review* 1 2.

<sup>228</sup> 227.

<sup>229</sup> See *inter alia* Corbin *Corbin on Contracts Vol 1A* §§ 261, 1197; Holmes *Corbin on Contracts Vol 3* § 11.3; Rosenoer 1990 *The Computer Lawyer* 13; 77 *American Jurisprudence 2d Vendor & Purchaser* § 49; *Henderson v Nitschke* (Tex Civ App) 46 ALR 3d 1369 1374.

<sup>230</sup> See *inter alia* Stutzman & Day 1983 *Idaho Law Review* 277 278; Daskal 1995 *Fordham Urban Law Journal* 461 467; *Sager v Rogers* 1987 WL 6718 at 2 (Tenn Ct App 1987).

<sup>231</sup> 49 *American Jurisprudence Landlord and Tenant* § 402, p 349.

<sup>232</sup> Tew 1989 *Eastern Mineral Law Procedures* 7-1 7-4 *et seq.*

<sup>233</sup> *Ibid.*

<sup>234</sup> *Brenner v Duncan* (1947) 318 Mich 127 NW 2d 320. A Canadian court has recognised that a right of first refusal amounts "to an option to purchase under certain conditions" (*Budget Car Rentals Toronto Ltd v*

refusal without specifically using the conditional option construction.<sup>235</sup> What could be the reasons for some courts' and writers' treatment of the right of first refusal as an option after a certain point but not as a conditional option from its creation? No good reason is stated by US writers and courts in common law states.<sup>236</sup> Louisianan academics have mentioned three reasons why it should not be regarded as an option. The first is that article 2462 of the Louisiana Civil Code requires all option contracts to stipulate a time period for acceptance of the option. If this should apply to rights of first refusal, most first refusal agreements would be invalid.<sup>237</sup> This objection should be irrelevant to other states. Secondly, Litvinoff protests that the normal agreement as to price in a first refusal contract, namely that the price may be named by the grantor or be the price at which the grantor is prepared to sell to a third party, though ascertainable, lacks the kind of

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*Petro-Canada Inc* (1989) 60 DLR (4th) 751 (Ont Ct) 756). In this case the first refusal clause was drafted similarly to the normal formulation in the USA. See also the cases cited by Tew 1989 *Eastern Mineral Law Procedures* 7-1 7-8 n 8. See also 49 *American Jurisprudence Landlord and Tenant* in § 397 which states that courts mostly treat the words "first option" as imparting a "conditional option" depending on the landlord's decision or offer to sell. See also Perell "Options, Rights of Repurchase and Rights of First Refusal as Contracts and as Interests in Land" March 1991 *Canadian Bar Review* 1 24 who states that rights of first refusal should be treated as options as they are specifically enforceable though contingent rights to complete a sale. In effect they are essentially similar to options but for the condition.

<sup>235</sup> Cf the terms "first privilege option" (71 *American Jurisprudence 2d Specific Performance* § 1461), "first refusal option" and "option holder" in 47 *American Jurisprudence 2d Judicial Sales* (1995) for 168 p 575 and "pre-emptive right option" as distinct from an "outright option" in *Wellmore Builders v Wannier* 140 A 2d 422, 49 NJ Super 456 (1958) (quoted by Corbin *Corbin on Contracts Vol 1A* § 261 p 472). See also 49 *American Jurisprudence 2d Landlord and Tenant* (1995) § 445 p 379, where it is stated that damages for the failure to honour a right of first refusal can be determined by the value of the "option contract" to the "option holder." Often the preference contract itself provides that the holder should have an option to contract if the grantor decides to contract at all, for example, in *Pritchard v Wick* 178 A2d 725, 406 Pa 598 (1962), quoted by Corbin *Corbin on Contracts Vol 1A* § 261 p 473. The contract provided that the holder would have a 30 day option in case the grantor decided to offer the business for sale.

<sup>236</sup> In American law, conditions simply suspend the operation of a valid and binding contract. The explanation therefore cannot be that no contract exists until fulfilment of a condition. (See McCauliff *Corbin on Contracts Vol 8: Conditions* revised edition (1999) §§ 30.9, 30.5-30.7; 17A *American Jurisprudence 2d Contracts 2<sup>nd</sup>* edition (1991) §§ 465, 52.)

<sup>237</sup> Wheat 1987 *Louisiana Law Review* 899 902 *et seq.*

certainty necessary for a valid option.<sup>238</sup> For this criticism he also relies on article 2462 Louisiana Civil Code. However, that article does not in fact require a specified price, and an ascertainable price should be sufficient. The third objection is that the grantor does not promise to grant an option if he decides to contract, but merely to make an offer with preference to anybody else, “an offer that may even be revocable.” Therefore, only where the parties agree that the grantor will grant the holder an option for a specified time, can the agreement be seen as an option subject to a suspensive condition.<sup>239</sup> This last criticism is well founded<sup>240</sup> except in those cases where the first refusal agreement stipulates a specified period for exercise of the right after notice had been given to the holder. Where such a period is stipulated, the right of first refusal does in fact amount to a conditional option. It should be remembered that Litvinoff’s criticism also applies to the usual formulation that a right of first refusal ripens into an option upon the trigger event. To conclude, American law in effect treat rights of first refusal as conditional options or at least as conditional offers. The condition would be notice to the holder of an acceptable third party offer, or another manifestation of a desire to sell, namely at least the conclusion of a contract with a third party without first granting the holder the opportunity to transact at the same terms.

The question which arises is whether this treatment of the right of first refusal as a conditional option leaves any room for the “bare preference” construction in American law; that is, the equivalent of the *pactum de non contrahendo cum tertii* or the negative or bare preference *Vorhand* construction. Is it possible, as is the case with English law, to explain the American default position on the basis that most if not all the preference contracts considered by the courts would fall under the *Angebotsvorhand* construction in Henrich's typology? This would be the case if they either specified a contract price or

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<sup>238</sup> Litvinoff “Consent revisited: Offer Acceptance Right of First Refusal and Contracts of Adhesion in the Revision of the Louisiana Law of Obligations” 1987 *Louisiana Law Review* 699 754.

<sup>239</sup> *Ibid.*

<sup>240</sup> In *Anderson v Stewart* 149 Neb 616, 32 NW 2d 140 (1948), a Nebraskan court held that the grantor was not bound to sell to the holder where he decided no longer to transact at all. See also 49 *American Jurisprudence 2d Landlord and Tenant* § 395.

contained some other indication that the holder should have a conditional right to buy as opposed to the mere right to be preferred, which is an entitlement to a “*non facere*.” The short answer to this question is “no.” An agreement which simply granted a “a right of first refusal” without any further qualifying terms was held to mean “according to general custom and practice that the holder has the right to elect to take the property at the same price and on the same terms and conditions as those of an offer by a third person that the owner is willing to accept.”<sup>241</sup> However, it could perhaps be argued that this “general custom and practice” arose because of the many cases in which the preference contracts did stipulate a contract price or a mechanism for its determination,<sup>242</sup> or contained a

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<sup>241</sup> *Brownies Creek Collieries Inc v Asher Coal Mining Co* 417 SW 2d 249, 252 (Ky 1967), quoted by Stutzman & Day 1983 *Idaho Law Review* 277 278.

<sup>242</sup> For example *Blair v Kingsley* 128 So 2d 889 and *New Haven Trap Rock Co v Tata* 177 A 2d 798, 149 Conn 181 (1962) (price to be determined by appraisal); *Schenley v Kauth* 96 Ohio App 345 (1953) (an option to purchase in the event that the grantor desires to sell the land, at \$325 per acre); *Old Mission Peninsula School District v French* 107 NW 2d 758, 362 Mich 546 (1961) (\$50); *Kershner v Hurlburt* 277 SW 2d 619 (Mo 1955) (at \$1275 and the cost of improvements); *City of East Orange v Gilchrist* 125 A 2d 225, 41 NJ Super 362 (1956) (\$12,000) (cited by Corbin *Corbin on Contracts IA* § 261A). As was pointed out above, it appears that in states where the right of first refusal is regarded as maturing into an option upon the mere manifestation of the owner's willingness to sell, the omission in a lease granting a right of first refusal of a specified purchase price is fatal to a request for specific performance. (49 *American Jurisprudence 2d Landlord and Tenant* § 439 n 97, p 374). Accordingly it appears that specific performance would not be granted upon a mere manifestation of a desire to sell, unless the preference agreement specifies a contract price. However, upon the conclusion of a contract with a third party, specific performance can be ordered at the price agreed with the third party, provided that the agreed terms are commercially reasonable, imposed in good faith and not specifically designed to defeat the pre-emptive right. (*Sessel Holdings Inc v Fleming Companies supra* 576-577. See also Corbin *Corbin on Contracts IA* § 261 p 474, 476-477). If the price does not comply with these requirements, the holder's failure to exercise his right does not terminate the right of first refusal. These requirements are obviously designed to protect the holder against a fraudulent evasion of his right. The simple solution to this problem supported by Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag*, namely that the preference continues until the grantor actually concludes and performs a contract with a third party on terms which the holder refused, is also followed by some US courts. See for example *Parker v Murphy* 146 SE 254, 152 Va 173 (1929) cited by Corbin *Corbin on Contracts* § 1197 p 378. See also Flannigan March-June 1997 *Canadian Bar Review* 1 2 n 1 and 4.

condition other than the desire to sell<sup>243</sup> or some other positive formulation that the holder would have the opportunity to transact on the occurrence of a certain event.<sup>244</sup> First refusal agreements usually provide that, if the grantor receives a good faith offer and desires to sell, he would give notice to the holder of such offer and the holder would have the option to transact for a specified number of days on the terms and conditions of such offer.<sup>245</sup> An argument may possibly be made that this wording, especially the given time period within which the holder may decide to transact, and the attempt to define the terms on which she may do so, show that a conditional right to transact is intended, and not

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<sup>243</sup> A preference contract which contained a different condition from the grantor's willingness to contract was considered to be specifically enforceable in *City of East Orange v Gilchrist supra* ("shall no longer desire to use and occupy said land") (cited by Corbin *Corbin on Contracts IA* § 261A, p 486). As to why this should make a difference see the discussion of the *Manchester Ship Canal Co* case at n 192 *supra et seq.*

<sup>244</sup> See the cases cited in the next footnote. Some US first refusal agreements create a *Vorkaufsrecht* in that the holder's right to buy is provided to arise on the conclusion of an agreement of sale. An example is *Brenner v Duncan* (1947) 318 Mich 127 1 27 2d 320, where the holder was given a first preference to purchase in the event that the land was to be sold and the parties could agree on a price. This wording clearly does not prohibit the grantor from first contracting with a third party. As the conclusion of an agreement with a third party was not prohibited it necessarily meant that the "right of first refusal" denoted an opportunity to buy and not a mere prohibition of preferring third parties above the holder. Compare *Sessel Holdings Inc v Fleming Companies Inc* 949 F Supp 572 (WD Tenn 1996) where the holder was given a "right of first refusal with respect to any agreement for the sale of SHI's capital stock to a third party." The grantor agreed to give written notice to the holder "upon the signing of a binding or non-binding letter of intent or similar agreement of understanding providing for a sale."

<sup>245</sup> One example is *Toledo P&WRR v Brown* 31 NE 2d 767, 375 Ill 438 (1941) cited by Corbin *Corbin on Contracts IA* § 261, p 480 (for five years the grantor would not accept an offer to purchase by a third party company without first giving notice thereof to the holder and giving the holder an option to purchase for 15 days at the offered price). Cf *Westpark Inc v Seaton Land Co* 171 A 2d 756, 225 Md 433 (1961) (the holder would have a right of first refusal on such terms as the grantor might offer to another or agree to accept); *Abdallah v Abdallah* 17 ALR 3d 967 (1966) (the holder would have the "first privilege of purchasing at the best *bona fide* price which the landlord could obtain"); *Burch v Milner Truck Lines Inc* 199 F Supp 575 (DC Colo 1961) quoted by Corbin *Corbin on Contracts IA* § 261 A, p 485 (if the grantor receives a *bona fide* offer to purchase and desires to sell the object, the grantor will give the holder immediate notice and the holder shall have the first option to acquire the object on the terms and conditions of any such offer).

merely a negative covenant or mere preference in the sense of the bare preference *Vorhand* construction. Unlike the case in South Africa, preference agreements in the US are apparently never drafted as negative covenants to the effect that the grantor shall not contract with a third party unless she first offers to transact with the holder.<sup>246</sup>

It is therefore not too surprising that there is no recognition of a right of first refusal constructed like Henrich's bare preference *Vorhand* or the similar construction laid down in *Hartsrivier*<sup>247</sup> and *Owsianick*<sup>248</sup> per Botha JA and recognised in English law. Of course, US writers recognise that parties could expressly structure the agreement as they please and would not exclude the possibility of such construction if the contract makes it clear that that is what is intended.<sup>249</sup>

If the explanation of the absence of the “the bare preference *Vorhand*” construction does not in fact lie in the normal wording of first refusal agreements, then the explanation must be that US courts generally favour the holder's interest in obtaining performance of the main contract<sup>250</sup> above the grantor's interest to remain as free as possible to deal with his property. However, in respect of a number of controversies surrounding rights of first refusal, many courts emphasise that, because rights of first refusal restrain the free

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<sup>246</sup> See for example the clauses in the numerous cases referred to by Corbin *Corbin on Contracts IA* §§ 261, 261 A, 1197.

<sup>247</sup> *Hartsrivier Boerderye (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T). See par 2 1 2.

<sup>248</sup> *Owsianick v African Consolidated Theatres (Pty) Ltd supra*.

<sup>249</sup> An example of a non-typical type of preference right recognized by American law is a right of first refusal which allows the grantor to contract with a third party as long as the third party acquires the property or other interest in it subject to the holder's right of first refusal (Corbin *Corbin on Contracts IA* § 261, p 474). First negotiation rights, the equivalent of the *Verhandlungsvorhand* of German law, are also recognized (See Rosenoer 1990 *The Computer Lawyer* 13 and Corbin *Corbin on Contracts IA* § 261 A, p 485). Strictly speaking, first negotiation rights are not rights of first refusal because the holder is not given a chance to refuse an offer or opportunity to contract, but only has a chance to submit an offer which need not be accepted.

<sup>250</sup> Whether as a purpose in itself or as a device to protect the holder against unwanted personal or economic associations with third parties. Cf Flannigan March-June 1997 *Canadian Bar Review* 1 6.

alienability of property, their default rules should involve a strict construction against the holder which leaves the grantor as free as possible to deal with his property as he pleases.<sup>251</sup>

The majority of American courts have held that donative transfers, conveyances between related parties, such as affiliated companies or relatives as well as involuntary judicial sales do not trigger the preemptor's right.<sup>252</sup>

Another example of such a controversy is the question whether a "package deal" with a third party triggers the right of first refusal. Many US courts hold that where the grantor sells the object of the right of first refusal as part of a bigger parcel of land, the holder is not entitled to an order for transfer or conveyance of the object of the right of first refusal to himself.<sup>253</sup> The basis of these decisions is that the grantor cannot be compelled to sell one of the lots of land if she desires to sell the land as a whole. Therefore such a package deal does not trigger or activate the right to buy. Some courts do not regard a "package deal" with a third party as a breach at all.<sup>254</sup> They argue that the grantor is only prohibited from selling that piece of land alone.<sup>255</sup> Others see the package deal as a violation of the right of first refusal as opposed to a triggering event and therefore hold that the holder is only entitled to an injunction, reconveyance where the third party knew of the right, or damages.<sup>256</sup> These decisions place the interest of the grantor to remain as free as possible

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<sup>251</sup> See, for example, *Vogel v Melish* 31 Ill 2d 620, 203 NE2d 411, 412-14 (1964) discussed by Mitchell at n 49 *et seq*, where the court reasoned that as a restraint on alienation, the shareholder's agreement was to be strictly construed, to support its finding that the right of first refusal is not assignable.

<sup>252</sup> Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-65 *et seq*.

<sup>253</sup> For details see Daskal 1995 *Fordham Urban Law Journal* 461; Flannigan March-June 1997 *Canadian Bar Review* 1, Stutzman & Day 1983 *Idaho Law Review* 277; Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-69 *et seq* and decisions there cited.

<sup>254</sup> For example, *Sautkulis v Conklin* (1956 2d Dept) 1 App Div 2d 962.

<sup>255</sup> For all details, see Daskal 1995 *Fordham Urban Law Journal* 461; Flannigan March-June 1997 *Canadian Bar Review* 1; Stutzman & Day 1983 *Idaho Law Review* 277 and decisions there cited.

<sup>256</sup> See especially Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-71 who holds that the majority of courts at the time of writing followed this approach.

above the interest of the holder to obtain the property. A number of these cases do in fact mention that, as restraints on the free alienability of property, rights of first refusal should be strictly construed against the holder. The opponents of this approach appeal to the holder's purpose to be able to obtain the property as the purpose of a contract as a whole. They argue also that remedies aimed at preventing the owner from making a sale to someone else are "worthless and illusory" as they give no "immediate, positive benefit" to the holder, so that the holder is unlikely to enter into litigation to obtain this "pyrrhic result."<sup>257</sup>

It is clear that the two sides simply focus on different concerns. The dispute whether the default regime should involve a strict or wider interpretation of rights of first refusal boils down to the question whether and to what extent the grantor's and society's interest in the free alienability of property must be preferred above the holder's desire to obtain the land.<sup>258</sup> Some of the arguments used by the "pro specific performance" camp display a complete disregard of the grantor's interest to be as free as possible in order to obtain the best possible price for his property. An example is Flannigan's argument that transactions like a package deal or dissolution of the grantor company should entitle the holder to buy the object at its market value because "this price standard is implicit in the nature of a right of first refusal."<sup>259</sup> In this way, he counters the argument that there is no way to establish the price at which the holder would be entitled to purchase the property. Flannigan's argument assumes that all rights of first refusal are meant to give the holder the right to buy and not the entitlement to a *non facere*. Secondly it unfairly limits the grantor to the market value, whereas some third party may be prepared to pay a higher

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<sup>257</sup> Flannigan March-June 1997 *Canadian Bar Review* 1 34.

<sup>258</sup> The same conflict of interests is behind many other controversies mentioned by Flannigan March-June 1997 *Canadian Bar Review* 1 *et seq* and Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-65 *et seq*, such as the question whether a gift, the dissolution of the grantor company, the sale of the entire share capital of the grantor company or a sale for consideration which is partly in cash triggers the right of first refusal. The possibility of the grantor deliberately circumventing the right of first refusal is a major consideration for those who argue that such transactions trigger the right of first refusal.

<sup>259</sup> *Supra* 31-32.

price.<sup>260</sup> The argument focuses only on the holder's interests on the basis that “the whole purpose of the right of first refusal is to benefit the holder.” However, this ignores the fact that the holder could benefit to various degrees and in various ways. A bare preference still benefits the holder to some extent. Equally, the holder definitely still benefits from a right of first refusal understood as a right to buy when the trigger event is limited to a sale for cash of that specific object on its own.

To conclude, preference contracts are usually interpreted in American law as creating a conditional right to contract, even where they do not predetermine the terms of the main contract. Where the grantor has breached the preference agreement by contracting with a third party without having granted the holder an opportunity to contract, the holder's right is said to “ripen” into an option so that the holder can bring the main contract into existence by a simple acceptance of that option. However, there is some authority that the preferential right to transact does not turn into an option upon a lesser manifestation of the grantor's desire to contract unless the preference contract predetermines the terms of the main contract. There is some recognition in American law that any desire to sell the preemption property on any terms triggers fixed-price or fair-market-value preemptions, but not necessarily other types of preemption rights which gives the holder a right to match a third party offer.<sup>261</sup> In this respect, American law is in agreement with Henrich and the German writers on publishing law. Henrich confines the *Angebotsvorhand* construction to preference contracts that predetermine the terms of the main contract.<sup>262</sup> The German writers on publishing law confine the conditional option (“in the narrow sense”), which grants the publisher the right to contract upon the author’s decision that her next work is ready for publication, to cases where the “option clause” predetermines the terms of the eventual publishing contract.

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<sup>260</sup> Cf *Soergel & Siebert* (Huber) Vor § 504 Rd Nr 4 (now § 463) who recognise this legitimate interest of the owner to obtain as high a price as possible.

<sup>261</sup> Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-69.

<sup>262</sup> See par 4 1 2 5 *supra*.

## 4 4 Conclusion

The reliance on the *Vorkaufsrecht* in the *Oryx* case is problematic. The normal wording of preference contracts in South Africa leads to the application of the *Vorhand* construction and not the *Vorkaufsrecht* construction. The *Vorkaufsrecht* differs radically from the right considered in the *Oryx* case as it does not prohibit a contract with a third party, instead positing such a contract as a requirement for forcing a decision by the holder whether she wishes to exercise her right. By contrast, the wording of the clause in *Oryx* could be and was interpreted as prohibiting a sale to a third party unless a prior offer was made to the holder.<sup>263</sup> The *Vorkaufsrecht* therefore necessarily implies that the holder has a right to contract with the grantor on the terms agreed with the third party. These are, however, not the only logically valid interpretations of preference contracts creating an *obligatio non contrahendo cum tertii*. German law recognises a number of different types of *Vorhand* contracts which may apply according to the different contexts in which preference contracts may be used, the relative bargaining power of the parties, the purpose of the holder and the wording chosen for the preference clause. Each of these constructions has some commercial justification.

According to Henrich, the writer of the most comprehensive exposition of *Vorhand* contracts, the default *Vorhand* construction amounts to an *obligatio non contrahendo cum tertii* that corresponds with the *Hartsvivier* construction<sup>264</sup> and Botha JA's construction in

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<sup>263</sup> In *Oryx* the clause was formulated as follows: The grantor is not entitled to sell the shares and claims before he has offered the shares and claims to the holder at the same price as that at which he is willing to sell to a third party. Any such offer must be made in writing with reference to the name of the third party and the holder could accept such offer within thirty days of receipt thereof (900E-F). The court saw conclusion of a contract of sale with a third party as breach (see at 904D “na sluiting van ’n koopkontrak in stryd met sy reg...”). In any event, the court did not limit its exposition to the specific clause under consideration.

<sup>264</sup> Recognised in *Hartsvivier Boerderye (Edms) Bpk v Van Niekerk supra*. See par 2 1 2 *supra*.

*Owsianick v African Consolidated Theatres (Pty) Ltd.*<sup>265</sup> However, where the price is set in the preference contract, the default construction is the *Angebotsvorhand* construction, which allows the grantor to obtain an order that an offer be made plus specific performance of the main contract in one action. The justification for this distinction is that the grantor has no *bona fide* interest in sounding out the market upon deciding to contract where the price was predetermined, whereas he has a legitimate interest to do so where no price was fixed.

The English cases on rights of pre-emption referred to in South African case law also do not support a uniform construction of all rights of pre-emption as creating an enforceable duty to make an offer upon manifestation of a desire to sell. English drafters of preference contracts generally provide a mechanism for determining the terms of the main contract upon the exercise of the right, such as valuation by a third party. Such drafting justifies the conclusion that the parties intend the holder to be entitled to contract on those terms. These cases cannot be equated with preference contracts that do not predetermine the price in a like manner. English law also recognises that preference contracts could be drafted with no obligation to make or accept an offer, as long as the grantor does not contract with a third party on terms not rejected by the holder.

In addition, the English case of *Manchester Ship Canal Company v Manchester Racecourse Company*<sup>266</sup> does not support the proposition for which it is widely cited in South African case law, namely that rights of pre-emption necessarily create a duty to make an offer on occurrence of the trigger event.

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<sup>265</sup> *Supra.*

<sup>266</sup> *Supra.*

The almost unanimous support of US courts for a remedy by which the holder can ultimately obtain performance of the main contract upon conclusion of a contract with a third party, challenges the hypothesis suggested by German law that the default construction of preference contracts should be the bare preference contract which only creates a negative obligation. The policy considerations in favour of each construction should be carefully considered. The logical possibility and desirability of a construction which combines the benefits of both the bare preference contract and the construction which allows specific performance of the main contract only upon the grantor actually contracting with a third party, should also be considered. In other words, it must be asked whether a preference contract comprising an *obligatio non contrahendo cum tertii*, and which does not predetermine the terms of the main contract, should entitle the holder to performance of the main contract, but then only upon the grantor in fact contracting with a third party in breach of the preference contract (and not upon a lesser manifestation of a desire to sell). If so, an attempt should be made to explain the basis of this remedy in order to arrive at a coherent, understandable construction.

## 5 A typology of preferential rights to contract

The previous chapters have demonstrated that parties may have very different consequences in mind when concluding agreements granting a so-called “right of first refusal”, “right of pre-emption” or “first option.”

Firstly, some courts and writers have realised that parties sometimes have in mind an *obligatio non contrahendo cum tertii*, which is only enforceable by remedies aimed at restoring the *status quo ante* breach.<sup>1</sup> Understood as such, the preference contract still grants the holder a preference above others – if the grantor decides to contract, she must first give the holder the opportunity to do so before contracting with third parties.

On the other hand, parties to a preference agreement may also intend to grant a right to contract enforceable upon the occurrence of a certain event.<sup>2</sup>

Unfortunately, many drafters do not state clearly what result is intended. In fact, preference agreements often merely state that a first option or right of first refusal is granted. Such a contract can therefore be understood in very different ways. Even those contracts that clearly grant an enforceable conditional right to contract, mostly fail to

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<sup>1</sup> See, for example, *Hartsrivier Boerderye (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T) discussed in par 2 1 2 *supra*, the “normal” (bare preference) *Vorhand* of German law discussed in par 4 1 2 4 *supra* and the Scottish case of *Roebuck v Edmunds* 1992 *Scots Law Times* 1055 discussed in par 4 2 n 212 *supra*. See also the English writer Castle *Barnsley's Land Options* 2<sup>nd</sup> edition (1992) 157-158, who mentions a type of pre-emption contract which merely obliges the grantor to notify the holder of the desire to sell, and leaves the holder to make a suitable offer to buy, which the grantor is free to accept or decline (discussed in par 4 2 *supra*).

<sup>2</sup> Numerous writers and courts have recognized this. See, for example, the decisions in *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd* 1982 3 SA 893 (A), *Owsianick v African Consolidated Theatres (Pty) Ltd* 1967 3 SA 310 (A), the discussion of the *Vorkaufsrecht*, *Angebotsvorhand* and *Annahmeverhand* of German law in paras 4 1 1, 4 1 2 1 and 4 1 2 2 *supra* and the discussion of the position in England and the United States of America in paras 4 2 and 4 3 respectively.

define the condition or trigger event clearly and unambiguously. Accordingly, it is often stated widely enough to include any manifestation of a desire to conclude the substantive contract, as opposed to a stronger indication that the grantor is about to contract with a specific third party, or only the conclusion of the substantive contract with a third party.

Apart from the multiplicity of types of preferential rights that parties may have in mind, there are also a multiplicity of possible juridical explanations, or views on the “legal nature” of these contracts. For example, a preference contract granting an enforceable right to contract could be understood firstly as giving rise to a conditional option, secondly as an enforceable conditional duty to make an offer, or, thirdly, as a conditional duty to make an offer supplemented by a contractual power to create the substantive contract by unilateral declaration. The choice of juridical explanation sometimes has practical implications. For example, if the holder has the contractual power just mentioned or if the preference contract is regarded as a conditional option contract, the holder need only approach a court once to obtain performance of the substantive contract. By contrast, a conditional right to an offer is arguably only enforceable by an order that an offer be made. The holder may therefore require a further court order for specific performance of the substantive contract against a recalcitrant grantor.

In this chapter, I will set out the different types of preference contracts that could conceivably be intended by parties as well as the possible juridical explanations of each type. I will therefore suggest a typology of preferential rights to contract to set the scene for a proposal on how our courts should deal with this multiplicity. This proposal will be set out in a later chapter.

The view that some preferential rights to transact amount to conditional options<sup>3</sup> calls for this typology to include options in order to clarify the relationship between these

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<sup>3</sup> See, for example, Lubbe 1985 *Annual Survey* 137; Reinecke & Otto “Voorkepe en ander voorkeurkontrakte” 1986 *TSAR* 18 24 *et seq*; Janisch “Maintaining the distinction between options and pre-emption agreements” 1990 *Responsa Meridiana* 434 443; Lambiris *Orders of Specific Performance and Restitutio in Integrum in South African Law* (1989) 82-85. *Cf Krauze v Van Wyk* 1984 2 SA 702 (NK).

phenomena. There is clearly a close connection between options and preference contracts. Both prohibit the grantor to contract with a third party until the holder has declined to contract. In this sense, the option holder is to be preferred above third parties, and has the right to first refuse the offer embedded in the option contract.<sup>4</sup> Both options and preference contracts leave the holder totally free to decide whether to contract, but limit the grantor's freedom to contract with others. As noted before, they can accordingly be described as "unilaterally binding" *pacta de contrahendo*, to distinguish them from bilaterally binding "agreements to contract in the future", which also qualify as enforceable *pacta de contrahendo* in some foreign legal systems.<sup>5</sup> The typology will therefore include all "unilaterally binding" *pacta de contrahendo*, with a *caveat* that this term is not wholly correct where the holder undertakes a counter-performance for the option or right of first refusal. In that case the *pactum de contrahendo* is not, strictly speaking, unilaterally binding. However, only the grantor's freedom to contract with whomever he pleases is restricted.

It may perhaps be argued that any attempt to systemise the different types of preference contracts is unnecessary and dangerously dogmatic, as each contract should simply be

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See also the English case of *Pritchard v Briggs* [1980] Ch 339 (CA) and the US case law discussed in the previous chapter. See also Hondius (ed) *Verbintenissenrecht 3 Suppl* 84 (Feb 2001) art 219 paras 285-286 on the position in the Netherlands.

<sup>4</sup> Sometimes American authorities refer to the optionee's power of acceptance as a "refusal" (Tew "Rights Of First Refusal: The "Options" That Are Not Options, But May Become Options" 1989 *Eastern Mineral Law Procedures* 7-1 7-6 and authorities there cited.)

<sup>5</sup> On such "agreements to agree" which bind both parties to conclude another contract, see for example, Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* (1965) 84 *et seq.* I use the term *pacta de contrahendo* in a wide sense to also include agreements which merely prohibit the grantor from concluding the specific contract with a third party, although they do not grant the holder an enforceable right to conclude the contract. For a similar wide definition see Lotz "Purchase and Sale" in Zimmermann & Visser *Southern Cross: Civil Law and Common Law in South Africa* (1996) 384 ("agreements which may lead to contracts"). For other definitions of *pacta de contrahendo* see chapter 1 n 36 *et seq supra*. If a *pactum de contrahendo* is defined as an agreement to conclude an agreement, this term is not wide enough to include all types of preference contracts.

interpreted in its specific context.<sup>6</sup> However, the identification of different types of preference contracts is meant, *inter alia*, as an aid to the process of interpretation, which remains paramount in the analysis of a particular contract. The emphasis on a multiplicity of possible constructions aims to increase awareness of the different legitimate variations that parties may intend, so as to counter the tendency to force preference contracts into a single mould. A number of South African decisions on preference contracts ostensibly recognise the principle of contractual freedom and the need to interpret each individual preference contract. In fact, their statements on the law of preference contracts reveal an insistence on one uniform construction, followed not because of the particular interests and likely intention of the parties involved, but rather on the basis of precedent and historical authority.<sup>7</sup> Another important aim of this typology is to disabuse drafters of preference arrangements of the misconception that hastily drafted, brief preference clause could be interpreted in only one possible way. In reality, the default construction of preference contracts is by no means settled, and more than one interpretation can be placed on the terms “right of first refusal”, “right of pre-emption” or “first option”.<sup>8</sup> The typology therefore also serves as a catalogue of possible constructions that drafters may use in an attempt to reflect the actual intention of the parties before them.

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<sup>6</sup> Huber in Mertens (ed) *Bürgerliches Gesetzbuch mit Einführungsgesetz und Nebengesetzen Kohlhammer-Kommentar begründet von Hs Th Soergel & W Siebert 3: Schuldrecht II (§§ 433-515) AGB-Gesetz, AbzG, EAG, EKG, UN-KaufAbk* (1991) (hereafter cited as *Soergel & Siebert* (Huber)) Vor § 504 RdNr 9 and Schurig *Das Vorkaufsrecht im Privatrecht* (1975) 95 n 423 (writing on German law) criticise Henrich’s attempt to systematically discuss the different possible types of preference contract on the basis that this is always rather a matter of interpretation.

<sup>7</sup> See chapter 2 for examples. Cf also Lubbe’s critique of *Hirschowitz v Moolman* 1985 3 SA 739 (A) in 1985 *Annual Survey* 141. Cf also the South African writers who reject the bare preference construction as illogical and commercially useless and only recognise preference contracts which grant a conditional right to contract (see the discussion under par 1 2 *supra*).

<sup>8</sup> By default construction I mean the body of rules that should apply in the absence of clear regulation by the parties.

Unilaterally binding *pacta de contrahendo* can be grouped in different ways. They could, for example, be grouped into two main groups according to whether they create an *obligatio non contrahendo cum tertii*, or not. In this chapter, I will instead categorise them into two main categories according to whether they grant the holder an enforceable right to contract or not. The first group comprises preference arrangements that grant the holder a mere right to be preferred above third parties (a “bare preference”) and not a right to contract (5 1 below). The second category, which grants a right to contract, could be conditional or unconditional and will be discussed in paragraph 5 2 below.

A “bare preference” is something less than a right to transact. It does not oblige the grantor to do anything else than refrain from contracting with third parties until the holder has declined the chance of contracting with the grantor. As such it only creates a negative obligation, an *obligatio non contrahendo cum tertii*. This negative obligation continues until the grantor has actually concluded and performed a contract with a third party on terms that the holder was given an opportunity to match. Therefore it can be described as a negative obligation subject to a resolutive condition.

The second main group of contracts (which grants an enforceable right to contract) can be divided into two main subtypes. Firstly those arrangements where the right to contract is unconditional (5 2 1 below). This subtype comprises unconditional option contracts in the traditional sense. Secondly, those arrangements where the right to contract is conditional (5 2 2 below). This group comprises conditional options in the traditional sense as well as some preference contracts. The preference contracts in this category are all conditional upon some manifestation of a desire to contract by the grantor, whereas the condition suspending conditional options in the traditional sense relates to some other event. The trigger event of a preference contract granting a right to contract could be any manifestation of a desire to sell (with some variation in its precise formulation) or it could only be an undertaking to contract with a third party. The exact operation of these preference contracts and their juristic explanation are also subject to variation. For example, a right of first refusal which is triggered only by conclusion of a third party contract could be understood as a conditional option, or as an enforceable right that an

offer be made immediately before the grantor contracts with a third party. These juristic explanations could impact on the remedies available for breach. For example, the conditional option explanation means that the holder may unilaterally create the substantive contract, whereas the other view implies that the holder must pray for an order that an offer be made.

Only some basic aspects of each construction will be discussed, such as its sphere of application, validity requirements, when and how it may be exercised, remedies for breach and termination.<sup>9</sup> Which type of preference contract should apply in which situation will only be fully considered in a later chapter after possible types have been set out here. Any comments in this chapter on a type's sphere of application will therefore only be provisional examples of situations in which that type could or could not apply.

## **5 1 The bare preference contract**

Parties to a preference contract sometimes intend that the holder should have no conditional right to contract, but rather a right that the grantor would not contract with a third party unless the holder has first been given a chance to do so. In such a case, the holder is not entitled to contract with the grantor upon the occurrence of a certain event. The term “trigger event” plays no role in these contracts, as the grantor’s obligation does not change from conclusion of the contract. The holder is only entitled to a *non facere*, namely that the grantor refrain from contracting with third parties. This negative obligation is subject to a resolutive condition, namely that the holder fails to match a third party offer submitted to the holder or fails to indicate that he is interested in contracting with the grantor. If the holder does not match the third party offer, the grantor is free to contract with the third party.

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<sup>9</sup> A detailed consideration of issues such as what transactions would trigger the right, the effect of the holder’s inability to perform some of the obligations undertaken by the third party, whether the right is actively or passively transmissible or capable of constituting a real right, are beyond the scope of this study, but some of these issues will be touched upon in chapter 7 *infra*.

This is the type of preference contract advocated by Henrich and German writers on publishing law as the default *Vorhand*.<sup>10</sup> The majority in *Owsianick v African Consolidated Theatres (Pty) Ltd*<sup>11</sup> and the court in *Hartsrivier Boerderye (Edms) Bpk v Van Niekerk*<sup>12</sup> construed the preference contracts under consideration in a similar manner, although they did not clearly decide on the remedies for breach of the *obligatio non contrahendo cum tertii*.<sup>13</sup> Although South African writers have criticized these decisions,<sup>14</sup> some writers concede that parties may expressly structure their preference contract as set out in the *Hartsrivier Boerderye* case.<sup>15</sup>

As a negative obligation, the bare preference agreement is specifically enforceable by an interdict prohibiting conclusion of a contract with a third party. Where the third party is *mala fide*, the holder is also entitled to have the transfer to the third party set aside.<sup>16</sup> In the alternative, the holder may claim cancellation of the preference contract and damages. The remedy of cancellation could be used to reclaim any counter-performance or consideration given for the preference.<sup>17</sup>

It is generally accepted that an award of damages should actually place the holder in the position it would have been in had the grantor contracted with the holder on the same

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<sup>10</sup> See *supra* paras 4 1 2 3 and 4 1 2 4.

<sup>11</sup> *Supra*.

<sup>12</sup> *Hartsrivier Boerderye (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T).

<sup>13</sup> See par 2 1 *supra*.

<sup>14</sup> Cooper *The South African Law of Landlord and Tenant* 2<sup>nd</sup> edition (1994) 143-144; Reinecke & Otto 20 1986 *TSAR* 18; Eiselen “*Souteriou v Retco Poyntons (Pty) Ltd* 1985 2 SA 922 (A): Voorkoopreg – regte en verpligtinge van partye” 1986 *THRHR* 95 97. Many writers have also welcomed the *Oryx* decision which rejected the approach of the majority in *Owsianick*. See further par 1 2 *supra*.

<sup>15</sup> Eiselen 1986 *THRHR* 95 97; Lubbe & Murray *Farlam & Hathaway's Contract: Cases, Materials and Commentary* 3<sup>rd</sup> edition (1988) 92; Van der Merwe *et al Contract: General Principles* (1993) 62-63; Floyd “Die Voorkoopreg” 1986 *THRHR* 253 261; Lubbe 1986 *Annual Survey* 144-145.

<sup>16</sup> By reason of the doctrine of notice (*Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd* 1982 3 SA 893 (A)).

<sup>17</sup> *Transvaal Silver Mines v Jacobs, Le Grange & Fox* 1891 4 SAR 116.

terms agreed with a third party.<sup>18</sup> What is the justification for this in the present context, seeing that the grantor never had an obligation to contract with the holder? Henrich states that the holder may claim damages if he can prove that he would have made an offer that would have persuaded the grantor to contract with him in response to notice by the grantor that she wishes to contract with a specific third party on specific terms.<sup>19</sup> He reasons further that the grantor cannot claim that she would not have sold to the holder, because this would amount to the guilty party relying on the contract which allows the grantor to refrain from selling to anybody.<sup>20</sup> The grantor can only rely on the contract insofar as the grantor has acted in accordance with the contract.<sup>21</sup> The following is perhaps a better explanation. A claim for damages aims to place the holder in the position she would have been in had the contract not been breached. The grantor could have fulfilled the contract in one of two ways. Firstly by not contracting with anybody and, secondly, by contracting with the holder. As the first situation is unlikely to have occurred because of the breach that clearly shows the grantor's wish to contract, it is more logical to compensate the holder on the basis of the second scenario. In other words, it could be said that the holder was able to prove on a balance of probabilities that if the grantor had obeyed the contract, the grantor would have contracted with the holder.

This type of bare preference contract can be structured in two ways, depending on the method by which the grantor can be released from the *obligatio non contrahendo cum tertii*. According to the first, the grantor need never make an offer to be freed of the obligation, but must only invite the holder to match a third party offer. According to the second, the grantor must make an offer to the holder to escape the *obligatio non faciendi*. This distinction is probably overvalued. Even if the second construction applies, the holder's failure or refusal to respond to an invitation to make an offer would very often be

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<sup>18</sup> *Bellairs v Hodnett* 1978 1 SA 1109 (A) 1139H-1140A; *Sher v Allen* 1929 OPD 137 147; Floyd 1986 THRHR 253 254; Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 367-368.

<sup>19</sup> *Ibid.*

<sup>20</sup> *Ibid.*

<sup>21</sup> *Ibid.*

regarded as a waiver of the preferential right to contract, so that the grantor would be released without having made an offer.

### *5 1 1 Notice of third party offer prerequisite for release*

In terms of this construction, the grantor can rid himself of the *obligatio non contrahendo cum tertii* by notifying the holder of the identity of an interested third party and the terms offered by her and inviting him to match the third party's offer.<sup>22</sup> The grantor need not take the risk of making an offer to the holder. This would be a risk because in the meantime a better third party offer may materialize before the grantor is able to withdraw the offer to the holder. If the holder responds with a matching or higher offer, the grantor need not accept that. The grantor may simply not contract with a third party at the terms acceptable to the holder or at more advantageous terms. Therefore the grantor is better able to sound out the market than if she had to make an offer to the holder in order to shake off the preference agreement.

In the *Hartsvivier* case,<sup>23</sup> the court interpreted a clause which granted the holder "a right of first refusal if the grantor would decide to sell the farm"<sup>24</sup> as placing a duty on the grantor to grant the holder a reasonable opportunity to make an offer, which the grantor need not accept.<sup>25</sup>

## *I Validity Requirements*

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<sup>22</sup> A notice that the grantor desires to contract should be regarded as a tacit invitation to make an offer.

<sup>23</sup> *Hartsvivier Boerderye (Edms) Bpk v Van Niekerk supra*.

<sup>24</sup> My free and abridged translation of the Afrikaans clause which read as follows: "Indien die verhuurder te enige tyd gedurende die huurtermyn of by die verstryking daarvan sou besluit om die plaas te verkoop dan sal die huurder die eerste reg van weiering besit om gemelde plaas aan te koop."

<sup>25</sup> 705H.

As this type of preference contract does not give the holder a right to ultimately obtain the object or property, it need not comply with formalities, such as those prescribed by the Alienation of Land Act. Because it is not a conditional option or conditional right to an offer, the terms of the substantive contract or offer need not be ascertainable from the preference contract.

## *II Termination*

In *Hartsrivier Boerderye (Edms) Bpk v Van Niekerk*,<sup>26</sup> the court decided that the grantor had to give the holder a reasonable time within which to make the offer.<sup>27</sup> If the holder fails to make a valid offer within a reasonable time fixed in the invitation, his right lapses. An oral indication that the holder wants to contract is therefore not sufficient where the substantive contract must comply with formalities.<sup>28</sup> This is a fair rule. If a mere non-binding indication that the holder is prepared to contract would prohibit the conclusion of the substantive contract with a third party, this would be unfair to the grantor if the holder later indicates that he no longer wishes to contract.

Where the grantor made a simple invitation to submit an offer without any additional information, the holder's outright failure or refusal to respond would normally amount to waiver of the right. This conduct normally indicates that the holder is not interested in contracting at all with the grantor, and that the grantor is free to contract with any third party at any terms whatsoever.

In the absence of such a waiver, does the preference contract continue until the grantor performs a contract concluded with a third party, of whose offer and identity the holder

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<sup>26</sup> *Supra*.

<sup>27</sup> 705H.

<sup>28</sup> 706H. See further par 2 1 2 *supra*.

knew at the time of the invitation, or does the rejected invitation to the holder result in the grantor's release?

It is submitted that, in the absence of any complaint from the holder, the grantor's failure to disclose a third party's identity should not preclude the grantor from contracting with that third party. If the holder never requested such information, the grantor may assume that this information is not important to the holder.<sup>29</sup>

However, the holder should be entitled to insist on disclosure of any third party offeror's identity. The primary purpose of a preference contract is often to enable the holder to control the identity of third parties with which the grantor may contract, rather than to allow the holder the chance of obtaining the property. If the grantor fails to accede to such a request, the preference contract should not terminate merely because the holder was granted an opportunity to make an offer. In other words, where the holder made such a request, the grantor would only be released upon contracting with a third party whose identity has been disclosed to the holder when the latter was invited to make an offer.

Should the same reasoning apply to a failure to inform the holder of the terms on which the grantor intends to contract? In other words, would the grantor only be released if her rejected invitation to the holder included information on competing third party offers? Can the onus be placed upon the holder to find out what offers the grantor is considering, so that the failure to do so would constitute a waiver of her right regardless of whether the grantor is considering any third party offers? A related question concerns the effect of an offer by the holder made without any knowledge of third party offers. Would the grantor then be free to immediately sell to a third party at a higher figure, even if the

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<sup>29</sup> Austrian law requires the grantor to inform the holder of the third party's identity before the time limit within which the *Vorkaufsrecht* must be exercised begins to run. See 1957 *Evidenzblatt* 547 (Nr 349) 548. However, where the holder comes to know of the third party's identity during the course of negotiations with the grantor, the failure to include these particulars in the grantor's notice is irrelevant (SZ 22/34 (16.3.1949)).

holder was not informed of the terms on which the grantor is willing to contract with the third party?

If the grantor is obliged to inform the holder of the terms on which she is prepared to contract before she may be released, the holder would more seriously consider the invitation to make an offer. This would enhance the probability of a realistic offer and reduce the risk of losing the preferential right through too low an offer. The terms of competing third party offers are evidently important for the holder's decision on the terms he should offer. The grantor, on the other hand, has a legitimate interest to obtain as high a price as possible and may perhaps expect the holder to make a much higher offer than the third party offers at hand. If the holder had an enforceable right to information on third party offers, he would very likely pitch the offer only just above the highest third party offer instead of at a much higher figure which he would otherwise be prepared to offer. The grantor would then lose the opportunity to sell at a higher price to the holder.<sup>30</sup> A balancing out of these interests requires that the holder need not be protected against voluntarily making "too high" an offer (too high because the grantor would probably have accepted a lower one), but should be protected against "too low" an offer, which would result in the holder losing the opportunity to contract to a third party of whose offer the holder did not know.

The fairest solution would therefore be a general rule that for the grantor to be free to contract with a third party on certain terms, the terms must be disclosed to the holder and the holder must be invited to make an offer at those terms.<sup>31</sup> This also means that where

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<sup>30</sup> Cf the reasoning in *Bellairs v Hodnett supra* 1138F-1139A.

<sup>31</sup> A requirement that the grantor must act *bona fide* by not conniving with the third party to place terms in the third party offer which the grantor knows the holder cannot match and in which he has no *bona fide* interest may be a necessary check on the grantor where the grantor proposes *incidental* in the offer to the holder which suits the third party but which the holder cannot fulfill, and in which the grantor has no actual interest. This would only concern incidental terms and not the contract price itself. The rule on termination argued for sufficiently protects the holder against the grantor seeking to rid himself of the holder by setting up a ridiculously high offer by a third party. This requirement of *bona fides* will not be considered in depth here. I will return to the topic in a later chapter.

the holder submits an offer of R5000 in response to the grantor's invitation without knowing of a competing third party offer of R6000, the grantor would not be free to contract with the third party at R6000 unless the holder has been given a chance to match that offer.

Moreover, the grantor should only be released if she contracts with that third party at the disclosed price within a reasonable time. Otherwise the possibility of a grantor deliberately evading his duties aided by inflation would still exist. For example, the grantor could offer the object for sale at R200 000 to the holder, knowing that this is way above market value at that stage. Upon the holder refusing this offer on the basis that the price is too high, the grantor could then wait another year and offer the property to a third party to whom he actually wishes to sell at R200 000, which could then be a fair price for the property. Would it not be fairer if the holder should again get an opportunity to buy at R200 000 a year later? Surely this would not prejudice the grantor. To protect the holder against such a scenario, a qualification should therefore be added that the grantor would only be released from the preference if she sells within a reasonable time after making the offer to the holder (to any third party).<sup>32</sup> The grantor would therefore be released only if she sells to the same third party whose offer was put to the holder, within a reasonable time after the holder has rejected or failed to accept the offer. If not, the preferential right continues to exist and the grantor would once more have to invite the holder to match terms on which the grantor is prepared to contract at a later stage, even if these terms are exactly the same as the ones originally offered to the holder.

This rule does not mean that the grantor is under an enforceable duty to inform the holder of each and every offer received. Neither can a holder force a grantor who has simply invited an offer to disclose the terms of third party offers received. Accordingly, the holder may request that information upon being invited to make an offer and may remind the grantor that without such disclosure the grantor may not lawfully contract with a third

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<sup>32</sup> It is granted that the "reasonable time" requirement may lead to uncertainties.

party, but the holder may not force the grantor by court order to make such disclosure.<sup>33</sup> The rule argued for is that failure to disclose such a third party offer means that the grantor may not lawfully contract on those terms with a third party. It does not express the grantor's duty, but merely amounts to a qualification of the method by which the grantor may be released from the preference contract.

### *III Sphere of Application*

Is the bare preference construction excluded by a formulation that “the grantor must offer to contract with the holder before the grantor contracts with a third party” or, “when the grantor wants to contract, she must first offer to contract with the holder”? Does the word “offer” mean that a mere invitation or notice to the holder is not good enough, but that only an offer would release the grantor?<sup>34</sup>

As was said before, even if these words do import that only an offer to the holder will release the grantor, this will not make much difference in practice as a failure or refusal to respond to the grantor's invitation to make an offer may nevertheless amount to a waiver of the holder's right, so that the grantor would be released without making an offer.

However, where, in reply to the grantor's invitation, the holder insists that it is the grantor who should make an offer, the refusal to make an offer cannot be said to amount to a waiver. In that case, would notice to the holder of a third party offer and an invitation to make an offer on those terms be enough, so that the holder's failure to do so, releases the

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<sup>33</sup> In any event, such a remedy would be rather toothless against a recalcitrant grantor.

<sup>34</sup> Although the Austrian code foresees that the grantor should make an offer to the holder before she is released (§ 1072 ABGB: *anbieten soll*), some Austrian writers argue that notice to the holder is sufficient. See, for example, Faistenberger C *Das Vorkaufsrecht* (1967), Welser R “*Das Vorkaufsrecht. Zum Vorkauf im Österreichischen Bürgerlichen Recht. Von Christoph Faistenberger (Buchbesprechung)*” 1971 *Zeitschrift für Rechtsvergleichung* 313.

grantor? It is submitted that in this scenario the grantor has given the holder the opportunity to contract on the same terms as the third party and if the holder fails to indicate a willingness to contract on those terms, the grantor should be free to contract on those terms with a third party. If this reasoning is not persuasive, the next sub-type must be recognised to cater for clauses providing for the making of an offer.

Grantors who want to grant a limited preferential right to transact should rather not use the word "offer" in the preference clause. An alternative formulation would be that when the grantor wishes to contract he should first invite the holder to make an offer. If the holder fails to do so within a stated or reasonable time, the grantor would be free to contract at any terms with any third party. If the holder does make an offer, the grantor need not accept that offer, but may not contract with a third party on the same terms or on terms more beneficial to the holder, unless the holder has first been given an opportunity to match those terms and has failed to do so.

#### 5 1 2 *Offer to holder prerequisite for release*

In terms of this construction, the grantor can never be forced to make an offer, but making an offer is the only way in which the grantor can lawfully be released from the obligation not to contract with third parties, that is, if the holder rejects or fails to accept that offer.

The rules relating to validity requirements and termination discussed under the previous heading<sup>35</sup> should apply *mutatis mutandis* to this construction. Again, the mere fact that the holder has rejected or failed to accept the offer, does not terminate the preference agreement. The grantor may not after such rejection contract with a third party at any price. The *obligatio non faciendi* only terminates when the grantor actually contracts with a third party within a reasonable time on terms offered to and rejected by the holder. This rule protects the holder against the possibility of the grantor making an

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<sup>35</sup> Par 5 1 1 *supra*.

unrealistically high offer in order to shake off the holder and thereafter contracting with a third party on more realistic terms. It precludes the need for a rule that the grantor would only be released upon making a good faith or reasonable offer as far as the price is concerned, which is bound to lead to disputes.<sup>36</sup>

## **5 2 A right to contract**

These arrangements do not merely grant a right to be preferred above third parties. They do not only encompass an *obligatio non contrahendo cum tertii*, but also grant the holder a right to contract with the grantor or to directly obtain performance of the substantive contract under certain circumstances. “Right to contract” is used to denote both these possibilities.

### **5 2 1 An unconditional right to contract (unconditional option)**

The holder of an unconditional option has an immediate right to contract. The only step required to bring the substantive contract into existence is the exercise of the option by the holder. This takes the form of acceptance of the offer embedded in or protected by the option contract.<sup>37</sup> Once the holder has exercised the option, the normal remedies for enforcement of the substantive contract are available.

The offer embedded in the option contract must comply with the normal requirements for certainty.<sup>38</sup> If nothing is said as to the contract price, the possibility of a tacit price

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<sup>36</sup> See n 31 *supra* on the possible need to still require a *bona fide* offer as far as other contract terms are concerned.

<sup>37</sup> See generally De Wet & Van Wyk *Kontraktereg en Handelsreg Vol 1* (1992) 34; Van der Merwe *et al Contract* 58 *et seq*; Lubbe & Murray *Contract* 75; Kerr *The Principles of the Law of Contract* 5<sup>th</sup> edition (1998) 77 *et seq*; Christie *The Law of Contract in South Africa* 4<sup>th</sup> edition (2001) 59 *et seq*.

<sup>38</sup> *McGregor v Jordaan* 1920 CPD 209 213; De Wet & Van Wyk *Kontraktereg* 34; Van der Merwe *et al Contract* 60 *et seq*; Lubbe & Murray *Contract* 74-75; *cf* Kerr *Contract* 77-78. On the requirement of

determination must be considered. The grantor would be taken to have tacitly intended the usual price, if one exists.<sup>39</sup> In the absence of a usual price, our courts have been unwilling to imply a reasonable price into a sale or lease contract, and have only done so in respect of contracts for services.<sup>40</sup> Such sale or lease contracts have therefore been held to be void for uncertainty. Recently, our courts have indicated that agreements to sell or lease at a reasonable price should be valid.<sup>41</sup> However, no court has stated that an obligation to pay a reasonable price should be implied where no price was agreed upon.

The offer embedded in the option contract and the acceptance thereof must, of course, comply with the formalities required for the substantive contract.<sup>42</sup>

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certainty generally see *De Wet & Van Wyk Kontraktereg* 93 *et seq*; *Lubbe & Murray Contract* at 314 *et seq*; *Van der Merwe et al Contract* 161 *et seq*; *Kerr Contract* 71.

<sup>39</sup> *Lombard v Pongola Sugar Milling Co Ltd* 1963 4 SA 119 (D); *Globe Electrical Transvaal (Pty) Ltd v Brunhuber* 1970 3 SA 99 (E); *Adcorp Spares PE (Pty) Ltd v Hydromulch* 1972 3 SA 663 (T); *Shell SA (Pty) Ltd v Corbitt* 1986 4 SA 532 (C) 526-527; *De Wet & Van Wyk Kontraktereg* 315.

<sup>40</sup> *Erasmus v Arcade Electric* 1962 3 SA 418 (T); *Adcorp Spares PE (Pty) Ltd v Hydromulch supra*; *Elite Electrical Contractors v The Covered Wagon Restaurant* 1973 1 SA 195 (RA); *Lubbe & Murray Contract* 315; *De Wet & Van Wyk Kontraktereg* 315.

<sup>41</sup> See the *obiter dictum* to this effect in *Genac Properties Jhb (Pty) Ltd v NBC Administrators CC (previously NBC Administrators (Pty) Ltd* 1992 1 SA 566 (A) 577G-578C. This dictum was approved in *Engen Petroleum Ltd v Kommandonek (Pty) Ltd* 2001 2 SA 170 (W) 170 173G-174G.

<sup>42</sup> *Rogers v Phillips* 1985 3 SA 183 (E) 187 emphasises that *Brand v Spies* 1960 4 SA 14 (E) only laid down that the offer and acceptance must be in writing. Therefore there is no reason why a written offer cannot be the subject of an oral (option) agreement to keep it open for a certain period. This is also the position laid down by *Venter v Birchholtz* 1972 1 SA 276 (A). *Hirschowitz v Moolman supra* overruled *Rogers v Phillips* as far as rights of pre-emption are concerned by deciding that *pacta de contrahendo* generally has to conform to the formal requirements for the contemplated contract (766D-E; *obiter* on options at 767F-G). However, it is submitted that the analysis in *Rogers v Phillips* is correct, and that the position regarding options is still as set out in *Venter v Birchholtz*. See further Van Rensburg "Formaliteitsvoorskrifte, Voorkoopregte en Opsies" 1986 *THRHR* 208 213-215; *Lubbe & Murray Contract* 75; *Van der Merwe et al Contract* 60-61; *De Wet & Van Wyk Kontraktereg* 31; *Lubbe 1985 Annual Survey* 140 *et seq*; *Reinecke & Otto* 1986 *TSAR* 18 31 *et seq* and authorities there cited.

The normal rules for an acceptance regulates the manner in which the conditional option must be exercised. Where the option contract does not specify a period for its duration, the default rule is apparently that the holder has a reasonable time to accept the offer, otherwise it will lapse.<sup>43</sup>

The option is breached when the grantor refuses to accept that the substantive contract came into being upon a valid exercise of the option. Breach also occurs where the grantor contracts with a third party although the holder has not rejected the offer embedded in the option contract. The normal remedies for breach and prevention of breach are available, including specific performance of the substantive contract.<sup>44</sup>

## 5 2 2 A conditional right to contract

This category comprises, firstly, options in the traditional sense that are subject to some suspensive condition (5 1 2 2 below), and secondly, rights of first refusal that entitle the holder to ultimately enforce the substantive contract upon occurrence of a certain event (5 1 2 1 below).

The distinction between these two subtypes lies firstly in the nature of the suspensive condition.<sup>45</sup> In the second subtype, the condition suspending the right to contract relates to the manifestation of a desire to contract by the grantor, which is a potestative or mixed condition. In the first subtype, the condition relates to something other than the manifestation of a desire to contract. It could, for example, be a change in the use of the land or the holder's marriage to the grantor's son. These conditions are mixed conditions as the grantor retains control over fulfilment of the condition.

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<sup>43</sup> Cf Lubbe & Murray *Contract* 39; Christie *Contract* 54; Van der Merwe *et al Contract* 60.

<sup>44</sup> *Thompson v Van der Vyver* 1954 2 SA 192 (C); *McGregor v Jordaan* 1921 CPD 301; *Botes v Botes* 1964 1 SA 623 (O); Van der Merwe *et al Contract* 61; Joubert *General Principles of the Law of Contract* (1987) 55-56.

<sup>45</sup> Tew "Rights of First Refusal: The 'Options' That Are Not Options, But May Become Options" 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-7.

Another difference encountered in South African law, but not in all foreign jurisdictions, is the notion that the second subtype does not oblige the grantor to keep open an offer made after fulfilment of the condition, whereas a conditional option traditionally does.<sup>46</sup> *Wissekerke v Wissekerke*<sup>47</sup> allows the grantor of a right of first refusal to withdraw any offer at that stage as long as the holder had not exercised the right, but only if the grantor can show that he no longer wishes to contract at all.<sup>48</sup>

The second subtype is subject to variation according to what suffices as a manifestation of the desire to sell, namely the conclusion of a contract with a third party or something less, as well as according to the exact duties and rights of the parties upon fulfilment of the condition.

#### 5 2 2 1 *Conditional options in the traditional sense*

The traditional understanding of a conditional option is that it is an option subject to a suspensive condition that does not relate to the grantor's desire to conclude the substantive contract.

An example is an agreement that, if certain land would cease to be used for racecourse purposes or would at any time be proposed to be used for dock purposes, the holder would have an option to buy it at an ascertainable price.<sup>49</sup>

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<sup>46</sup> *Boyd v Nel* 1922 AD 414 421; *Hersch v Nel* 1948 3 SA 686 (A) 695; *Brand v Spies* 1960 4 SA 14 (E) 16; *Venter v Birchholtz* 1972 1 SA 276 (A) 283; *Anglo Carpets (Pty) Ltd v Snyman* 1978 3 SA 582 (T) 585. See also Lubbe & Murray *Contract* 72 n 1; Kerr *Contract* 77 *et seq.* However, there is some uncertainty as to the effect of an option which does not specify a period for its duration. See further at n 100 *infra*.

<sup>47</sup> 1970 2 SA 550 (A).

<sup>48</sup> Kerr *Contract* 77 suggests that the grantor should show some change in circumstances giving cause for his change of mind, in order to ensure that the grantor is acting in good faith.

<sup>49</sup> *Cf Manchester Ship Canal Company v Manchester Racecourse Company* 1900 2 Ch 352; 1901 2 Ch 37 (CA) and *Taylor & Claridge v Van Jaarsveld & Nellmapius* 1887 TS 137. Another example is where A

The rules on the validity requirements, exercise and remedies for breach of conditional option are *mutatis mutandis* the same as that of unconditional options and will not be repeated here.

#### 5 2 2 2 Right to contract conditional upon the manifestation of a desire to contract

The trigger event of a preference contract granting a right to contract could be any manifestation of a desire to sell or it could only be an undertaking to contract with a third party. The exact operation of these preference contracts and their juristic explanation are also subject to variation. For example, a right of first refusal which is triggered only by conclusion of a third party contract could be understood as a conditional option, or as an enforceable right that an offer be made immediately before the grantor contracts with a third party. These juristic explanations impact on the remedies available for breach. For example, the conditional option explanation means that the holder may unilaterally create the substantive contract by acceptance of the offer embedded in the preference contract, whereas the other view implies that the holder must pray for an order that an offer be made.

South African lawyers may protest that “desire to sell” is a potestative condition, which therefore makes the conditional right to contract nonsensical. Specifically they could argue that an option conditional upon a desire to sell cannot exist, as the intention to create an obligation is an essential prerequisite for a substantive offer.<sup>50</sup> This objection has been dealt with under par 4 11 2 dealing with the *BGB Vorkaufsrecht*. It will be recalled that German writers have correctly pointed out that the economic need to

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agrees with B that if A cannot upgrade the zoning classification of a certain property by a specific date, B will have the right to purchase the property at a specified sum for the next 30 days (*cf* Tew 1989 *Eastern Mineral Law Procedures* 7-1 7-5).

<sup>50</sup> *Cf* Van der Merwe *et al Contract* 76. See Wessels *Contract* par 1312-1321 on potestative conditions generally.

recognise contracts subject to at least partly potestative conditions ("mixed conditions"), means that a blanket objection to potestative conditions as inconsistent with a serious intention to be bound is suspect of a formalistic, *Begriffsjurisprudenz* approach.<sup>51</sup> A more functional and sensible approach is to consider the reasons for the objections to potestative conditions and to test any particular potestative condition against them before rejecting it as inconsistent with an intention to be contractually bound. Only potestative conditions which state liability to be dependent on the mere *ipse dixit* of a party are objectionable because such a contract could never be enforced by a court against that party as long as she insists that she does not want to be bound.<sup>52</sup> The condition that the grantor concludes a contract with a third party is therefore not an objectionable potestative condition.<sup>53</sup> A court could enforce it against a grantor who insists that she does not want to be bound by merely pointing to the fact that a contract with a third party has been concluded. The same applies even where the condition is an "overt act manifesting a serious desire to contract" or simply "a desire to contract." The court can point to the grantor's actions which manifests such a desire or intention. Liability depends on those actions, not on the grantor's mere *ipse dixit*. The condition is mixed rather than purely potestative, and for that reason not objectionable. Also unfounded is the more theoretical objection that the intention to be bound is of the essence of an offer so that an option conditional upon the manifestation of a desire to sell simply cannot be an offer. Any condition that is added to an option means that the grantor does not intend to be bound to contract at that point, but only once the condition is fulfilled. However, the grantor confirms that he is prepared to be bound once the condition is fulfilled. The same is true of any other conditional contract. Yet the same objection is not raised against such conditional contracts: they still bind the grantor pending fulfilment of the condition.

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<sup>51</sup> Cf *Soergel & Siebert* (Huber) Vor § 504 RdNr 10; *Münchener Kommentar* (Westermann) § 158 RdNr 60. Pound *Interpretations of Legal History* (1946) 119 speaks of a "jurisprudence of conceptions" which amounts to a mechanistic application of legal concepts.

<sup>52</sup> See also *Christie Contract* 112.

<sup>53</sup> Cf *Münchener Kommentar* (Westermann) § 158 RdNr 60.

It is true that a condition referring to the grantor's desire to contract may lead to disputes, depending on what precisely is taken to be a manifestation of a desire to contract. This issue will be dealt with more fully below.

I will now set out the two main types of preference contract under this rubric, namely those which are triggered by any manifestation of a desire to contract and those which are only triggered by a contract with or offer to a third party.

#### 5 2 2 2 1 Any manifestation of a desire to contract triggers the right

Many South African commentators and decisions do not specifically limit the trigger event to the conclusion of a contract with or an offer to a third party.<sup>54</sup> Some specifically argue that a lesser manifestation of a desire to sell should be sufficient.<sup>55</sup> So, for example, Wessels JA in *Owsianick v African Consolidated Theatres*<sup>56</sup> said that

“Desire, like intention, resides in the mind, and its existence, sometimes settled and sometimes ephemeral, is to be determined in the light of the available, relevant evidential material, such as considered, or even unguarded confessions or other conduct which points unequivocally to its existence.”<sup>57</sup>

The wording of preference arrangements is often wide enough to support such a wide understanding of the trigger event. These contracts often provide that when the grantor “desires” or “wishes” to contract, he shall first give the holder a chance to do so.

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<sup>54</sup> Kerr *The South African Law of Sale and Lease* (1996) 410; Cooper *Landlord and Tenant* 144-146; Lubbe 1982 *Annual Survey* 128 130; Floyd 1986 *THRHR* 253 267; Lotz “Purchase and Sale” in Zimmermann & Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 386; Eiselen 1986 *THRHR* 95 99; Janisch 1990 *Responsa Meridiana* 434 442-443. Cf for example *Soteriou v Retco Poyntons* 1985 2 SA 922 (A) 932H *et seq.* By contrast, Reinecke & Otto 1986 *TSAR* 18 26 state that a lesser manifestation than a valid offer to the holder should not lightly be regarded as a trigger event.

<sup>55</sup> Floyd 1986 *THRHR* 253 258-259, 264.

<sup>56</sup> *Supra.*

<sup>57</sup> 327H.

## *1 Exercise of the right: the trigger event and contract price*

The precise trigger event may be more narrowly defined than “desire to contract” but still refer to a stage before the grantor actually contracts with a third party. For example, it could be defined as a willingness, here and now, to contract with a specific third party.<sup>58</sup> Another view is that the test should be whether the grantor's action can be interpreted as “the initiation of the accomplishment of the decision to alienate.”<sup>59</sup> According to this view, any manifestation of an intention to contract shortly is not sufficient.

By contrast, if any manifestation of a desire to contract should trigger the holder's right, the commencement of negotiations with third parties, or listing a property for sale would also qualify.

Which should be the default definition of the trigger event will be considered in a later chapter after all the possible constructions have been set out in this one.

The view that the trigger event may be a lesser manifestation of a desire to sell than an offer to or contract with a third party, raises the question of the counter-performance or price against which the holder may enforce his right at such an early stage. Some South African decisions and commentators favour an implied term that the holder may contract on the terms at which the grantor is prepared to contract with a third party, apparently even in the absence of an actual third party offer.<sup>60</sup> However, until the grantor has agreed

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<sup>58</sup> This is the suggestion of Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 339.

<sup>59</sup> In the words of Larenz “Die rechtliche Bedeutung von Optionsvereinbarungen” 1955 *Der Betrieb* 210 (my translation). See also Nipperdey “Über *Vorhand, Vorkaufsrecht* und Einlösungsrecht” 1930 *Zeitblatt für Handelsrecht* 300 301.

<sup>60</sup> See *Bellairs v Hodnett* 1978 1 SA 1109 (A), cited with approval by Lubbe 1985 *Annual Survey* 137; *Hirschowitz v Moolman supra* 6D-E; *Dithaba Platinum (Pty) Ltd v Erconovaal Ltd* 1985 4 SA 615 (T) 623H; *Soteriou v Retco Poyntons supra* per Nicholas JA: “not beyond the bounds of commercial reason and practice and made for the purpose of inducing a rejection” (932I-J, quoting Corbin *On Contracts* section 261 at 477) and “fair and reasonable offer” (933D); see also at 933F.) See also Floyd 1986 *THRHR*

to contract with a third party, there is no basis to prove the terms on which he is in fact prepared to contract with a third party. This is open to speculation and likely to lead to disputes.<sup>61</sup>

Others suggest that, in the absence of a third party contract, the holder is entitled to a fair or reasonable price.<sup>62</sup> However, forcing the grantor to contract at a reasonable or fair price would be unfairly restrictive as there may be third parties which may offer a higher price, and the grantor has merely undertaken to give the holder the chance to contract at the best price she can find in the open market, before the grantor contracts with a third party at that price. The grantor therefore has a legitimate, *bona fide* interest in obtaining as high a price as possible, even higher than the reasonable or market price, as long as the holder is ultimately preferred above third parties.<sup>63</sup>

Another view would allow the grantor to make an offer in her discretion as long as it is “in good faith”<sup>64</sup> or “not beyond the bounds of commercial reason and practice and made for the purpose of inducing a rejection.”<sup>65</sup>

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253 257 and 260: “die bedinge wat die gewer van ‘n derde sou verlang as hy ‘n aanbod aan die derde sou maak....Die koopprys wat [so]... vasgestel word, is nie noodwendig gelykstaande aan die markprys nie.”

<sup>61</sup> Radesich “*Soteriou v Retco Poyntons (Pty) Ltd* 1985 2 SA 922 (A): Landlord and tenant-lease-right of first refusal” 1985 *De Jure* 407 409-410.

<sup>62</sup> As noted in the previous chapter, the Canadian writer Flannigan “The Legal Construction of Rights of First Refusal” March-June 1997 *Canadian Bar Review* 1 31-32 argues that transactions like a package deal or dissolution of the grantor company should entitle the holder to buy the object at its market value because “this price standard is implicit in the nature of a right of first refusal.” *Cf Soteriou v Retco Poyntons supra* 933D per Nicholas JA: “a fair and reasonable offer.”

<sup>63</sup> Setting a very high price may simply be due to optimism or stupidity on the part of the grantor and not to a devious attempt to shake off the holder.

<sup>64</sup> The majority in *Soteriou v Retco Poyntons (Pty) Ltd supra* 932H, 933F per Nicholas JA held that while the clause was silent as to the method of determining rental to be stated in the offer, the grantor was not free to fix any rental it pleased; it had to act *bona fide*. (On the facts, the grantor had indeed already concluded a contract with a third party, so that it was not necessary to decide what should occur upon a lesser manifestation of a desire to sell.)

<sup>65</sup> See *Soteriou v Retco Poyntons supra* 932I-J per Nicholas JA, quoting Corbin *On Contracts* § 261 at 477.

## II Remedies for breach

How may the holder enforce her right to contract upon occurrence of the trigger event? The possibilities are, firstly, by the *Oryx* mechanism,<sup>66</sup> secondly, by unilateral declaration regarded as acceptance of an offer embedded in the preference contract, which is therefore understood as a conditional option, and thirdly by an order that an offer be made.

The *Oryx* mechanism is irrelevant to the cases under discussion here. According to the *Oryx* case it only applies where the grantor had in fact already contracted with a third party, and perhaps also if he had granted an option.<sup>67</sup>

The juristic explanation of preference contracts as conditional options has the distinct advantage for the holder that she could unilaterally create the substantive contract upon the trigger event by accepting the offer embedded in the preference contract. She can therefore pray directly for specific performance of the substantive contract. This provides a more streamlined remedy than an order that an offer must be made. However, the uncertain price standard that must apply upon a lesser manifestation of a desire to sell, makes the “conditional option” explanation unsatisfactory: it is unlikely that an option to buy at a “good faith” price or “price which the grantor would accept from a third party” would be certain enough to be enforceable, in any event, where the grantor had not yet contracted with a third party. As was argued above, an implied term that the holder may buy at a reasonable price, is also not desirable. By contrast, where the parties had agreed on a price or mechanism for its determination in the preference contract, the agreement could be equated with a conditional option.<sup>68</sup>

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<sup>66</sup> See par 1 1 for a description of this remedy.

<sup>67</sup> *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd supra* 908F-G.

<sup>68</sup> As was noted before, the grantor would be taken to have tacitly intended the usual price, if one exists (*Shell SA (Pty) Ltd v Corbitt* 1986 4 SA 532 (C) 526-527; *Adcorp Spare PE (Pty) Ltd v Hydromulch* 1972 3

Sometimes parties may provide that the grantor must invite an offer by the holder and must then contract with the holder on the terms offered unless a higher third party offer exists at the time the holder's offer is made. This is how the *Annahmeverhand* of German law operates. Such a contract can also be understood as a conditional option to contract at the terms set by the holder, subject to the further resolutive condition that a higher third party offer exists. After the decisions in *NBS Boland Bank v One Berg River Drive CC*; *Deeb & Ano v ABSA Bank Ltd*; *Friedman v Standard Bank Ltd*<sup>69</sup> and *Engen Petroleum Ltd v Kommandonek (Pty) Ltd*<sup>70</sup> our courts may perhaps accept such an option contract which leaves the determination of the contract price up to the holder. This type of contract leaves the grantor more room to obtain the best possible price than the type that forces the grantor to make an offer upon the trigger event. The grantor need only inform the holder that the condition has been fulfilled and does not have to make an offer at that stage. If the holder makes no offer, the grantor is free to sell to a third party.<sup>71</sup> If the grantor has in the meantime obtained a better offer from a third party, the grantor is not bound to the holder's offer.

Insofar as the possible price standards which could apply on a lesser manifestation of a desire to sell is too vague to found an option, the preference contract can be regarded as an enforceable undertaking that an offer will be made on a manifestation of a desire to sell. This was the remedy suggested by the minority in the *Owsianick* case<sup>72</sup> and ordered by some English courts.<sup>73</sup> It allows the view that the grantor should have a discretion to make any offer he pleases.

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SA 663 (T); *Lombard v Pongola Sugar Milling Co Ltd* 1963 4 SA 119 (D); *Globe Electrical Transvaal (Pty) Ltd v Brunhuber* 1970 3 SA 99 (E); *De Wet & Van Wyk Kontraktereg* 315).

<sup>69</sup> 1999 4 SA 928 (SCA).

<sup>70</sup> 2001 3 SA 1013 (W).

<sup>71</sup> *Cf* Floyd 1986 *THRHR* 253 258 who states that Roman-Dutch law only required a notice to the holder if the grantor desired to sell (whereas, on the authority of *Soteriou v Retco Poyntons (Pty) Ltd supra*, South African law is said to require an offer).

<sup>72</sup> *Supra*.

<sup>73</sup> See *supra* par 4 2.

Of course, some limitation should be placed upon his discretion to prevent him to get rid of the holder by an unrealistically high offer that the holder would never accept. Wide parameters like “good faith” and “the bounds of commercial reason and practice and not made for the purpose of inducing a rejection” has been suggested as a check on the grantor’s freedom to make whatever offer he pleases. However, it is submitted that the best way to prevent a *mala fide* evasion of the holder’s right is to hold that the preference contract does not terminate until the grantor in fact contracts with and performs to a third party at a price which the holder had an opportunity to match.<sup>74</sup> This solution prevents the uncertainty inherent in price standards like “good faith” and “reasonableness” and sufficiently protects the holder against any *mala fide* attempt to shake off the holder by an outrageously high offer.<sup>75</sup>

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<sup>74</sup> As suggested by Henrich 363. See par 4 1 2 1 5 *supra*.

<sup>75</sup> For criticism against such vague requirements see Radesich 1985 *De Jure* 407 409-410. Floyd’s rejoinder that the market or true value could be taken into account wrongly assumes that there is always a market value for the performance in question. The established requirement that any contractual discretion must be exercised *bona fide* (*NBS Boland Bank v One Berg River Drive CC*; *Deeb & Ano v ABSA Bank Ltd*; *Friedman v Standard Bank Ltd* 1999 4 SA 928 (SCA); *Engen Petroleum Ltd v Kommandonek (Pty) Ltd* 2001 3 1013 (W)) may still be a necessary check on the grantor where the grantor proposes *incidental* in the offer to the holder which suits the third party but which the holder cannot fulfill, and in which the grantor has no actual interest. This issue will be considered in more depth in chapter 7, as will the *BGB* rule that a *Vorkaufsrecht* may still be exercised where the third party undertook a subsidiary personal performance (*Nebenleistung*) which the holder cannot fulfill, as long as a monetary value can be placed on that performance. This is a sensible rule that fairly balances both parties’ interests. It should also be added that where the preference arrangement indicates a mechanism for determining the price, the holder’s rejection of an offer to exercise her right should extinguish the preferential right even if the grantor thereafter does not contract at all or contracts with a third party at better terms. This is because the holder is entitled to an opportunity to contract at the terms agreed, and once this opportunity is given, the holder’s right should terminate.

If the grantor remains recalcitrant to make an offer, contempt proceedings could be instituted to persuade her to make an offer.<sup>76</sup> An objection that the grantor would then probably set a ridiculously high price to "spite" her litigious adversary, is trumped by the reminder that this would be unlikely if the grantor is serious about contracting at all, as the grantor cannot lawfully contract with a third party at a lower price than that offered to the holder. South African civil procedure may also benefit from the power given to courts in countries like Germany and the Netherlands to order payment of a penalty for each day that a court order remains unfulfilled.<sup>77</sup> This would be a more effective incentive for the grantor to make the offer as ordered.

### *III Possible juristic explanations of this type of preference contract*

The "conditional option" and "conditional right to an offer" constructions were already mentioned in the previous rubric. Apart from their implications for the holder's remedies, these juristic explanations may also affect the necessity of compliance with formalities prescribed for the substantive contract, such as those prescribed by the Alienation of Land Act, 68 of 1981. If the preference contract is understood as a conditional option, it must comply with such formalities, since it then encompasses a conditional offer to contract with the holder. The "exercise" of the holder's right must then also comply with all the requirements for a valid acceptance. If the preference contract is simply understood as an enforceable right to an offer, the preference contract does not strictly speaking have to comply with the formalities legislation, but only the

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<sup>76</sup> Floyd 1986 *THRHR* 253 268-269 and the authorities there cited argue persuasively that courts should not be unwilling to grant such an order on the basis that its performance is difficult to supervise or that it would lead to protracted disputes. If the holder wants such an order, it is up to her to end the uncertainty caused by the grantor's refusal to perform the order by claiming damages. See also Lambiris 129-130.

<sup>77</sup> See for example Asser-Hartkamp 4 *I Verbintenissenrecht: Die Verbintenis in het algemeen* 11<sup>th</sup> edition (2000) 581 Nr 647 iro the Dutch institution of *dwangsom* and § 888 *ZPO (Zivilprozessordnung)* regarding the German institution of *Zwangsgeld*).

offer eventually made by the grantor and the acceptance thereof. On the other hand, the purpose of the legislation may arguably be thwarted if an oral preference contract could entitle the holder to a court order that effectively forces the grantor to contract with and ultimately transfer the object to the holder.<sup>78</sup>

Another juristic explanation of pre-emption contracts has been put forward by Lambiris. He defines pre-emptive agreements as any contractual agreement in terms of which a *future* contract of sale is made subject to a suspensive condition, usually that the owner of the property will decide to sell that property.<sup>79</sup> On the one hand, he stresses that the effect of fulfilment of the condition may vary depending on the specific agreement. On the other, he apparently insists that such fulfilment has only two possible results.<sup>80</sup> Firstly, if the essential terms of the future sale have been agreed in the pre-emption agreement, a perfected sale immediately comes into existence *retroactively*.<sup>81</sup> There is

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<sup>78</sup> The “anomalous situation” which would otherwise ensue, namely that the grantee could become a purchaser on the strength of a verbal contract, was an important reason for the court’s decision in *Hirschowitz v Moolman supra* that preference contracts must comply with the formalities in the Alienation of Land Act, 68 of 1981. This view is approved by Lotz “Purchase and Sale” 386 and Van Rensburg “Formaliteitsvoorskrifte, Voorkoopregte en Opsies” 1986 *THRHR* 208 215. In the case of non-compliance with the formalities, the preference contract could still be valid, but only in the form of a bare preference which merely entitles the holder to a *non faciendi*. The court in *Hirschowitz v Moolman supra* did not have this variation in mind when it declared that all preference contracts should comply with the formalities. Although a price determination in the preference contract would indicate a conditional right to contract rather than a bare preference, a court may be prepared to enforce only the *obligatio non faciendi* and therefore treat the preference contract as a bare preference.

<sup>79</sup> Lambiris *Orders of Specific Performance and Restitutio in Integrum in South African Law* 82. Lambiris would have the conditional future sale co-exist with the pre-emptive agreement itself while the condition remains unfulfilled, because he believes that the suspended future contract cannot give rise to legally enforceable contractual obligations “until it actually comes into existence”, presumably on fulfilment of the condition. He thus states that the existence of the pre-emptive agreement as something apart from the future sale explains why the grantor has certain enforceable duties in the interim, such as to refrain from selling to a third party (84-85).

<sup>80</sup> 83 and 85. That he envisages only these two possibilities, is also clear from his discussion at 86.

<sup>81</sup> 83 and 85.

“perhaps” a further resolutive condition which enables the purchaser to avoid the sale within a certain period of time if he renounces it.<sup>82</sup> The effect of this construction is that the holder’s right as buyer is stronger than that of a third party buyer, as his contract of sale comes into existence *retrospectively* on fulfilment of the condition.

Secondly, where the essential terms of a future sale have not been agreed in the agreement of pre-emption, an option to purchase comes into being.<sup>83</sup> The effect of this construction is that the third party buyer has a stronger (prior) right to delivery than the holder whose right comes into existence only upon exercising the option.

Lambiris’s construction is problematic for a number of reasons.

Firstly, the contrived suspended sale construction is not necessary to protect the holder in the event of a sale to a third party in conflict with the holder’s rights. In *Le Roux v Odendaal*<sup>84</sup> the Natal Provincial Division decided that a prior right of pre-emption places the holder in the same position in law as a prior purchaser.<sup>85</sup> In *Krauze v Van Wyk*<sup>86</sup> the Appeal Court stated, albeit *obiter*, that a holder of a right of first refusal or option is

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<sup>82</sup> 83.

<sup>83</sup> It is not totally clear what criterion would determine whether a specific agreement of pre-emption amounts to a suspended future sale or a conditional option. In discussing his “conditional option” construction, he merely mentions a passage in *Owsianick v First Consolidated Theatres* in which Ogilvie Thompson JA merely stated there that the language of the clause must be examined to determine the contingency upon which the right of pre-emption comes into operation (316D). This is not very helpful in the quest to determine when which approach is applicable, unless he means that the clause is expected to state specifically whether a sale or option is created. The criterion that Lambiris apparently envisages in the absence of clear agreement is whether the terms of the agreement are such that the essential terms of the future sale have been agreed upon (83, 85, 86).

<sup>84</sup> 1954 4 SA 432 (N).

<sup>85</sup> 442C- 443A.

<sup>86</sup> 1986 1 SA 158 (A).

protected by the maxim *qui prior est tempore, potior est jure*, before exercising his right, just like a prior purchaser.<sup>87</sup>

Secondly, the holder does not intend to bind herself to a sale. If the holder has not signified her consent to be bound to a conditional sale, there is no justification in regarding this contract as a conditional contract of sale.<sup>88</sup> This is why this construction is so contrived.

Thirdly, it is confusing and unnecessary to say that a *future* sale exists, which is moreover suspended, but which comes into existence retroactively,<sup>89</sup> and which co-exists with the pre-emption contract.<sup>90</sup> Lambiris relies on *Corondimas v Badat*<sup>91</sup> for his statement that no contract of sale exists pending fulfilment of the condition.<sup>92</sup> However, the *Corondimas* case has been criticised by the Appellate Division in *Tucker's Land & Development Corporation (Pty) Ltd v Strydom*.<sup>93</sup> Certainly, a suspended sale binds the parties thereto in the sense that a party may not resile from the contract and the creditor (holder in the present context) may protect his rights by an interdict.<sup>94</sup> Thus it is not necessary for Lambiris to maintain that the conditional sale co-exists with a separate agreement of pre-emption. If the agreement of pre-emption could have been regarded as a conditional sale, the holder's power to obtain an interdict prohibiting the grantor from selling to a third party, would flow from the conditional sale itself. There would be no

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<sup>87</sup> 172B-E.

<sup>88</sup> The main justification for the doubly conditional sale construction of the *BGB Vorkaufsrecht*, namely that the *BGB* requires the preference contract to be in writing whereas the holder may exercise the right orally, does not apply to South African law. See further par 4 1 1 2 *supra*.

<sup>89</sup> 84.

<sup>90</sup> 84 *in fine* to 85.

<sup>91</sup> 1946 AD 548.

<sup>92</sup> 84

<sup>93</sup> 1984 1 SA 1 (A).

<sup>94</sup> Lubbe & Murray 435 n5, relying on *Fichardts Motors (Prop) Ltd v Nienaber* 1936 OPD 221 and *Odendaalsrust Municipality v New Nigel Estate Gold Mining Co Ltd* 1948 2 SA 656 (O). Lambiris apparently accepts this in n 25.

need for the agreement of pre-emption to exist in more than one guise: as conditional sale and agreement of pre-emption creating a negative duty only.

Fourthly, Lambiris's criterion for whether the agreement amounts to a conditional option or conditional sale is problematic. It is trite law that an option also requires that all the essential terms of the envisaged transaction are set out in the offer, whether it is conditional or not.<sup>95</sup> Perhaps Lambiris means that if the price is set in the agreement of pre-emption, it would amount to a conditional sale, whereas if the price is implied to be the price at which the grantor is prepared to sell, the agreement of pre-emption amounts to a conditional option. If such a term can be implied into the conditional option, why could it not be implied into the conditional sale?

#### IV *Sphere of application*

In many cases "first options" are granted after the grantor has already manifested a desire to contract.<sup>96</sup> In such a situation, it would be absurd to regard the trigger event as any manifestation of a desire to sell, which entitles the holder to contract with the grantor. If that was the intention of the parties, the grantor would have made an outright offer to the holder. In such cases, the parties must intend a more limited preferential right than a right to contract conditional upon a manifestation of a desire to sell. What the default rule or construction should be in such a case will only be considered in chapter 7 after all the possible types of preference contracts have been set out in this one.

The question also arises whether a formulation that requires the grantor to make an offer necessarily excludes the "conditional option" explanation of this type of preference

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<sup>95</sup> *Brand v Spies* 1960 4 SA 14 (E) 16-17. Cf *Hattingh v Van Rensburg supra* 582C-E. See Lubbe & Murray *Contract* (1988) 74 n 6; Joubert *General Principles of the Law of Contract* (1987) 37. In *McGregor v Jordaan* 1920 CPD 209 213 for example, the court said that if the agreement was an option and not a right of pre-emption, the exception that the term "for a price not exceeding £500" was too vague, would have been a good one.

<sup>96</sup> For example by advertising a property for sale and commencing negotiations with interested buyers.

contract. The argument would be that if an offer must still be made it indicates that there is not yet an offer embedded in a conditional option contract. To interpret such wording as creating a conditional option or conditional offer, is arguably strained.<sup>97</sup> However, the argument that a preference agreement should be construed as a conditional option in spite of a reference to a future offer is very strong when the preference contract already specifies a price. In that case, an offer by the grantor would really be superfluous. The duty to make an offer should then be interpreted rather as a duty to give notice that the condition has been fulfilled and, where the price was determinable, that it has now been determined, for example by valuation.<sup>98</sup>

Another question is whether the preference contract can be regarded as a conditional option where it does not specify a time period for which the offer is to be kept open. Most preference contracts encountered in South African case law do not specify such a time period. The effect of an “option” which does not specify a time limit is presently uncertain.<sup>99</sup> However, it is submitted that such an agreement could still be regarded as an option that tacitly obliges the grantor to keep the offer open for a reasonable time upon

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<sup>97</sup> For example, the clause in the *Oryx* case provided that the grantor shall not have the right to sell the shares, until it has first offered them for sale to the holder. The court decided that if the grantor breached the contract by contracting with a third party first, the holder may bring the substantive contract into existence by unilateral declaration. The court did not regard the preference contract as a conditional option. An attempt to explain the so-called *Oryx* mechanism as a conditional option may appear strained considering the wording of the agreement that calls for the making of an offer.

<sup>98</sup> Cf the Austrian writers who argue that notice to the holder of an intention to contract is sufficient despite the reference to an offer in their code (§ 1072 ABGB: *anbieten soll*). See for example Faistenberger C *Das Vorkaufsrecht* (1967), Welser R “Das Vorkaufsrecht. Zum Vorkauf im Österreichischen Bürgerlichen Recht. Von Christoph Faistenberger (Buchbesprechung)” 1971 *Zeitschrift für Rechtsvergleichung* 313.

<sup>99</sup> See De Wet & Van Wyk *Kontraktereg* 34-35; Van der Merwe *et al Contract* 60; Lubbe & Murray *Contract* 75; Christie *Contract* 62 n 179. In *Treadwell v Roberts* 1913 WLD 54 an option “for an indefinite period” was held to be either terminable at will or too vague to enforce as an option. In *Hanekom v Mouton* 1958 1 PH A9, it was held that an option could endure for an indefinite time.

occurrence of the trigger event.<sup>100</sup> *Wissekerke v Wissekerke*<sup>101</sup> is often quoted as authority for a statement that the grantor of a preferential right to contract is not obliged to keep an offer open, but may withdraw an offer to the holder as long as the grantor no longer wishes to contract at all.<sup>102</sup> Accordingly, it appears that preference contracts cannot be understood as options. However, the court in *Wissekerke*<sup>103</sup> was not required to decide on the revocability of offers in respect of preference contracts generally. Firstly, it was common cause that the grantor may have withdrawn the offer before acceptance thereof.<sup>104</sup> Secondly, the grantor's offer was made voluntarily. Other considerations may apply when the grantor has breached the preference contract by contracting with a third party, which could be considered as the event triggering the holder's conditional option. If the reasoning in *Wissekerke* should apply to all preference contracts that do not specify a period for their exercise, and whether or not breach has occurred,<sup>105</sup> a preference

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<sup>100</sup> This appears to be the suggestion of Van der Merwe *et al Contract* 60: "The better view is that...an option which does not specify a period for its duration or which is stated to be of unlimited duration, is not void for vagueness, although it may terminate after a reasonable time."

<sup>101</sup> *Supra*.

<sup>102</sup> Christie *Contract* 62; Reinecke & Otto 1986 *TSAR* 18 33; Floyd 1986 *THRHR* 253 259; Janisch 1990 *Responsa Meridiana* 434 444.

<sup>103</sup> *Supra*.

<sup>104</sup> 650D.

<sup>105</sup> The typical aspect of a preferential right to contract is that the grantor is totally free in the decision whether to contract. There is therefore a strong case for the correctness of *Wissekerke v Wissekerke supra* according to which the grantor who does not want to contract at all anymore after the occurrence of the trigger event, is not obliged to contract with the holder. This is also the position in England. See *Lyle & Scott v Scott's Trustees; Same v British Investment Trust Ltd* 1959 AC 763. Interestingly, Van der Keessel *Theses Selectae* 3 16 2 states that the law in Holland was initially that upon a completed sale to a third party, the owner was bound to the *ex lege naastingsreg* and that the holder's remedies remained in spite of a purported withdrawal from the sale. However, later legislation allowed a *bona fide* withdrawal from the sale before exercise of the *naastingsreg*. Floyd 1986 *THRHR* 253 258 seems to have overlooked this text by relying solely on Voet 18 3 24 (on the *ex lege naastingsreg*) for his statement that the intention to sell triggers the right even where the sale to the third party is later cancelled or even where the third party sale is subject to non-exercise of the right of pre-emption. By contrast to Roman-Dutch law, the *BGB* does not allow a withdrawal from the third party contract to influence the holder's power to exercise the *Vorkaufsrecht* (§ 506).

contract could still be regarded as an option, in the sense that it does limit the grantor's capacity to withdraw the offer. The offer that becomes operative upon fulfilment of the condition may not be withdrawn in order to contract with another, as in the case of an ordinary offer. It may only be withdrawn where the grantor no longer wishes to contract at all.

Interestingly, Christie says that an option that does not specify a time limit, is open for acceptance or rejection for a reasonable time, but may be withdrawn at any time before acceptance unless the contract forbids the grantor to do so.<sup>106</sup> If this is correct, a preferential right to contract which does not specify a period for exercise thereof would indeed be equal to an option which does not specify a time limit. However, Christie's statement on options is based on *Wissekerke* itself, and is therefore not supported by authority in respect of options generally.<sup>107</sup> Such a preference contract could instead be described as a *sui generis* conditional option, which deviates from normal conditional options in this respect.

Alternatively, its revocability could be considered as fatal to its status as a conditional option. In such a case, it could be understood as a conditional offer coupled with an *obligatio non contrahendo cum tertii*. Like any offer it would lapse if not accepted within a reasonable time after fulfilment of the condition. Although the offer may be withdrawn before acceptance by the holder, the preference contract, including the *obligatio non contrahendo cum tertii*, continues to exist. Accordingly, if the condition is fulfilled again, the offer becomes operative once more.

Whether *Wissekerke* should apply to all preference contracts and which judicial explanation should be chosen as the default construction under which circumstances will be considered finally in chapter 7.

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<sup>106</sup> Christie *Contract* 62 n 179.

<sup>107</sup> *Ibid.* As stated before, both parties accepted that the offer could be withdrawn before acceptance and the court therefore did not decide this point. Moreover, the court did not typify the offer made as an option.

5 2 2 2 2      Only an undertaking to contract with a third party triggers right

There is also authority that the only event which should trigger the holder's right to contract, should be an offer to or contract with a third party, and not a lesser manifestation of a desire to sell.<sup>108</sup> This is therefore certainly an alternative possible construction or type of preference contract.

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<sup>108</sup> Reinecke & Otto 1986 *TSAR* 18 26-27 explicitly state that any lesser manifestation of a desire to sell should not easily be held to trigger a right of pre-emption as this would be unfair to the grantor and contrary to the spirit of a right of pre-emption. *Cf* also the *Oryx* case *supra* at 908E where the court left open the question whether only the conclusion of the contract with a third party would entitle the holder to the *Oryx* mechanism, "and not also, for example, if the seller made an offer to a third party" (my translation). In the *Oryx* case the court only stated that the relevant contract of December 1973 provided that the grantor was not entitled to sell or alienate the shares and claims to a third party until he had first offered it to the holder at the same price and terms on which he was prepared to sell to a third party. As this wording does not speak of a duty to offer upon a manifestation to sell, and only prohibits the sale or alienation to a third party, the wording of the clause itself supports an interpretation that any duty to make an offer would arise only immediately before such a sale or alienation. In *Skinner v Goldberg* 1943 WLD 42 *supra* the court also decided that the date for calculating the damages is the date of conclusion of the contract with the third party (44). The implication could be that breach only occurred at that point and that up to that point the grantor need not have made an offer. In *Ah Ling v Community Development Board & Others* 1972 4 SA 35 (E) 39G, the court interpreted "a desire to dispose of the property" in the context of a statutory right of pre-emption as "an unqualified and sustained desire on the part of the owner [grantor] resulting in a sale to the [holder]." The statutory provision in question was art 15(5)(a) of the Community Development Act 3 of 1966, which provided as follows: "Any owner of immovable property in an area in respect of which any notice under sub-sec (2)(e) is in operation, who desires to dispose of such property shall offer such property for sale to the Board and the Board shall thereupon have a preferent right to purchase such property at a price agreed upon between it and the owner concerned, or (if within 60 days after the date on which the offer was made the Board and such owner fail to agree as to the price to be paid) at a price fixed by arbitration..." This case was not concerned, however, with the situation where the grantor has shown a desire to contract with a third party, but rather revolved around the question whether the grantor has shown a sufficient desire to contract with the holder by writing to the holder that it intends to contract, but only at certain specific prices, which the holder did not accept, insisting instead to have the price fixed by arbitration. However, the same reasoning arguably applies in both contexts.

The advantages of this construction over the previous one is that there can be no uncertainty about either the occurrence of the trigger event or the price on which the holder may contract upon the trigger event. It is either the price determined by the preference contract itself, or the price offered to or agreed with the third party. Moreover, the grantor is left free to negotiate with third parties in order to obtain as high a price as possible where the preference contract does not stipulate a price.

There are two main types of preference contracts under this category. First, preference contracts which allows the grantor to contract with a third party first, and second, preference contracts prohibiting this.

#### *I* No obligatio non contrahendo cum tertii

This is the type of preference contract known to German law as the *Vorkaufsvertrag*, and for brevity's sake I will use the term *Vorkaufsrecht* to refer to the preferential right to contract that it creates.<sup>109</sup> This type of preference contract was discussed in depth in paragraph 4 1 1. In short, one distinctive characteristic of the *Vorkaufsrecht* is that it can only be exercised upon a completed valid contract with a third party. However, the grantor is not obliged to refrain from contracting with a third party until she has first offered to contract with the holder. Contracting with a third party without first having given the holder the opportunity to do so is not a breach of a *Vorkaufsrecht*. Instead, it is a neutral trigger event or condition for the holder's right to become operative. Any agreement worded to the effect that there is a duty to refrain from selling to a third party

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<sup>109</sup> Such contracts are also encountered in other jurisdictions. See for example the discussion of the English case of *Birmingham Canal Co v Cartwright* 1879 11 Ch D 421 and the American decision of *Brenner v Duncan* 1947 318 Mich 127 1 27 2d 320 in paras 4 2 and 4 3 *supra* respectively. The term "right of first refusal" may be too narrow to encompass these rights. "First refusal" implies that the holder will have the first opportunity to contract, and not that the grantor may first contract with a third party.

unless the holder has first been given a chance to contract, therefore excludes the *Vorkaufsrecht*.<sup>110</sup>

This type of contract is clearly intended when the preference contract provides that the holder should have a chance to contract on the terms *agreed* with a third party. It could be understood as a conditional option. As the agreement with the third party fixes the terms of the offer to the holder, it is not necessary to require an explicit predetermination of the terms of the substantive contract in the preference contract. They are certain enough when the holder may accept the offer. The situation is analogous to a conditional option providing for a third party to fix the price upon fulfilment of the condition.

## // *An obligatio non contrahendo cum tertii*

What is the juristic explanation of this type of preference contract? I will consider three possible explanations. The first is that the *obligatio non contrahendo cum tertii* is coupled with an option conditional upon breach thereof (that is, in the form of agreement to contract with a third party). This means that breach entitles the holder to create the substantive contract by accepting the offer embedded in the option contract. Conclusion of a contract with a third party is not just a neutral condition which triggers the option, but is typified as breach due to the normal understanding and formulation of preference clauses in South African law as prohibiting the grantor from contracting with a third party unless the holder has first been given the opportunity to contract. The terms of the offer reinforced by the option are sufficiently certain – it is the price actually agreed with or offered to a third party.

The second explanation is the existence of a duty to make an offer immediately before the grantor agrees to contract with a third party. This point in time can only be established *ex post facto*, after the conclusion of the contract or the making of the offer.

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<sup>110</sup> See the authorities cited in paragraph 4 1 1 *supra*.

Therefore the grantor is only in breach upon contracting with or making an offer to the third party and can only be forced to make an offer at that point.

A third alternative explanation is that the preference contract remains a bare preference, and therefore a negative obligation, but upon breach the holder has a contractual power to create the substantive contract by unilateral declaration. Alternatively, the preference contract could be understood as entailing a duty to make an offer before the grantor contracts with a third party, but coupled with such a contractual power upon breach of that duty. Breach occurs only where the grantor has concluded a contract with or made a valid offer to a third party. The holder's power is implied into the preference contract on the basis of policy considerations. In German legal terminology, the holder has a *Gestaltungsrecht*.<sup>111</sup>

These three juristic explanations will be discussed in more depth in chapter 7 when I finally make a proposal on how our courts should approach preference contracts.

### **5 3 Conclusion**

There are two main types of preference contracts. The first creates only a bare preference or negative obligation, whereas the second creates a conditional right to contract. Each type can be understood in a number of different ways, so that sub-types exist.

The grantor of a totally negative or bare preference contract only has an obligation not to contract with a third party. He may not be forced to make an offer to the holder simply because there is never an obligation to contract with the holder. This negative obligation continues until the grantor has actually concluded and performed a contract with a third

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<sup>111</sup> As indicated above (par 4 1 1 2 *supra*) South African law knows the concept of contractual powers to unilaterally terminate or amend the contents of a contract or to bring a new contract into existence, which is the meaning of *Gestaltungsrecht* in German law.

party on terms that the holder was given an opportunity to match. As such it can be described as a negative obligation subject to a resolutive condition. A variation on the totally negative preference contract would be to allow the holder a contractual power to unilaterally create the substantive contract on breach, on the basis of policy reasons or express agreement by the parties, and not because the grantor is regarded as having a duty to contract with the holder. However, as this sub-type of contract ultimately grants a right to contract with the holder, it belongs more properly under the second main category.

Mostly, preference contracts in South Africa are worded so as to prohibit the grantor from contracting with a third party before the holder has been given a chance to do so. However, preference arrangements may be drafted to allow conclusion of a contract with a third party as a neutral and necessary precondition or trigger event for the holder's exercise of the right to contract. This is the construction of the *BGB Vorkaufsrecht*. In this case, the holder has a right to contract, which she can enforce only after the grantor had already concluded a contract with a third party.

In cases where the wording does import an *obligatio non contrahendo cum tertii*, preference contracts creating a conditional right to contract could be triggered at various points in time. The trigger event could be:

1. any manifestation of a desire to contract (such as listing a property for sale or negotiating with third parties); or
2. at least a manifestation of a serious desire to contract shortly with a specific third party (which would include serious negotiations with that third party); or
3. at least the existence of a third party offer plus a manifestation of a desire to contract with that third party which may come short of an undertaking to contract.
4. only an undertaking to contract with a third party (it would be sensible to include not only the conclusion of a contract under this trigger event, but also an offer by the grantor to contract with a third party as they amount to the same thing.)

There are also a number of possible juristic explanations of the conditional right to contract, which may impact on certain practical aspects thereof, such as the holder's remedies upon breach. Preference contracts that create a conditional right to contract could be understood, firstly, as conditional options. However, this explanation is problematic when the trigger event is a lesser manifestation of a desire to sell than a concluded contract as the terms on which the option may be exercised is uncertain in such a case. One variation on the conditional option construction is that the preference contract constitutes a conditional option to buy at a price offered by the holder, unless a better third party offer exists at that stage. Secondly, preference contracts creating conditional rights to contract could be understood as enforceable conditional rights to an offer. They could also be understood as *obligationes non contrahendo cum tertii* coupled with a power to unilaterally create the substantive contract on breach thereof. Lambiris' construction, namely of a suspended future contract of sale, is not a persuasive juristic explanation.

Where it is decided that only an agreement to contract with a third party should allow the holder to exercise the right to contract, whereas the grantor has an *obligatio non contrahendo cum tertii*, the preference contract could only be understood as a conditional option contract on the following basis. The basic obligation of the grantor would be an *obligatio non contrahendo cum tertii* subject to a resolutive condition that the holder has failed to match the terms offered by the third party with whom the grantor has subsequently contracted. The grantor is only in breach of her obligation when she contracts with a third party. This basic obligation is then supplemented by an option conditional upon breach.

If the preference contract is instead regarded as a conditional right to an offer, the grantor only has a duty to make an offer to the holder the moment before the grantor contracts with a third party. This explains why the holder would only be entitled to enforce the right to contract once the grantor has agreed to contract with a third party.

If the preference contract is understood as a conditional option, the holder's remedies are straightforward and effective. By contrast, if it is understood as a conditional right to make an offer, it can be enforced in a number of different ways. They will all, however, eventually entitle the holder to performance of the substantive contract. The court could enforce the preference contract:

1. by an order that an offer be made. This means that the holder must approach the court again if the grantor refuses to make the offer or fails to perform upon acceptance of his offer.
2. by an order that an officer of the court makes the offer or acceptance on behalf of the grantor, after which the holder must first accept the offer before an order for specific performance of the substantive contract may be prayed for.
3. by an order for specific performance of the substantive contract. This could be explained, firstly, by procedural rules, for example a rule that allows simultaneous orders that an offer be made and the substantive contract be performed or a deliberate bypass of an order that an offer be made. There is some authority for such an approach in South African law and overseas jurisdictions. Alternatively, it could be explained by recognising a contractual power to unilaterally create the substantive contract upon breach of the duty to make an offer.

Accordingly, preference contracts could also be grouped as follows according to the point at which the holder can force the grantor to conclude or perform the substantive contract. This point could be:

1. never, in terms of the totally negative or bare preference contract. Only the usual remedies for breach of a negative obligation are then available.

2. upon conclusion of a contract between the grantor and a third party. Logically, any undertaking to contract with a third party, including an offer to the third party, should also trigger the holder's remedy. This category includes both the *Vorkaufsrecht*, which contains no *obligatio non contrahendo cum tertii*, and preference contracts which contain such a negative obligation. The *Vorkaufsrecht* could be juridically explained as an option conditional upon conclusion of a third party contract, or as a *sui generis* (preference) contract which grants the holder a contractual power to create the substantive contract by unilateral declaration at that point. As noted before, preference contracts with an *obligatio non contrahendo cum tertii* could be juridically explained either as an option conditional upon breach of the negative obligation in the form of conclusion of a third party contract only, or as a duty to make an offer immediately before the grantor contracts with a third party, or as a negative obligation coupled with a contractual power to unilaterally create the substantive contract upon breach.
  
3. upon an overt act manifesting a serious intention to contract with a specific third party, which is not to be equated with any manifestation of a desire to contract. Preference contracts in this category could be understood as conditional options, where the price must however be ascertainable and where it would be unacceptable to accept simply that the holder would have an option to contract at a price which the grantor would be prepared to accept from a third party, since this is too vague and disputable in the absence of an actual undertaking by the grantor to contract with a third party. The preference contract could also be construed as a conditional right to an offer or as a conditional right to an acceptance of the holder's offer if that is the highest offer available. In the case of the conditional right to an offer there is probably no justification or need to require that the offer be "reasonable" or *bona fide* as far as its price component is concerned. The holder is sufficiently protected against a grantor who attempts to escape the preference contract by submitting a ridiculously high price by the rule that the preference

contract does not terminate before the grantor has contracted with and performed to a third party whose offer the holder had an opportunity to match.

4. upon any manifestation of a desire to sell. Once again the preference contract could be construed as a conditional option where the price is ascertainable. It could also be regarded as a conditional right to an offer.

In choosing a default type and delineating the default field of application of each construction, it will be important to decide at which point, if any, the holder should be able to force to grantor to perform the substantive contract. This issue will be considered in chapter 7.

It remains to comment on the relationship between options and preference contracts. It is clear that the second main type of preference contract, which grants a conditional right to contract, can often be understood as a conditional option (or at least as a conditional option subject to a resolutive condition that the grantor does not want to contract at all anymore). The traditional distinction between options and rights of first refusal can only be maintained in respect of some types of preference contracts, namely negative or bare preference contracts which only give rise to remedies aimed at restoring the *status quo ante* the breach, and those preference contracts creating conditional rights to contract which courts refuse to treat as conditional options because their wording points to a duty to make or accept an offer, or because the requirement of certainty precludes them from being options.<sup>112</sup>

If the term *pactum de contrahendo* is understood as an agreement to conclude a contract in future, or if it necessarily implies the existence of the substantive offer to contract in

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<sup>112</sup> Cf Lubbe 1985 *Annual Survey* 137. Although the contract price was tacitly fixed in the preference contract in *Shell SA (Pty) Ltd v Corbitt & Another* 1986 4 SA 523 (C), so that it is tempting to describe it as a conditional option to sell, the quantity of gas to be supplied from time to time was not specified. Therefore the agreement does not contain a completed offer that is required for an option contract (Lubbe 1986 *Annual Survey* 143).

future,<sup>113</sup> not all preference contracts fall under that concept. Bare preference contracts could only constitute a *pactum de contrahendo* if the latter term is defined widely as any agreement which may lead to the conclusion of a further contract.<sup>114</sup>

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<sup>113</sup> As Reinecke & Otto 1986 *TSAR* 18 33 states.

<sup>114</sup> Cf Lotz "Purchase and Sale" 357.

## **6 Methodological considerations in constructing existing and new types of specific contracts**

The previous chapter has demonstrated the very different ways in which contracts of pre-emption may be understood in the absence of clear regulation by the parties.

The common denominator in preference contracts is a negative duty to refrain from either negotiating or contracting with or performing to a third party until the holder has rejected an opportunity to either negotiate or equal the terms on which the grantor has contracted or intends to contract with the third party. To this common denominator could be added an enforceable duty to negotiate, contract with or perform to the holder.

South African case law and legal literature reveal a number of different views on the precise construction or legal nature of preference contracts. Adoption of a specific construction is in most cases not based on the interpretation of the arrangement under consideration, but rather on the view that there is one “correct” construction prescribed by precedent and historical authority, which should apply unless otherwise agreed. The study so far has demonstrated that there is not a single correct understanding of the basic rights and duties which parties may intend. Precedent and historical authority do not clearly and convincingly support only one construction. All the conflicting constructions identified here make economic sense and may very well be intended by parties to preference arrangements. As such, they can all be regarded as different types of preference contracts, reflecting very different contractual purposes. In fact, policy considerations can be garnered in favour of more than one type as the most suitable default construction for unclear transactions.

What, therefore, must courts do when the wording of a preference contract is wide enough to encompass more than one type? This would certainly be the situation where the contract grants a “right of pre-emption” or “first option.” In such a case the basic contractual purpose and consequences intended are open to conflicting

interpretations, so that classification of the transaction is difficult. Obviously courts will be loath to declare the contract invalid for uncertainty as the parties clearly intended to be bound and it would be unfair to allow one of them to escape from the bargain.<sup>1</sup> How must the court choose between the different possible understandings of the contractual end, and thus, the basic rights and duties of the parties? On what basis can the court supplement the contract to provide for situations not expressly provided for?

The variability of contractual purpose also raises the following question: when is a recurring contractual purpose worthy of recognition as a separate type of contract with special default legal consequences, and what are the prerequisites for the classificatory criteria of such a contract type? The methodological questions posed by preference agreements are therefore more basic than and go beyond the more familiar question on the determinants of default legal rules governing the consequences of a specific contract type. This latter question presupposes that the specific contract type in question is already recognised as a separate type and that there are sufficiently clear criteria for the classification of transactions into that contract type. For example, considering that a particular agreement can be classified as a contract of lease, the question familiar to lawyers is what the default legal consequences of a lease contract should be, and on what basis one default rule is chosen above another.

In the terminology of the *essentialia – naturalia – incidentalialia* model traditionally used to formulate default legal rules for a specific type of contract, the present difficulty with preference contracts is that neither the *essentialia* nor the *naturalia* of the different types of preference contracts are clear. This raises the more fundamental question whether the types of preference contract identified in the previous chapter can be cast into the “*essentialia – naturalia – incidentalialia*” model, where the *essentialia* are supposedly clear and definite preconditions for the application of the *naturalia*, which together form the body of rules on a specific

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<sup>1</sup> See, for example, *Soteriou v Retco Poyntons (Pty) Ltd* 1985 2 SA 922 (A) 931G-H; *Genac Properties JHB (Pty) Ltd v NBC Administrators CC* 1992 1 566 (A) 579G; *Burroughs Machines Ltd v Chenille Corporation of SA (Pty) Ltd* 1964 1 SA 669 (W) 670.

contract type. In other words, is it possible to formulate clear and definite characteristics or preconditions (*essentialia*) for each type of preference contract? If not, does this prevent a particular construction from being regarded as a separate sub-type? If not, how does a court choose which type applies? Do we need a default type or types of preference contract which should apply when the contract wording is unclear? If yes, what considerations should guide the process if deciding which type or types should be the default type or types?

Clearly, the construction of existing or new types of specific contracts raises methodological concerns, which will be considered in this chapter. After establishing some working definitions (6.1 below), the function and determinants of contract law rules on the identification and consequences of specific types of contract will be considered in general (6.2 below). Next, the preconditions of recognising a recurring type of transaction as a specially regulated contract type or sub-type will be considered (6.3 below). This enquiry will centre on the adequacy of the traditional *essentialia – naturalia – incidentalialia* model to fulfil the purposes of specific contract law, as well as a possible alternative to this model. Thereafter I will discuss the interrelationship between the various conceptual tools used to regulate the consequences of contracts, namely the rules on interpretation and implication of terms, including the different kinds of residual rules or *ex lege* terms (6.4 below). The insights gained will finally be applied to preference contracts (6.5 below).

## 6.1 Terminology

I use the terms “contract type”, “specific contract type” or “type of specific contract” to refer to a category of contracts<sup>2</sup> with a recurring, typical contractual purpose or recurring, typical “interest constellations”,<sup>3</sup> for which the law traditionally formulates reserve rules that apply absent regulation by the parties.<sup>4</sup> An obvious example is the

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<sup>2</sup> As contracts they are enforceable agreements complying with the validity requirements set by general contract law rules.

<sup>3</sup> Martinek *Moderne Vertragstypen Band I: Leasing und Factoring* (1991) 2.

<sup>4</sup> Nereus Joubert *Die Finansiële Huurkontrak* (1991) 62 defines contract types as having an own typical identity in legal traffic. Elsewhere he defines them as contracts which have already obtained a certain

contract of sale where the recurring contractual purpose or the major result intended by the parties, is the permanent transfer of undisturbed possession of an object, and eventually all the transferor's rights therein to another against payment of a sum of money. Because this type of contract occurs recurrently and parties often make no detailed provision for the various circumstances which may arise and lead to disputes after conclusion thereof, a body of residual rules has developed to regulate the consequences of such contracts. These rules take their cue from the purpose or main consequence intended by the parties to some extent. How these rules are and should be arrived at exactly will be considered below.

Differentiation within some specific contract types are also recognised. As a result of this differentiation, sub-types can be identified, although the variation mostly concerns only one or two residual rules amongst the many attached to such contracts. These variations find their authority or source either in common law or in statute. In the case of sales contracts, they may relate to the identity of the seller, as in the case of sales by manufacturers and certain traders which are treated differently to sales by normal sellers.<sup>5</sup> They may also result from the identity of the buyer. The Credit Agreements Act 75 of 1980 creates the subtype of credit sales of certain consumer goods in order to protect consumer buyers. Variations may also be precipitated by the nature of the object sold. There are different rules relating to the sale of movables or immovables, for example. The counter-performance for transfer of undisturbed possession of the object may also lead to differentiation. For example, there is a difference between the rules for cash sales and credit sales.

As stated in the first chapter, I use the verb “construct” to refer to the formulation of rules surrounding a specific contract type. It encompasses the abstract process of incorporating a specific contract type, identified in practice, into the legal system,

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recurring content in legal practice (“Regsonwikkeling by nuwe verkeerstipiese kontrakte” 1992 *TSAR* 213).

<sup>5</sup> See, for example, *Holmdene Brickworks v Roberts Construction* 1977 3 SA 670 (A); *Kroonstad Westelike Boere Ko-operatiewe Vereniging Bpk v Botha* 1964 3 SA 561 (A); *Langeberg Voedsel Bpk v Sarculum Boerderye Bpk* 1996 2 SA 656 (A).

which enables comparisons with other provisions.<sup>6</sup> A category of contracts is therefore described and coherent rules developed for it, which category is then added to the pantheon of separately regulated specific contract types. The “construction” of a specific contract type refers not only to reserve rules or legal incidents regulating the consequences of the contract,<sup>7</sup> but also to the criteria for classifying a transaction as belonging to the contract type in question. It therefore also encompasses rules on the main rights and duties of the parties which may be classed together with the consequences of the contract, but which may also constitute the criteria for application of the other reserve rules.

The term “residual rules” is used to refer to the reserve rules already mentioned.<sup>8</sup> A “residual rule” can be defined as a rule deliberately formulated with a particular, recurring kind of situation in mind, provided only that it is not inconsistent with the parties’ contract.<sup>9</sup> They can also be defined as “contractual provisions which the law provides and imposes in the absence of express or implied [tacit] agreement of the parties.”<sup>10</sup> However, I occasionally also use the terms “legal incident”, “*ex lege* term” and “term implied by law” in the same sense. These terms arguably connote a wider class of terms, referring also to terms implied by law that will not necessarily function

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<sup>6</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 268. The definition of “construct” as verb in the *Concise Oxford Dictionary* reads as follows: “fit together, frame, build (lit. or fig.); (Gram.) combine (words) syntactically; draw, delineate, esp. according to given conditions...”. As a noun it is defined as “thing constructed, esp. by the mind....”

<sup>7</sup> These terms are defined *infra* under this same rubric.

<sup>8</sup> Kerr is a great champion of this terminology. See, for example *The Principles of the Law of Contract* 5 ed (1998) 335; “The need to use words with different meanings to describe different categories of provisions of contracts” 1999 *SALJ* 711; “Dangers in the use of synonyms to describe different categories of contractual terms” 1994 *THRHR* 279; “Some problems concerning implied (tacit) provisions of contracts” 1993 *THRHR* 114 and other articles cited in Kerr *The Principles of the Law of Contract* 5<sup>th</sup> edition (1998) 316, 318.

<sup>9</sup> Vorster *Implied Terms in the Law of Contract in England and South Africa* unpublished PhD thesis, St John’s College, Cambridge (1987) 72; Vorster “The resolution of contractual disputes: interpretation *versus* the recognition of novel *naturalia*” 1987 *THRHR* 450 452.

<sup>10</sup> Kerr *Contract* 344.

as “residual terms” due to the rather unique circumstances necessitating implication of the term,<sup>11</sup> as in the case of innominate contracts.

I will use the term “general residual rules” when referring to the residual rules on the consequences of contracts generally. These are the rules that apply *prima facie* to all types of contracts, such as the general rules on the remedies for breach of contract.

“*Naturalia*” is used in its well-known sense as the residual rules particular to a specific type of contract, the supposed “natural” consequences of entering into a contract of that type.<sup>12</sup>

“Tacit terms” is used to refer to provisions based on unexpressed consensus (or reasonable reliance thereof).<sup>13</sup>

## **6 2 The function and determinants of residual rules of contract law**

Contract law has two main functions. First, contract law lays down prerequisites for the formation and validity of the legal institution it regulates, namely contracts. These could be called the constitutive rules.<sup>14</sup> These rules may cause a supposed contract to be wholly or partially unenforceable.<sup>15</sup> Second, it comprises rules on the consequences attached to valid contracts (consequential rules). These rules apply

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<sup>11</sup> “Legal incidents” is the term preferred by Vorster (see the previous two footnotes) who also proposes such a wide sphere of operation for *ex lege* terms, as will appear hereunder.

<sup>12</sup> See for example Van Jaarsveld (editor) *Suid-Afrikaanse Handelsreg Vol I* 3<sup>rd</sup> edition (1988) 22.

<sup>13</sup> As “implied term” and “the implication of terms” is often used with reference to both residual rules and tacit terms, I prefer not to use it in respect of only one of these categories (contrary to what Kerr *Contract* 316 *et seq* suggests).

<sup>14</sup> See Van der Merwe “*Judicis est ius dicere, non dare*: Judicial law-making by institutional development of the common law” in Van Wyk & Van Oosten (eds) *Nihil Obstat: Feesbundel vir WJ Hosten/Essays in honour of WJ Hosten* (1996) 225 233.

<sup>15</sup> Contract law rules may cause some contractual terms to be unenforceable, for example, because they are unlawful, but severable from the rest of the contract, and therefore regarded as *pro non scripto*.

where the contract is unclear or ambiguous on its consequences, or where certain circumstances were not expressly provided for in the agreement.

The consequential rules exist because, once it appears that parties intend a binding transaction, courts are loath to refuse to enforce the bargain simply because every possible circumstance or dispute which may arise have not been provided for, or because the express terms may be ambiguous. It would be patently unfair to allow a party to escape from the contract simply because the parties did not clearly provide for all possible eventualities. If such a dispute arises, the law must therefore provide a solution. The parties expect the law to supplement their agreement where necessary to provide for circumstances that their contract does not clearly regulate. The beneficial effect of the law's willingness to do so, is to "reduce the complexity and the cost of transactions by supplying a set of normal terms that, in the absence of a law of contract, the parties would have to negotiate expressly."<sup>16</sup>

The consequential rules of contract law encompass the rules on interpretation of contracts, as well as the residual rules on the rights and duties of the parties, including the remedies for breach of their rights, the transferability of their rights, and termination of the contractual relationship. The rules on termination of contracts can be classed on their own as the terminative rules of contract law.<sup>17</sup> The interrelationship between the rules on interpretation and the residual rules, as well as the different categories of residual rules recognised in South African law, will be discussed in more depth below. Under the present rubric, I will concentrate on the general function and determinants of the consequential rules.

It is generally accepted that the first category of rules (the constitutive rules) are co-determined by policy considerations which do not only take the parties' interests into account, but also the function of the legal system and the interests and values of society as a whole. The requirement of legality most clearly demonstrates the regulatory role of contract law. In this respect contract law goes beyond establishing and giving effect to contracting parties' (likely) intention. As the courts are

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<sup>16</sup> Posner *Economic Analysis of Law* 2<sup>nd</sup> edition (1977) 69.

<sup>17</sup> Van der Merwe "*Judicis est ius dicere*" 233.

instruments of the state and the state must and may protect certain values, most notably those protected in the Constitution,<sup>18</sup> the courts will not enforce bargains which conflict with these values.<sup>19</sup>

In this study, that first category of contract law rules are left out of consideration as it is presumed that preference contracts comply with the validity requirements for contracts generally.<sup>20</sup> Therefore only the consequential rules will be considered, and any further remarks under the present rubric pertain only to that category.<sup>21</sup>

## 6 2 1 Two broad ideals: fairness and legal certainty

In broad terms, the consequential rules on contracts strive for approximation of two supreme ideals, namely fairness or justice and legal certainty.

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<sup>18</sup> The Constitution of the Republic of South Africa, 108 of 1996.

<sup>19</sup> Lubbe & Murray *Farlam & Hathaway Contract: Cases, Materials and Commentary* 3<sup>rd</sup> edition (1988) 238-239; Van der Merwe *et al Contract: General Principles* (1993) 140 *et seq*; Kerr *Contract* 179, 202 *et seq*; Christie *The Law of Contract in South Africa* 4<sup>th</sup> edition (2001) 172, 398 *et seq*. *Cf Magna Alloys and Research (SA) (Pty) Ltd v Ellis* 1984 4 SA 874 (A); *Sasfin v Beukes* 1989 1 SA 1 (A).

<sup>20</sup> Preferential rights to contract in fixed term employment contracts may conceivably be challenged as unlawful restrictions on freedom of trade. The employee (for example, a sportsman) could assert that his fundamental right to engage in work of his own choice is not sufficiently protected by the provision that he can only be forced to remain in employment if the employer matches a third party offer. He could maintain that monetary compensation is not the only benefit obtained from work, but that a good relationship with his employer and colleagues is also important, so that where these relationships have deteriorated, the employee should be allowed to find other employment, even where the employer can match the monetary terms offered. *Cf* the unpublished decision by Swart J of the Transvaal Provincial Division in *Golden Lions Rugby Union v Venter & Others* case no 2007/2000 dated 11 February 2000, in which an argument was rejected that a right of first refusal in respect of a rugby player's services was an unreasonable and unenforceable restraint of trade. See also the discussion of this case by Loubser "Sport and competition law" in Basson & Loubser (eds) *Sport and the Law in South Africa* Service Issue 2 (August 2001) Ch 8-39 *et seq* and Prinsloo "Enkele opmerkings oor spelerskontrakte in professionele spansport" 2000 *TSAR* 229 235 *et seq*. A full consideration of this issue is beyond the scope of this study.

<sup>21</sup> This study is also not concerned with mandatory consequential rules.

That law has something to do with justice and that judges must aim to find just solutions to disputes should be axiomatic.<sup>22</sup> The Constitutional mandate to “develop the common law, taking into account the interests of justice” clearly adopts this truism for our legal system.<sup>23</sup> It is also widely accepted in our case law and legal literature that residual rules aim for the fairest and most reasonable solution for each case or dispute that the parties had failed to regulate.<sup>24</sup> The aims of “justice, fairness and reasonableness” will be considered further below. At this stage I will concentrate on the relationship between justice or fairness and legal certainty in broad terms.

Justice calls for flexibility in the law. The precise circumstances of a particular dispute may not have been allowed for when the existing residual rule was formulated. Even though the existing rule was stated wide enough to encompass that situation, its application may come to be regarded as unfair. The resultant unfairness of applying the existing rule might result from its failure to take into account existing needs, practices and notions of fairness in legal reality, or because new needs and practices have evolved in the increasingly complex business world, which the rule did not take into account. In such a case, the rule must be qualified or changed in order to arrive at a just solution.<sup>25</sup> This need for change or flexibility is denied or resisted by some judges, but most realise that judges inevitably change the law, thereby

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<sup>22</sup> Neels “Regsekerheid en die korrigerende werking van redelikheid en billikheid (deel 1)” 1998 *TSAR* 702 and “Regsekerheid en die korrigerende werking van redelikheid en billikheid (deel 2)” 1999 *TSAR* 256 261 and the numerous Roman, Roman-Dutch and South African authorities there cited; Larenz *Methodenlehre der Rechtswissenschaft* 2<sup>nd</sup> edition (1975) 12, 121; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) II 3<sup>rd</sup> edition (1995) 168. Cf Dworkin *A Matter of Principle* (1985) 90.

<sup>23</sup> Section 173.

<sup>24</sup> See, *inter alia*, *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration* 1974 3 SA 506 (A) 532G-H; *Tuckers Land and Development Corporation (Pty) Ltd v Hovis* 1980 1 SA 645 (A) 651-2; *A Becker & Co (Pty) Ltd v Becker* 1981 3 SA 406 (A) 420G-H; *Ex Parte Sapan Trading (Pty) Ltd* 1995 1 SA 218 (W) 226H *et seq*; Vorster *Implied Terms* 78-79, 81-83, 85, 150-9; Kerr *Contract* 348; Van der Merwe *et al Contract* 201; Lubbe & Murray *Contract* 423; Neels “Die aanvullende en beperkende werking van redelikheid en billikheid in die kontraktereg” 1999 *TSAR* 684 697; Cockrell “Substance and form in the South African law of contract” 1992 *SALJ* 40 53; Joubert 1992 *TSAR* 213; cf Joubert *General Principles of the Law of Contract* (1987) 69; Smits *Het vertrouwensbeginsel en de contractuele gebondenheid* (1995) 23.

<sup>25</sup> Vorster *Implied Terms* 147; Joubert 1992 *TSAR* 213 214 *et seq*.

creating law. The oft-quoted *dicta* of Sir James Rose Innes in *Blower v Van Noorden*<sup>26</sup> and Lord Tomlin in *Pearl Assurance Co v Union Government*<sup>27</sup> immediately springs to mind. Rose-Innes CJ stated that:

“There come times in the growth of every living system of law when old practice and ancient formulae must be modified in order to keep in touch with the expansion of legal ideas, and to keep pace with the requirements of changing conditions. And it is for the courts to decide when the modifications, which time has proved to be desirable, are of a nature to be effected by judicial decision, and when they are so important or so radical that they should be left to the Legislature.”<sup>28</sup>

To that, Lord Tomlin added that our Roman-Dutch common law “is a virile, living system of law, ever seeking, as every such system must, to adapt itself consistently

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<sup>26</sup> 1909 TS 890 905.

<sup>27</sup> 1934 AD 560 563.

<sup>28</sup> This suggests the argument that judicial modification of the law serves the public interest in the sense that it could effect the desirable solution faster and in a more cost-effective manner than parliament. Legislators should not be bothered with all the minor amendments to the law that changing conditions require and that could be solved by the courts consistent with any principles laid down in legislation (such as constitutional values and the constitutionally sanctioned aim of “justice”). In any event, since legislation is forward-looking and requires imagination as to the situations that may arise, gaps and inapposite applications are likely. History has shown that not even the most careful legislator could ever force all eventualities of life within the framework of legislation (Weber “Einige Gedanken zur Konkretisierung von Generalklauseln durch Fallgruppen” 1992 *Archiv des civilistische Praxis* 516 518, 520, 521, 549). To refer each gap revealed by the judicial process in its grappling with concrete situations to the legislator would not solve the problem and be very costly: new gaps and unfair effects would probably be shown up shortly thereafter by the judicial process. In fact, legislators sometimes deliberately refuse to decide certain issues, “passing the buck to the judiciary” (Hlophe “The Role of Judges in a transformed South Africa – Problems, Challenges and Prospects” 1995 *SALJ* 22 27) or deliberately delegates limited “legislative powers” to the judiciary (cf Hart *The Concept of Law* 2<sup>nd</sup> edition (1994) 275). This is what the legislator has done by expressly mandating courts to develop the common law “taking into account the interests of justice” (s 173 of the Constitution, 108 of 1996). Hart also argues that judicial law-making is “a necessary price to pay for avoiding the inconvenience of alternative methods of regulating them such as a reference to the legislature.” (*The Concept of Law* 275).

with its inherent basic principles to deal effectively with the increasing complexities of modern organised society.”<sup>29</sup>

Our courts have also specifically recognised the need for residual rules of contract law to adapt to changing circumstances. For example, the Supreme Court of Appeal has said that

“Die naturalia van verskillende kontraksoorte kan, wat die Suid-Afrikaanse reg betref, in hoofsaak teruggevoer word na begrippe van redelikheid en billikheid wat in die Romeinse reg ontwikkel het, maar kan in ‘n lewende regstelsel nie as ‘n numerus clausus beskou word nie. By die aanpassing van die reg by veranderde omstandighede en nuwe behoeftes kan dus steeds by wyse van analogie addisionele naturalia erken word.”<sup>30</sup>

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<sup>29</sup> See also *A Becker & Co (Pty) Ltd v Becker supra* 420G-H; *Phame (Pty) Ltd v Paizes* 1973 3 SA 397 (A) 418H-419C; *Alpha Trust (Edms) Bpk v Van der Watt* 1975 3 SA 734 (A) 749D-E; *Janse van Rensburg v Grieve Trust* 2000 1 SA 315 (C) 323 *et seq*; *Tuckers Land and Development Corporation (Pty) Ltd v Hovis* 1980 1 SA 645 (A) 651-652; Olivier JA in *Eerste Nasionale Bank v Saayman NO* 1997 4 SA 302 (A) 319 *et seq*; *Payen Components SA Ltd v Bovic Gaskets CC* 1994 2 SA 464 (W) 475H *et seq*; *Jajbhay v Cassim* 1939 AD 537 at 542; *Bank of Lisbon v De Ornelas* 1988 3 SA 580 (A) 612H-I; *Blower v Van Noorden* 1909 TS 890 905; *Zimnat Insurance Co Ltd v Chawanda* 1991 2 SA 825 (ZSC) 832C-D. *Cf Minister of Justice v Hofmeyr* 1993 3 SA 131 (A) 157; *Willis Faber Enthoven (Pty) Ltd v Receiver of Revenue and Another* 1992 4 SA 202 (A) 220D-221; *S v Graham* 1975 3 SA 569 (A) 576F. In Roman law the *praetor* could adapt the *ius civile* when fairness demanded this. In Roman contract law, the ideal of *bona fide* conduct was an important driving force for amendments to the law. The *praetor*’s appointment by election in the *comitia centuriata*, an assembly of the people, provides a justification for this power which modern judges arguably lacks. However, later judges were also expressly granted the power to prefer justice and equity rather than the demands of the strict law by the emperor Constantine (C 3 1 8). Of course, many other developments in Roman law took place after the *praetor*’s power was curtailed by the *Edictum Perpetuum* around 132AD. Roman-Dutch writers and South African case law also acknowledge the power of courts to change the law when it leads to injustice (see, for example, Voet 1 1 5, 1 1 6 and the other Roman-Dutch writers and case law cited by Neels 1998 *TSAR* 702 716-717 and Van der Merwe “*Iudicis est ius dicere*” 230-231). See also De Vos & Kelbrick “Discretionary powers of the judge in South Africa” 2000 *THRHR* 537 541; Joubert 1992 *TSAR* 213 214; Corbett “Aspects of the role of policy in the evolution of our common law” 1987 *SALJ* 52 54; Neels “Regsekerheid en die korrigerende werking van redelikheid en billikheid (deel 3)” 1999 *TSAR* 484 and authorities there cited; Smits *Het vertrouwensbeginsel* 43.

<sup>30</sup> *A Becker & Co (Pty) Ltd v Becker supra* 420G-H. The first five cases listed in n 29 *supra* also confirm the need for residual contract law rules to adapt to changing circumstances and notions of justice.

The Constitution clearly mandates judges to *develop* the common law in order to reflect the spirit of the Bill of Rights<sup>31</sup> and “taking into account the interests of justice.”<sup>32</sup> In any event, contract law rules, like all legal doctrine, are only conceptual intellectual constructions or products of human thinking, which are aimed at grasping, comprehending, explaining and ordering legal reality, and which do not exist for their own sake. Therefore if they do not serve their function well, they should be changed or refined.<sup>33</sup>

Apart from this broad ideal of justice or fairness, contract law rules also serve the aim of legal certainty. Contracts are planned relationships that require a predictable legal framework to proceed with confidence.<sup>34</sup> Law does not operate only in courtrooms. The outcomes of specific scenarios should be predictable to enable parties to draft contracts and to decide whether to proceed with litigation. Parties cannot be satisfied by a mere assurance that contract law exhorts a judge to find a fair solution in each particular case, changing the law where necessary. There is a need for understandable, abstract rules that give guidance as to the likely resolution of future possible disputes.

The ideals of fairness and certainty appear to clash with each other. It has been said that contract law has always struggled to serve the conflicting aims of certainty and flexibility.<sup>35</sup> In similar vein is the statement that “the central question of practical

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<sup>31</sup> Section 39(2) provides that “When...developing the common law...every court, tribunal or forum must promote the spirit, purport and objects of the Bill of Rights.”

<sup>32</sup> Section 173.

<sup>33</sup> Smits *Het vertrouwensbeginsel* 45. This notion enjoys widespread support in South African legal literature. See, for example, Corbett 1987 SALJ 52 54; Corder & Davis “Law and social practice: an introduction” in Corder (ed) *Essays on law and social practice in South Africa* (1988) 1 *et seq*; Lubbe “Estoppel, vertrouwensbeskerming en die struktuur van die Suid-Afrikaanse privaatreë” 1991 *TSAR* 1 13-18; De Vos & Van Loggerenberg “The activism of the judge in South Africa” 1991 *TSAR* 594. See also Esser “Dogmatischen Denken im Zivilrecht” 1972 *Archiv des civilistische Praxis* 97 112, 124.

<sup>34</sup> Smits *Het vertrouwensbeginsel* 45; Tillotson *Contract Law in Perspective* 3<sup>rd</sup> edition (1995) 27.

<sup>35</sup> Smits *Het vertrouwensbeginsel* 43; Lubbe “Die verpanding van vorderingsregte en die regsdogmatiek – quo vadis?” 1991 *Stell LR* 131 137; *cf Payen Components SA Ltd v Bovic Gaskets CC* 1994 2 SA 464 (W) 476.

jurisprudence" is how far certainty in the law may be reconciled with the achievement of justice in the particular case.<sup>36</sup>

However, it is important to note that the aims of justice and certainty are interlinked. That there is a link between them emphasises the need to aim for the best compromise or optimum between these goals, so that the one is not downplayed at the expense of the other.<sup>37</sup> The link is this. On the one hand, uncertainty and unpredictability is unfair.<sup>38</sup> On the other hand, unjust rules or an unjust result is surprising and unpredictable and therefore creates legal uncertainty. The first proposition has already been alluded to. It is only fair that parties who draft contracts or decide whether to embark on litigation, have guidelines in the form of abstract, consistent rules as to what a court is likely to lay down in respect of their rights, duties and remedies. It would be unfair and unjust if they had little or no guidelines as to what may be expected from a court, apart from a general assurance that the court will endeavour to reach a fair solution in the circumstances of each case.<sup>39</sup> The party who loses the dispute would have had no opportunity to appreciate her legal position, so that the resultant loss of time and money is unfair.<sup>40</sup> On the other hand, inflexible and strict rules aimed at legal certainty create a false sense of legal certainty when they turn out to be clearly unfair in certain circumstances. Such rules that are unjust in certain situations actually create legal uncertainty, as parties are bound to challenge rules that are out of step with commercial reality and generally accepted notions of fairness and collective welfare goals (public policy), and courts are bound, sooner or

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<sup>36</sup> Lord Reid "The Law and the Reasonable Man" 1986 *Proceedings of the British Academy* 193. See also Van Aswegen "Policy Considerations in the Law of Delict" 1993 *THRHR* 171 194; Neels 1998 *TSAR* 702 266; Weber 1992 *Archiv des civilistische Praxis* 516 536; Van Dunné *Verbintenissenrecht Deel 1: Contractenrecht* 2<sup>nd</sup> edition (1993) 121.

<sup>37</sup> Esser 1972 *Archiv des civilistische Praxis* 97 120.

<sup>38</sup> Cf Neels 1998 *TSAR* 702 703 ("Redelikheid sluit onder meer die strewe na regsekerheid in"). However, Neels imbues reasonableness with a different meaning than fairness, as discussed in n 92 *infra*.

<sup>39</sup> Cf Van Aswegen 1993 *THRHR* 171 194.

<sup>40</sup> Moreover, previous decisions create a reasonable reliance that the same result would be reached on similar facts, provided that the result is not clearly unjust. Cf Neels "Regsekerheid en die korrigerende werking van redelikheid en billikheid (deel 2)" 1999 *TSAR* 256.

later, to adapt or overturn these rules.<sup>41</sup> For example, there is bound to be uncertainty when courts hold that one set of residual rules should apply to all rights of pre-emption if in commercial reality pre-emption contracts are expected to serve different purposes in different contexts.

## 6 2 2 The determinants of fairness

What considerations determine whether a solution, or set of default rules is "fair" or "reasonable"?

### 6 2 2 1 *Not a matter of mere intuition or logic*

Firstly, it is not a matter of mere intuition or a subjective sense of equity and fairness, as different people may have different views of what is fair and reasonable.<sup>42</sup> Schorer has famously said that "... a judge who judges in accordance with his own common sense and sense of equity and without rules of law is to be feared more than dogs and snakes."<sup>43</sup> One implication is that detailed reasons must be given for why a solution or rule is fair and reasonable, especially where a court deviates from the *prima facie* legal position.<sup>44</sup> One of the advantages of formal modes of reasoning is to prevent judges from simply reaching conclusions that they regard as logical and obviously correct, whereas there may be a difference of opinion on the matter.<sup>45</sup> As it is aimed at persuasion, such reasoning also assists a discourse by other judges and commentators on the correctness of the decision. Giving reasons forces judges to

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<sup>41</sup> Cf Smits *Het vertrouwensbeginsel* 58; Neels 1999 *TSAR* 256 271.

<sup>42</sup> Smits *Het vertrouwensbeginsel* 13.

<sup>43</sup> Cited with approval in *Preller and Others v Jordaan* 1956 (1) SA 483 (A) 500G.

<sup>44</sup> *Edouard v Administrator Natal* 1989 2 SA 368 (D) 378D-F; Lubbe "Bona fides, billikheid en die openbare belang in die Suid-Afrikaanse kontrakreg" 1990 *Stell LR* 13 15; Neels 1999 *TSAR* 684 696; Neels 1999 *TSAR* 256 260, 267; Neels 1999 *TSAR* 484 486 and authorities there cited.

<sup>45</sup> Cf Weber 1992 *Archiv des civilistische Praxis* 516 561.

critically evaluate their judicial hunch or innate legal sense (*regsgevoel*).<sup>46</sup> The judicial hunch or legal sense can probably be partially ascribed to actual experience of applying the law and ingrained knowledge of legal rules and standards, which may therefore differ from person to person.<sup>47</sup> It should also be accepted that people's thought processes are frequently not "logical" so that their "judicial hunch" is not a guarantee of correctness.<sup>48</sup> Consider for example the South African writers on preference contracts who simply branded the bare preference constructions of Botha JA and the *Hartsvrivier* case<sup>49</sup> as "illogical", "unreasonable,"<sup>50</sup> and "practically useless,"<sup>51</sup> without giving any reasons, whereas these constructions are championed as commercially sensible in other jurisdictions.<sup>52</sup>

#### 6 2 2 2 *The hypothetical consensus of typical parties*

Secondly, contract law rules can only be fair if they are in fact suitable and appropriate to comprehend, explain or reflect legal reality, including practices of the business community or other contractants.<sup>53</sup> Therefore, "an increase in the complexity of some areas of law may be desirable, if it accurately mirrors the increased complexity of social and economic life."<sup>54</sup> Contract law should not be less changeable than the economy and society. Formalism is to be decried because it

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<sup>46</sup> Smits *Het vertrouwensbeginsel* 13 who emphasises that one's legal intuition (*regsgevoel*) should only be a factor which starts off the process of searching for grounds that would cause a certain result to be regarded as just.

<sup>47</sup> Van Aswegen 1993 *THRHR* 171 179.

<sup>48</sup> Vorster *Implied Terms* 10.

<sup>49</sup> *Hartsvrivier Boerderye (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T). See par 2 1 2 *supra*.

<sup>50</sup> Eiselen "*Souteriou v Retco Poyntons (Pty) Ltd* 1985 2 SA 922 (A): Voorkoopreg – regte en verpligtinge van partye" 1986 *THRHR* 95 97.

<sup>51</sup> Reinecke & Otto 1986 *TSAR* 18 20, 21 n 26.

<sup>52</sup> See Ch 4 *supra*.

<sup>53</sup> Tillotson *Contract Law* 3; Zweigert & Kötz *Introduction to Comparative Law* 3<sup>rd</sup> edition (translated by Tony Weir) (1998) 34. Cf Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 154-155.

<sup>54</sup> Eisenberg "The Bargain Principle and its Limits" 1982 *Harvard Law Review* 741 801 (reproduced in Alexander *Contract Law Volume I* (1991) 323 *et seq.*)

tends to isolate law from society, thereby encouraging the spurious idea that law is autonomous and an end in itself rather than a means to social order.<sup>55</sup> The need for law to be in step with commercial reality has often been pointed out. Apart from the *dicta* from *Pearl Assurance Co v Union Government*<sup>56</sup> and *Blower v Van Noorden*<sup>57</sup> cited above, the following statement by Lord Wilberforce drives the point home:

If I am faced with the alternative of forcing commercial circles to fall in with a legal doctrine which has nothing but precedent to commend it or altering the doctrine so as to conform with what commercial experience has worked out, I know where my choice lies. The law should be responsive as well as, at times, enunciatory, and good doctrine can seldom be divorced from sound practice.<sup>58</sup>

Therefore specific contract types must be continually rethought, changed and refined to make sure that they are functional and related to the demands of life.<sup>59</sup> The economic realities of the typical situation, the economic purpose of the contract type, must therefore be taken into account when formulating default rules.<sup>60</sup> This means that it is clearly dangerous to try and formulate general rules or propositions for a class of contracts, for example preference contracts, if the contracts in the class do not

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<sup>55</sup> Tillotson *Contract Law* 18. This problem with formalism has long been recognised by, *inter alia*, North American pragmatists and realists like Pound (“Mechanical jurisprudence” 1908 *Columbia Law Review* 605; cf Van Blerk “American Realism Revisited” in Van Wyk (ed) *Nihil Obstat: Feesbundel vir WJ Hosten/Essays in Honour of WJ Hosten* 191) and the German *Freirecht* (“free law”) school (see Weber 1992 *Archiv des civilistische Praxis* 516 519-520). Of course, already in Roman times fairness and the demands of a society active in international trade came to be seen as more important than formalistic doctrine or “strict law”. See n 29 *supra* and texts like C 3 1 8 and D 50 17 183. See also the Roman Dutch writers cited by Neels 1998 *TSAR* 702 716-717 and Van der Merwe “*Judicis est ius dicere*” 230-231.

<sup>56</sup> *Supra*.

<sup>57</sup> *Supra*.

<sup>58</sup> Cited by Tillotson *Contract Law* 3.

<sup>59</sup> Martinek *Moderne Vertragstypen* 2; cf Zweigert & Kötz *Introduction to Comparative Law* 34.

<sup>60</sup> Vorster *Implied Terms* 33; Martinek *Moderne Vertragstypen* 30; Gordley *The Philosophical Origins of Modern Contract Doctrine* (1991) 241. Cf Smits *Het vertrouwensbeginsel* 30-31. The originators of the concepts of *essentialia* and *naturalia* in the middle ages emphasised this: one had to establish the end or purpose of the contract, and its *essentialia* and implied terms would be determined by that end (see par 6 4 1 at n 228 *infra* where the origin of this model is discussed in more depth).

in fact follow a single pattern in practice.<sup>61</sup> It also means that a set of default rules accepted for preference contracts should not be denounced simply on the basis of historical authority, precedent or “logic,” without considering its social or economic usefulness. Moreover, the law must be prepared to recognise new types of specific contracts that require special rules.<sup>62</sup> This is the necessary consequence of contractual freedom.<sup>63</sup>

In the endeavour to correctly reflect legal reality, residual rules should attempt to reflect the conventional understanding of most parties to such contracts where the parties’ actual purpose or interests cannot be known.<sup>64</sup> One of the functions of dispositive contract law is therefore to seek the typical will of parties for typical conflicts of interests, in an attempt to approximate the actual parties’ likely intention.<sup>65</sup> Many terms implied by law probably developed from an interpretation of what typical parties intended in the normal case.<sup>66</sup>

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<sup>61</sup> Vorster *Implied Terms* 157 n 109, 37. A danger of generalising abstraction is that concepts are defined so broadly that factual situations may be grouped together on formally logical and systematic, but essentially artificial grounds. See Lubbe 1991 *Stell LR* 131 137 n 48; cf Wicke *Vicarious Liability in Modern South African Law* unpublished LLM thesis, University of Stellenbosch (1997) 244, 247.

<sup>62</sup> For examples of new contract types see Martinek *Moderne Vertragstypen* 2.

<sup>63</sup> Martinek *Moderne Vertragstypen* 15.

<sup>64</sup> Joubert *Die Finansiële Huurkontrak* 63.

<sup>65</sup> Leenen *Typus und Rechtsfindung* (1977) 180. Cf Eisenberg “The Theory of Contracts” in Benson (ed) *The Theory of Contract Law: New Essays* (2001) 206 227.

<sup>66</sup> Joubert *General Principles* 66; Corbett AJA (as he then was) in *Alfred McAlpine & Son (Pty) Ltd v Transvaal Provincial Administration* 1974 (3) SA 506 (A) 532G-533A recognised that implied terms in the sense of rules of law which the Court will apply unless validly excluded by the contract itself “may have originated partly in the contractual intention”. The “objective” application of the bystander test in terms of which the question is what reasonable persons in the position of the parties would have agreed to, confirms that the understanding of typical parties to such contracts are relevant to the implication of terms. For examples of cases where the bystander test was applied in this objective manner, see Vorster *Implied Terms* 167 *et seq*; Kerr *Contract* 335 *et seq*; cf Cockrell 1992 *SALJ* 40 53. These cases are criticised by some authors for failing to distinguish clearly between tacit and residual provisions (see for example Kerr *Contract* 335-336). I agree with this criticism insofar as courts implying residual provisions should not only rely on the likely consensus of the parties (as I will show below). On the other hand, it is better to expressly involve objective fairness and reasonableness considerations in the process of implying tacit terms than to totally ignore these considerations by hiding behind a façade of

That an *ex lege* term would probably concur with the conventional understanding of most parties to such contracts provides an additional justification for overcoming the fear of “making contracts for parties.” The implication of *ex lege* terms can therefore also be partly defended with reference to what parties would probably have done themselves had they negotiated the matter.

The legitimacy of considering the conventional understanding of typical parties allows consideration of the respective positions of bargaining power of parties who typically conclude these contracts, at least where this does not lead to oppression or exploitation as a result of a typical disparity in bargaining power. The need for a paternalistic attitude that seeks to protect the weaker party, is excluded where neither party typically has such a preponderance of bargaining power as to be in a position to oppress the other,<sup>67</sup> and where market forces operate freely.<sup>68</sup> Freedom of contract is only undermined and injustice done where there is an almost complete lack of bargaining power so that terms are basically imposed on the weaker party to the latter's disadvantage.<sup>69</sup> Therefore, the only sensible way of dealing with inequality in bargaining power is to have regard to its causes and the circumstances surrounding it.<sup>70</sup> It should be checked whether any oppression or exploitation typically results from the inequality. If yes, the weaker party should be protected. If no, effect should be given to the relative bargaining positions of the parties.<sup>71</sup> Transposed to preference contracts, these principles mean that it can be taken into account that grantors of

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unexpressed *consensus* between the parties. See also Van der Merwe *et al Contract* 199; Neels 1999 *TSAR* 684 695.

<sup>67</sup> Vorster *Implied Terms* 34.

<sup>68</sup> *Ibid.* Where two businessmen have contracted at arms's length, the fact that one of the parties was unwise or unlucky in agreeing to a specific bargain, or that one party is richer than the other or that supply exceeds demand at that stage, has nothing to do with ensuring that justice is done. Justice is only done if parties who have bargained on equal terms in a free market without oppression are forced to stick to their agreements (Vorster *Implied Terms* 34). Inequality between a consumer and a corporate body that virtually monopolises a market is very different from inequalities in the marketplace due to demand for a commodity (Vorster *Implied Terms* 56).

<sup>69</sup> Tillotson *Contract Law* 7, 41.

<sup>70</sup> Vorster *Implied Terms* 56.

<sup>71</sup> *Ibid.*

rights of pre-emption in respect of property are generally in a stronger bargaining position than the holders, and that such rights are often granted gratuitously, without any oppression of the holders. Therefore it is legitimate to argue for a default construction that limits the grantor's freedom to deal with his property as little as possible, as that this is what grantors would most likely have agreed to and what holders would most likely have been forced to accept.<sup>72</sup> The only contexts in which a paternalistic attitude may be called for is in favour of artists such as authors as grantors vis-à-vis publishers, in favour of franchisees as grantors vis-à-vis franchisors and in favour of employees or independent contractors as grantors vis-à-vis employers. In most other contexts where preference contracts operate, free market conditions prevail.

However it would be very problematic to regard the approximation of the subjective will of typical parties to a specific type of contract, in other words the parties' hypothetical consent, as the only determinant and justification of residual rules for that contract type. This is what libertarian "contractarianist" or "consensualist" theorists seek to do,<sup>73</sup> and their radically individualist theories have justly been criticised.<sup>74</sup>

There are at least two reasons why an attempt to only approximate the actual or hypothetical consent of parties when determining the consequences of a contract is unsatisfactory.

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<sup>72</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 305.

<sup>73</sup> Prime examples are Charles Fried (*Contract as Promise: A Theory of Contractual Obligation* (1981)) and Randy Barnett. Barnett's "consent theory" has been set out in articles such as "A Consent Theory of Contract" 1986 (vol 86) *Columbia Law Review* 269-321. Posnerian contract theory also justifies the criterion of wealth maximisation on the basis that wealth maximisation is based on implied general consent. In this sense Posnerian contract theory is also consensualist. Posner's argument rests on the debatable presupposition that parties seek only to maximise wealth.

<sup>74</sup> Posner's fictional assumption about human nature "denies human desires for fairness, decency, trust, co-operation and the like." (Braucher "Contract versus Contractarianism: The Regulatory Role of Contract Law" 1990 *Washington and Lee Law Review* 697 707). See Braucher 737 n 160 on the other problematic aspects of pure Posnerian contract theory. See also Eisenberg "The Theory of Contracts" 225 *et seq.*

Firstly, searching after the presumed intention of parties would often involve an artificial inquiry and a fiction, which makes it unnecessary to articulate the basis for the decision, and opens the door to speculation.<sup>75</sup> To regard all residual rules as consensual “is to ascribe too much calculation to parties.”<sup>76</sup> When a court is guessing at an intention that never in fact existed, it is difficult to discover what factors have really weighed with the court in reaching its decision.<sup>77</sup> This allows courts to give effect to their own unreasoned perception of justice in the individual case without being forced to consider conflicting views of doing justice.<sup>78</sup> Because the basis of decisions is left obscure and unarticulated, it becomes unnecessarily difficult for lawyers to advise clients.<sup>79</sup> The dangers and inadequacy of the “officious bystander” test and the “*Moorcock* doctrine” of English law which focus on the hypothetical consensus of parties (both in the context of establishing “actual tacit terms agreed on” as well as terms implied by law), have been clearly demonstrated by, amongst others, Vorster in his extensive study of implied terms, and will not be repeated in depth here.<sup>80</sup>

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<sup>75</sup> Vorster *Implied Terms* 177, 187; Lubbe & Murray *Contract* 463; Van der Griten *Redelijkheid en Billijkheid in het Overeenkomstenrecht* (1978) 3 cited by Neels 1999 *TSAR* 684 696 n 82. The court’s decision needs merely be justified by judicial assertion that, of course, this is what (typical) parties would have agreed.

<sup>76</sup> Braucher 1990 *Washington and Lee Law Review* 697 731; cf Gordley *The philosophical origins* 209-210.

<sup>77</sup> Cf Atiyah *An Introduction to the Law of Contract* 5<sup>th</sup> edition (1995) 203. The search for the probable consent of the parties is beset with difficulties especially because the search commences at a time when the relationship has broken down and there are disputes on what was intended. Therefore interpretation and supplying of terms cannot depend entirely upon consent, except in a fictitious sense. (See also Lubbe & Murray *Contract* 463; Van Dunné *Verbintenissenrecht* 119; Braucher 1990 *Washington and Lee Law Review* 697 711; Eisenberg “The Theory of Contracts” 237).

<sup>78</sup> Vorster *Implied Terms* 177, 187; Eisenberg “The Theory of Contracts” 237-258.

<sup>79</sup> *Ibid* 190.

<sup>80</sup> See especially at 63 *et seq* and 177 *et seq*. See also Vorster *Implied Terms*; Vorster “The Influence of English Law on the implications of terms in the South African Law of Contract” 1987 *SALJ* 588-598; Vorster “The bases for the implication of contractual terms” 1988 *TSAR* 161 178-179; Van der Walt “Die huidige posisie in die Suid-Afrikaanse Reg met betrekking tot onbillike kontrakbedinge” 1986 *SALJ* 646 653; Findlay & Kirk-Cohen “On Fictitious Interpretation” 1953 *SALJ* 145; Olivier *Legal Fictions: An Analysis and Evaluation* (1973) 127-128. Vorster’s criticism has been referred to with approval by, amongst others, Neels 1999 *TSAR* 684 696. Neels points out that whereas courts

Vorster argues that where the parties' actual intention cannot in fact be ascertained, the law should rather aim for the rational development of guidelines for solutions of particular problems and thereby contribute to the predictability of law,<sup>81</sup> instead of insisting on using the fictitious bystander test. Other authors have also argued strongly that the law should make policy choices explicitly and in a reasoned manner and not mask the choices as "consent", whether actual but tacit or hypothetical.<sup>82</sup> The need to take into account policy considerations in formulating residual rules and the desirability of legal certainty, means that the courts should not insist that each dispute on the apposite rule could be decided simply by construing or interpreting the transaction without reference to normative considerations. Such an *ad hoc* approach would require courts to embark upon "an exasperating goose chase after non-existent contractual meaning" in cases where the parties left the situation completely unprovided for.<sup>83</sup> Such an approach is actually more exposed to undue reliance on personal preference and the spectre of legal uncertainty than one admitting to judicial law-making on the basis of fully fleshed out policy considerations. Moreover, rules or principles formulated in the abstract give future courts the benefit of previous

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habitually used the tacit term approach in the context of choice of law provisions, more recent decisions are accepting that an *ex lege* term is involved. See also Kerr *Contract* 346 who points out that residual provisions would frequently not pass the officious bystander test.

<sup>81</sup> Vorster *Implied Terms* 190; Vorster 1987 *THRHR* 450; Neels 1998 *TSAR* 702 707. On the undesirability of legal fictions, see Olivier *Legal Fictions* (especially at 125 *et seq* with regard to interpretation); Lubbe & Murray *Contract* 442 n 6; Braucher 1990 *Washington and Lee Law Review* 697 707. The use of fictions to disguise a new rule is an ancient technique in which the "new" (a policy choice) can overcome the prejudices of the present without dealing with the resultant doctrinal contradictions (Joubert 1992 *TSAR* 213 217; Esser 1972 *Archiv des civilistische Praxis* 97 105). If a term was recognised as a (probably fictional) tacit one in a number of cases, it may develop to a *naturale*. Recognition of a tacit term in the face of unwillingness to create law by recognition of a novel *naturale*, is therefore better than total refusal to imply any term at all when fairness and policy considerations demand this.

<sup>82</sup> Braucher 1990 *Washington and Lee Law Review* 697 733. Cf Kerr *Contract* 336.

<sup>83</sup> Vorster *Implied Terms* 37, quoting from Stoljar "Prevention and Co-operation in the Law of Contract" 1953 *Canadian Bar Review* 231 244. See also Cockrell "Second-guessing the exercise of contractual power on rationality grounds" 1997 *Acta Juridica* 26 39.

courts' experience and insights in attempting to reach a fair solution.<sup>84</sup> Rules reflect current opinions about the fair weighing of interests and policy considerations, and the factual case can therefore be compared with what has been achieved earlier.<sup>85</sup> This is another reason why courts should generally not be content with mere *ad hoc* pronouncements on a fair implied term in the specific case.<sup>86</sup>

Whether these laudable goals for the filling of contractual gaps should be accomplished by means of the conceptual tool of *ex lege* terms in situations traditionally regarded as the territory of "tacit terms", or rather through a process of "normative interpretation" of each contract, or both, is considered at a later stage.<sup>87</sup>

Secondly, presumed intention or consent as the only determinant of default rules, would not help much where the typical interests of typical parties conflict. That their interests conflict means that they would very likely not have considered a particular solution as "obviously correct" or "obviously fair" in terms of an officious bystander type of test aimed at establishing their probable consensus.<sup>88</sup> Therefore, the development of default rules must aim for a fair balance of typical party interests by an outsider, that is, the courts. An important function of default rules is indeed to ensure a just and suitable, expedient and functional balance of conflicting party interests.<sup>89</sup> In other words, absent provision by the parties, courts should consider what parties *should* have agreed, and accept the probability that that is what they *would* have agreed.<sup>90</sup>

### 6 2 2 3 Policy considerations and underlying principles

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<sup>84</sup> Smits *Het vertrouwensbeginsel* 46.

<sup>85</sup> Smits *Het vertrouwensbeginsel* 40, 46.

<sup>86</sup> Cf Martinek *Moderne Vertragstypen* 10. See also Neels 1998 *TSAR* 702 711 *et seq* on the general undesirability of *ad hoc* decisions on the basis of a judge's idea of fairness.

<sup>87</sup> Par 6 4 *infra*.

<sup>88</sup> Cf Cockrell 1997 *Acta Juridica* 26 39; Eisenberg "The Theory of Contracts" 227.

<sup>89</sup> Leenen *Typus und Rechtsfindung* 129; Joubert *Die Finansiële Huurkontrak* 63-64.

<sup>90</sup> Cf Gordley *The philosophical origins* 243.

“Fairness” entails not only fairness between the parties, but also doing justice in the eyes of the community as a whole. This requires the advancement of desirable goals of collective social welfare, including the promotion of ethical values and generally accepted underlying principles of our law. The Roman Dutch writer Huber recognised this extended meaning of “fairness” by his distinction between natural fairness and civil fairness (*burgerlijke billijkheid*). The latter, he says, includes “the considerations of what is useful and profitable for a nation.”<sup>91</sup> All these determinants of fairness can be grouped together as “policy considerations”<sup>92</sup> (Their interrelationship is considered in more depth below.)

The relevance of policy considerations to residual rules is not a new truth for South African courts and lawyers. Vorster has clearly shown that South Africa courts do not shy away from using their power to recognise new residual rules or *ex lege* terms on the basis of policy considerations relevant to the kind of contractual relationship in question.<sup>93</sup> For example, the South African *locus classicus* on implied terms, *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration*<sup>94</sup> expressly recognises that legal policy contributes to the creation of residual provisions.<sup>95</sup> Already in Roman law, an important source of South African contract law rules, residual rules were based not on hypothetical consent, but on objective notions of fairness and good faith, as *formulae* of contractual actions ordered the judge to reach a solution which is in accordance with *bona fides*.<sup>96</sup>

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<sup>91</sup> HR 1 1 15 (Gane’s translation).

<sup>92</sup> The following writers agree that “policy considerations” refer to ethical values or desirable goals of collective social welfare: Van Aswegen 1993 *THRHR* 171 174; Corbett 1987 *SALJ* 52 59; Lubbe 1990 *Stell LR* 13-17; Lubbe & Murray *Contract* 241; Cockrell 1992 *SALJ* 40; Bell *Policy arguments in judicial decisions* (1983) 22-23.

<sup>93</sup> See *inter alia* at 74, 147 of his thesis. See also Joubert *Die Finansiële Huurkontrak* 63; Corbett 1987 *SALJ* 52 52; Van der Merwe & Lubbe “*Bona fides* and public policy in contract” 1991 *Stell LR* 91 99-101; Lubbe & Murray *Contract* 424; Neels 1999 *TSAR* 684 697. A number of the cases listed in n 29 *supra* serve as examples. See also *Par Excellence Colour Printing (Pty) Ltd v Ronnie Cox Graphic Supplies (Pty) Ltd* 1983 1 SA 295 (A); *Falch v Wessels* 1983 4 SA 172 (T).

<sup>94</sup> 1974 3 SA 506 (A).

<sup>95</sup> 532G–H.

<sup>96</sup> The judge was enjoined to decide the case in accordance with *bona fides*, either by the *intentio* of actions on *contractus consensu* like sale and lease, or by the *exceptio doli*, a clause which could be

In fact, all legal rules ought in the final analysis to be justifiable by reference to some consideration of policy.<sup>97</sup> This is because all law, including contract law, is regulatory: it involves use of state power.<sup>98</sup> When it is worthwhile for the state to put the machinery of the law in the service of the one party against the other, and how that should be done, are important questions of public policy.<sup>99</sup> The application or statement of the law (*ius dicere*) is therefore “unavoidably embedded in political considerations.”<sup>100</sup> Policy considerations should be seen “as an inherent part of legal materials, often reflecting fundamental principles immanent in the legal system.”<sup>101</sup> The reasons why the application of rules do not always go hand in hand with a detailed analysis of the relevant policy considerations is that it is (mostly correctly) presumed that existing rules based on precedent or legislation are based on sound considerations of policy.<sup>102</sup> Usually it would therefore only be necessary to refer to policy considerations if an existing rule is challenged or a dispute is not covered by

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inserted into the *formulae* of other contractual actions whose *intentiones* did not contain a reference to *bona fides*, such as the *actio ex stipulatione*. See generally Schermaier “*Bona fides* in Roman contract law” in Zimmermann & Whittaker (eds) *Good Faith in European Contract Law* (2000) 63 66 *et seq.* For a historical overview see Zimmermann “Good faith and equity” in Zimmermann & Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 217. See also *Tuckers Land and Development Corporation (Pty) Ltd v Hovis supra* 652 where the court refers to Roman law as justification for the court’s power to imply an (*ex lege*) term on the basis of good faith or fairness. See also *A Becker & Co (Pty) Ltd v Becker supra* 420G-H.

<sup>97</sup> Vorster *Implied Terms* 18. Cf Corder & Davis “Law and social practice: an introduction” 1 2.

<sup>98</sup> Braucher 1990 *Washington and Lee Law Review* 697 699.

<sup>99</sup> Braucher 1990 *Washington and Lee Law Review* 697 700 quoting from Cohen “The Basis of Contract” in *Law and the Social Order* (1933) 78-79; 103-104. Cf Eisenberg “The Theory of Contracts” 228.

<sup>100</sup> Van der Merwe “*Iudicis est ius dicere*” 231. See also Hlophe 1995 *SALJ* 22 28, quoting from Wade *Constitutional Fundamentals* revised edition (1989) 78.

<sup>101</sup> Van Aswegen 1993 *THRHR* 171 194. Cf Hutchison’s description of good faith as “an ethical value or controlling principle based on community standards of decency and fairness that underlies and informs the substantive law of contract” (“Non-Variation Clauses in Contract: Any Escape from the *Shifren* Straitjacket?” 2001 *SALJ* 720 quoted with approval by the majority in *Brisley v Drotsky* 2002 4 SA 1 (SCA)).

<sup>102</sup> Vorster *Implied Terms* 18.

precedent or statute.<sup>103</sup> (Of course, another reason for the dearth in policy analysis in some South African legal literature and case law is the mistaken assumption by some authorities that contract law, or at least its consequential rules, is a “seamless web of [value-neutral] rules which possesses a determinative rationality of its own, such that answers to any dispute will be thrown up by the inexorable logic that is internal to the system itself.”<sup>104</sup>)

#### 6 2 2 3 1 Underlying principles

Conflicting interests and purposes must therefore ultimately be balanced fairly by having regard to fundamental principles underlying our contract law rules, such as the protection of reasonable reliance,<sup>105</sup> good faith,<sup>106</sup> individual autonomy,<sup>107</sup>

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<sup>103</sup> Cf Van Aswegen 1993 *THRHR* 171 194-5 who says judicial law-making using policy considerations is “basically interstitial” as it occurs where a plain and clear valid legal rule cannot by means of the conscious rational use of ordinary logical and deductive reasoning, furnish an answer.” Policy considerations should in my view also be kept in mind where “a plain and clear valid legal rule” does apparently “furnish an answer”, but is challenged on the basis that it does not adequately reflect and fairly regulate the situation which it seeks to order, even though the situation is not a novel one. Van Aswegen 1993 *THRHR* 171 probably caters for this concern by including cases where law is changed or adapted by using policy considerations as “interstitial” in the sense that the settled legal materials are “inadequate” to reach a decision (189).

<sup>104</sup> Cockrell 1992 *SALJ* 40.

<sup>105</sup> That reasonable reliance should be protected, is widely acknowledged as an important principle underlying our law, particularly as a supplementary basis for contractual liability. See Lubbe & Murray *Contract* chapter 3 especially at 108, 163 *et seq* and authorities there cited; Van der Merwe *et al Contract* 29-41; Kerr *Contract* 20, 23; Cockrell 1992 *SALJ* 40 49. This necessarily means that legal consequences may be determined by the reasonable expectations of a party (Lubbe & Murray *Contract* 425; Vorster 1988 *TSAR* 161). However, this principle is so open-ended that a statement that a certain residual term is justified by it should not be accorded much weight without full motivation. Some of the authors who deny the commercial utility of Botha JA’s construction of preference contracts have, for example, simply stated that it is unreasonable, and by implication, that it thwarts the reasonable expectations of the holder, without considering whether parties may in fact have reason to agree to such contracts. Use of the language of reasonable reliance without further motivation comes close to the radically consensualist or “hypothetical bystander” method of implying residual terms for which the only test for residual terms is “the terms that typical parties would have consented to.” The limitations of this approach was discussed at n 73 *et seq supra*. See also Weber 1992 *Archiv des civilistische*

reciprocity,<sup>108</sup> that there should be a balance of power<sup>109</sup> or “substantial equivalence” of exchanges,<sup>110</sup> and that the vulnerable should be protected. These are all expressions of the fairness ideal and simultaneously desirable policy goals.<sup>111</sup> They are regarded as underlying principles as they are the motivation or basis for a number of legal rules.<sup>112</sup> As they are realised and sanctioned through accepted rules, they have

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*Praxis* 516 524 who regards “reliance” as an open-ended standard together with “good faith” and “fairness”.

<sup>106</sup> See especially *Tuckers Land and Development Corporation (Pty) Ltd v Hovis* 1980 1 SA 645 (A) 652G. See also the majority decision in *Brisley v Drotsky supra* par 21 and *Afrox Health Care Limited v Strydom* 2002 6 SA 21 (HHA) par 32. Cf Lubbe “*Bona fides*, billikheid en die openbare belang in die Suid-Afrikaanse kontraktereg” 1990 *Stell LR* 7 20; Van der Merwe & Lubbe 1991 *Stell LR* 91 and Cockrell 1997 *Acta Juridica* 26 42-43 who attempt a closer description of this policy consideration. See also Lubbe & Murray *Contract* 425 n 7; Cockrell 1992 *SALJ* 40 55 *et seq*; Zimmermann “Good faith and equity”.

<sup>107</sup> See especially Lubbe 1991 *TSAR* 1 13 *et seq* for a discussion of this principle.

<sup>108</sup> *BK Tooling (Edms) Bpk v Scope Precision Engineering (Edms) Bpk* 1979 1 SA 391 (A) 415H; 417 (“*wederkerigheidsbeginsel*”). See also Nieuwenhuis *Drie Beginselen van Contractenrecht* (1979), an in depth study of the three basic principles of party autonomy, the protection of reasonable reliance and reciprocity.

<sup>109</sup> Braucher 1990 *Washington and Lee Law Review* 697 701.

<sup>110</sup> Vorster *Implied Terms* 20; Joubert 1992 *TSAR* 213 214. Cockrell 1992 *SALJ* 40 51 calls this goal “preservation of justice-in-exchange”. Grotius *De iure naturae et gentium libri tres* 2 12 9 1, for example, relies on the principle that contracts requires equality as an argument for the duty to disclose defects in the *merx*.

<sup>111</sup> Hart *The Concept of Law* 260 states that “principles, because they refer more or less explicitly to some purpose, goal, entitlement, or value, are regarded from some point of view as desirable to maintain, or to adhere to, and so not only as providing an explanation or rationale of the rules which exemplified them, but as at least contributing to the justification.” Because they are expressions of the fairness ideal and desirable policy goals, some of these principles, such as the protection of reasonable reliance and individual autonomy, also play a role in other fields of private law. See Neels 1999 *TSAR* 484 488 *et seq* for an overview of fundamental principles applicable to private law generally and to delict and property law in particular.

<sup>112</sup> On the concept of principles of law and their function see Lubbe 1991 *TSAR* 1 3; Van Aswegen 1993 *THRHR* 171 177 *et seq*; Neels 1999 *TSAR* 484 486 *et seq*; Canaris *Systemdenken und Systembegriff in der Jurisprudenz* (1969) 46 *et seq*; Larenz *Methodenlehre der Rechtswissenschaft* (1975) 458 *et seq*; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 223 *et seq*, 302 *et seq*; Dworkin *Taking Rights Seriously* (1978); Dworkin *A Matter of Principle* (1985) 72; Nieuwenhuis *Drie Beginselen van Contractenrecht* (1979) 3 *et seq*; Hart *The Concept of Law* 260 *et seq*. The

normative power in arguments about what rules should be, apart from their inherent persuasive power as ethical postulates.<sup>113</sup>

The Supreme Court of Appeal in *Brisley v Drotsky*<sup>114</sup> and *Afrox Health Care Limited v Strydom*<sup>115</sup> has recently expressly recognised the creative function of underlying principles of contract law, such as good faith, in so far as they may inspire and justify the creation and amendment of rules.<sup>116</sup> The majority in *Brisley v Drotsky* approved Dale Hutchison's statement that good faith as an underlying principle has a creative, controlling, legitimating and explanatory function, but emphasised that it is only one of the principles underlying our law.<sup>117</sup> This implies that the same functions are served by other principles underlying our law.

As open-ended concepts, their application comprises a value judgment, especially since some of them appears to conflict with each other. An attempt must be made to avert these contradictions between principles by an optimal or fair balancing of the relevant principles, with due regard to their interrelationship.<sup>118</sup> Sub-principles have

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distinction between principles and (black letter) rules is gradual or fluid: principles sometimes function directly as open-ended rules or standards. Cf the rule that contracts contrary to public policy are void (*Magna Alloys and Research (SA) (Pty) Ltd v Ellis* 1984 4 SA 874 (A)). See also Neels 1999 *TSAR* 256 258 *et seq*; Nieuwenhuis *Drie Beginselen* 4; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 307-308; Hart *The Concept of Law* 260.

<sup>113</sup> Cf Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 302; Hart *The Concept of Law* 260.

<sup>114</sup> *Supra* 15E-G par 22 of the joint majority judgment.

<sup>115</sup> 2002 6 SA 21 (HHA) par 32.

<sup>116</sup> The court in *Brisley v Drotsky* ultimately decided that the other fundamental principle of party autonomy weighed against a proposed rule that would qualify or abolish the "Shifren straitjacket" on the basis that it conflicts with the principle of good faith. See also Lubbe 1991 *TSAR* 1 for an interesting analysis of a legal problem (the requirements for estoppel) by reference to the underlying principles of individual autonomy and reasonable reliance (especially at 16 *et seq*).

<sup>117</sup> Hutchison 2001 *SALJ* 720, quoted in par 22 of the decision.

<sup>118</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 263, 303. The authors speak of the *Optimierungsgebot*. As they are all meritorious goals, the fact that they sometimes conflict and must therefore be balanced does not mean that they are inconsistent. Eisenberg "The Theory of Contracts" 243-244 explains this by the example that it does not lessen our commitment to the moral norm of truth-telling that we believe it is sometimes morally permissible not to tell the truth, for

evolved from these general principles, which are also helpful for arriving at a fair solution, or, at least, to test and legitimate a solution regarded as “fair” on the basis of one’s legal intuition (*regsgevoel*). The principle of good faith, for example, embraces the principle of protection of reasonable reliance and the “general principle of contractual co-operation” relied upon by Corbett AJA for implication of a residual term in *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration*.<sup>119</sup> Protection of the vulnerable finds expression in the principle that the burden of clear communication must be placed on the generally most sophisticated party. Effect must therefore rather be given to the interests of the other party where the more sophisticated party has not clearly provided in the contract how its interests are to be protected. For example, in the context of rights of first refusal granted by authors to publishers, this principle may be used to argue for a restrictive default construction of such preference contracts in order to safeguard the author (grantor) as the weaker party, whilst placing the burden of clear communication on the publisher (holder) as the more sophisticated party.

#### 6 2 2 3 2 Other policy considerations

Other policy considerations to be taken into account when balancing the parties’ interests include the effect of the different possible solutions on third parties as well as the benefit of maximisation of wealth and cost-effectiveness to society as a whole. These policy goals include ideals such as the desirability of the free alienability of property<sup>120</sup> and the quick settlement of disputes. However, the ideal of

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example in lying to an assassin about his victim’s whereabouts, because of the moral norm that life must be venerated. He also gives the example that the goal of developing a fruitful and rewarding career is not inconsistent with the goal of being a nurturing parent, although time pressures may lead to a conflict between these goals.

<sup>119</sup> 1974 3 SA 506 (A) 534D. Corbett AJA relied on the statement of this principle in *Mackay v Dick* 1881 6 App Cas 251 263, per Lord Blackburn, and by Viscount Simon in *Luxor Ltd v Cooper* 1941 AC 108 118.

<sup>120</sup> Cases on preference contracts confirming the general principle that restraints on alienation should be strictly construed, include the majority decision in *Owsianick v African Consolidated Theatres (Pty) Ltd* 1967 3 SA 310 (A) 321; *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 188; *Edwards (Waaikraal) Gold Mining Co Ltd v Mamogale NO & Bakwena Mines Ltd* 1927 TPD 288; *Ah*

“maximisation of wealth” must not be understood as the only value served by contract law as radical Posnerian contract theory would have it. Posner’s contract theory assumes that people are only ever out to maximise wealth, which simply does not reflect reality correctly.<sup>121</sup> Courts should also realise that, just like “fairness” and “reasonableness”, “cost-effectiveness” is so open-ended that it should not be the only language of justification for a particular term.<sup>122</sup>

Vorster mentions further policy considerations that have been taken into account by courts in England and South Africa in formulating residual rules.<sup>123</sup> They are whether a rule would tend to encourage or discourage conduct that is not beneficial or detrimental to the interests of society, which party is generally in a better position to ascertain and guard against the risks regulated by the proposed rule, whether one of

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*Ling v Community Development Board & Others* 1972 4 SA 35 (E) 37G-38A. See also *Gien v Gien* 1979 2 SA 1113 (T) 1120-1121; *Regal v African Superslate (Pty) Ltd* 1963 1 SA 102 (A) 106-107. This principle is also encountered in other jurisdictions. See for example, Cross “The ties that bind: preemptive rights and restraints on alienation that commonly burden oil and gas properties” 1999 *Texas Wesleyan Law Review* 193 209-210; Conine GB “Property provisions of the operating agreement - interpretation, validity, and enforceability” 1988 *Texas Tech Law Review* 1263.

<sup>121</sup> Cf note 73. One illustration is that many parties litigate to enforce contracts when litigation is commercially unviable (cf *Van Dunné Verbintenissenrecht* 18). Even if efficiency is widely defined as making one person better off without making another worse off, where “better off” means to move to a position which the person chooses in preference to another, the theory remains problematic when it attempts to explain all contract law. As Posner has noted, it is puzzling from an economic standpoint that Shylock cannot enforce his contract with Antonio, or that a person cannot sell himself into slavery (Posner *Economic Analysis of Law* 2<sup>nd</sup> edition (1977) 187). However, it is generally accepted even by opponents of Posnerian theory that wealth maximisation is one of the values which the consequential rule of contract law should serve. See, for example, Braucher 1990 *Washington and Lee Law Review* 697 711; cf Eisenberg “The Theory of Contracts” 238.

<sup>122</sup> Certainly law and economics theorists who claim a consensualist basis for their theories, contradict themselves when they seek to argue about implied terms on the basis of economic efficiency, because the fact that the parties *did not* provide for the contingency shows that “*ex ante* it was not worth the parties’ time to decide how to deal with the risks and burdens. If so, the way these risks and burdens are allocated *ex post* will not affect the value of the contract to the parties *ex ante* or their decision to enter into it. If it does not, then an economist has no reason for caring about what happens *ex post*” (Gordley “Contract Law in the Aristotelian Tradition” in Benson (ed) *The Theory of Contract Law: New Essays* (2001) 265 (hereafter cited as Gordley “Contract Law in the Aristotelian Tradition”) 324).

<sup>123</sup> Vorster *Implied Terms* 30 *et seq* and 157 *et seq*, cited with approval by Joubert 1992 *TSAR* 213 215.

the parties is entitled to an indemnity from a third party, whether a refusal to recognise the residual rule will mean that the innocent party will have no remedy, the economic realities of the typical situation, which includes the respective bargaining positions of the parties and the need to protect the weaker party in the case of oppression, the ability of the party on whom it is sought to place the obligation to redistribute the costs spent in fulfilment of the obligation, the ability of the parties to insure against the regulated risk, the onerousness of the duty sought to be imposed and the degree to which the proposed residual rule fits with existing rules and principles.<sup>124</sup>

Therefore, the formulation of residual rules requires that both the approximation of the typical intention of typical parties to the class of contract and the ideals of fairness and efficiency be strived for.<sup>125</sup> This reflects the fact that in contract law elements of the old idea of market individualism are not entirely displaced by, but mingles with elements of the newer competing ideology of the social welfare mixed economy state.<sup>126</sup> In any event, there is no clear-cut, radical division between consent and residual rules supplied on the basis of policy considerations.<sup>127</sup> The residual rule is supposed to be consistent with a general intention of the parties that their transaction should be effective and fair.<sup>128</sup>

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<sup>124</sup> *Ibid.*

<sup>125</sup> *Cf* Kerr *Contract* 348 n 239.

<sup>126</sup> Tillotson *Contract Law* 43-45. Of course, market individualism still forms an important part of a social welfare mixed economy state like ours.

<sup>127</sup> Braucher 1990 *Washington and Lee Law Review* 697 735.

<sup>128</sup> Vorster *Implied Terms* 80, 83. Gordley "Natural Law Origins of the Common Law of Contract" in Barton (ed) *Towards a General Law of Contract* (1990) 367 418 also shows that the natural lawyers believed the requirement of equality and, therefore, fairness, for the *naturalia* ("natural terms") was not something imposed on parties against their will, but honoured the intention of contracting parties (hereafter cited as Gordley "Natural Law Origins"). A comment in the *Restatement of Contracts* in the USA on supplying terms, illustrates this link between consent and community standards. The comment explicitly rejects the fiction that "the search is for the term the parties would have agreed to if the question had been brought to their attention" (*Restatement (Second) of Contracts* § 204 comment d (1979) quoted by Braucher 1990 *Washington and Lee Law Review* 697 736). Rather, "the probability that a particular term would have been used if the question had been raised" is described as relevant to the question what is a reasonable term (*Ibid. Cf* Kerr *Contract* 348 n 239.) The comment emphasises

Specific contract law rules therefore have both empirical and normative elements: they capture the dialectic of “is” (adhesion to reality) and “ought” (the normative quality of the rules).<sup>129</sup>

It should be clear from the above discussion that contract law rules on the consequences of valid contracts seek to attain the best compromise between mixed and sometimes conflicting ideals,<sup>130</sup> which are moreover vague and open-ended. The possibility always exists that some policy considerations, principles or business practices which are relevant have been ignored or that new policy considerations have become relevant which the existing rules did not take into account due to changing

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that where there is in fact no agreement, a term should be supplied which accords with community standards of fairness and policy. *Restatement (Second) of Contracts* § 204 comment d (1979) quoted by Braucher 1990 *Washington and Lee Law Review* 697 736. Another comment on the duty of good faith and fair dealing in the *Restatement (Second) of Contracts* (USA) confirms the close connection between the need to honour expectations, both subjective and objective, on the one hand, and community standards on the other: “Good faith performance or enforcement of a contract emphasises faithfulness to an agreed common purpose and consistency with the justified expectations of the other party; it excludes a variety of types of conduct characterised as involving “bad faith” because they violate community standards of decency, fairness or reasonableness.” (*Restatement (Second) of Contracts* § 205 comment a (1979) quoted by Braucher 1990 *Washington and Lee Law Review* 697 735).

<sup>129</sup> The latter phrase is taken from Martinek *Moderne Vertragstypen* 31. Cf Joubert *Die Finansiële Huurkontrak* 63-64.

<sup>130</sup> *Brisley v Drotsky supra* par 24: “Die taak van die howe in die algemeen ... is om hierdie grondliggende waardes wat soms met mekaar in botsing kom teen mekaar op te weeg en om by geleentheid, wanneer dit nodig blyk te wees, geleidelik en met verdrag aanpassings te maak.” Cf Lubbe “A doctrine in search of a theory: reflections on the so-called doctrine of notice in South African law” 1997 *Acta Juridica* 246 271 (“multiplicity of factors exerting a normative influence”); cf Corbett 1987 *SALJ* 52 67-68; Braucher 1990 *Washington and Lee Law Review* 697 702; Neels 1998 *TSAR* 702 707; Nieuwenhuis *Drie Beginselen* 3-4. Braucher 701 states that she “remain[s] a skeptic about the need for and the wisdom of a unified field theory of contract, particularly a one-dimensional one; a good grey compromise statement of competing concerns will probably do.” Eisenberg “The Theory of Contracts” 241 also favours a “multi-value theory” which he calls *the basic contracts principle*, which includes an exhortation to affectuate the objectives of parties, subject to appropriate constraints, and which aims at “the best possible rules of contract law” “taking into account all relevant moral, policy and empirical propositions.”

views or practices in society.<sup>131</sup> The endeavour to lay down fair default rules can therefore not be regarded as anything but a continuing, never-ending quest, an eternal debate or discourse.<sup>132</sup> Courts must therefore be prepared to give up the present position or solution when it is shown to be clearly out of step with existing policy considerations and notions of justice as well as the actual purposes of typical parties to such contracts.<sup>133</sup> Similarly, the specific contract types are only model contracts catering for the most important contractual purposes and courts must recognise that new or mixed forms of typical contracts may arise requiring new default rules.

The relevance of policy considerations to residual rules raises a number of questions. May courts take judicial notice of policy goals or are they supposed to be proved on evidence?<sup>134</sup> Are judges not fundamentally incapable of assessing the interests of the community at large due to lack of training and capacity to conduct sociological data gathering?<sup>135</sup> Does a heterogeneous society like ours prevent judges from determining public interest?<sup>136</sup> Is there some kind of systematic hierarchy between the policy considerations and principles mentioned? Does the consideration of policy considerations and open-ended principles of law not make the law utterly unpredictable?

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<sup>131</sup> Cf Joubert *Die Finansiële Huurkontrak* 65; Lubbe 1991 *Stell LR* 131 137; Larenz *Methodenlehre der Rechtswissenschaft* (1975) 14.

<sup>132</sup> Martinek *Moderne Vertragstypen* 29 states that the determination of the legal nature of contract types and their legal consequences can only be understood as a long development process and that institutionalisation of these very complex economic and legal backgrounds and purposes must necessarily proceed in a pluralistic discursive communication process. Cf Lubbe 1991 *Stell LR* 131 138; Cockrell 1992 *SALJ* 40 46 after n 24; Weber 1992 *Archiv des civilistische Praxis* 516 563-564, 566.

<sup>133</sup> Leenen *Typus und Rechtsfindung* 127; Martinek *Moderne Vertragstypen* 15; Joubert *Die Finansiële Huurkontrak* 65.

<sup>134</sup> These issues are raised, but not explicitly addressed by Hawthorne "The principle of equality in the law of contract" 1995 *THRHR* 157 173 and Van der Merwe *et al Contract* 140.

<sup>135</sup> This is a question identified by Hlophe 1995 *SALJ* 22.

<sup>136</sup> Hawthorne 1995 *THRHR* 157 173; Van der Merwe *et al Contract* 140; Lubbe & Murray *Contract* 241.

## 6 2 2 3 3 Judicial notice of policy considerations

There is no reason why courts should not “take judicial notice” of policy goals as they always have done. Judges are “in reality...up to their necks in policy, as they have been all through history...”<sup>137</sup> The application of the *boni mores* standard in delict, which includes the consideration of policy factors weighing against delictual liability (such as unlimited liability) and the application of the “public interest” test for legality of contracts are stock examples of overt policy decisions usually taken without sociological evidence.<sup>138</sup> Sometimes policy goals have been recognised in so many cases that they have become underlying principles of our law, and evidence should therefore not be required to prove them. An example is the principle that contractual restraints on alienation should be strictly interpreted. The constitutional mandate to develop the common law in accordance with the spirit of the Bill of Rights is sufficient authority for courts to interpret and apply the values underlying the Constitution in the absence of evidence on society’s general understanding of these values. This process requires policy decisions. Nevertheless, judges should not easily disallow evidence on public policy issues in appropriate cases, especially where interpretation of the Constitution is at stake. Rule 30 of the Constitutional Court Rules allows parties to present social science and economic data relevant to interpretation of the Constitution.<sup>139</sup> It provides that parties may canvass factual material which are relevant to the issues to be decided by the court, regardless of whether such material appear on the record, provided that such facts are common

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<sup>137</sup> Wade *Constitutional Fundamentals* revised edition (1989) 78, as quoted by Hlophe 1995 *SALJ* 22 28. As a result Hlophe 1995 *SALJ* 22 states that judges’ fear of trespassing upon the functions of the legislature and involvement in political controversy and policy decisions is insupportable. See also the text at n 97 *et seq supra*.

<sup>138</sup> According to *Schultz v Butt* 1986 3 SA 667 (A) 679, the legal convictions of the community must be sought in the convictions of the community’s legal policy makers, such as the legislator and judiciary. According to Van Aswegen 1993 *THRHR* 171 195 “the reference to the generally accepted views of the community, does not simply imply a type of majority view based on a simple opinion poll. It presupposes a reflection of inherent values accepted in the community and apparent from the accepted legal standards and institutions of the community.”

<sup>139</sup> See Chaskalson & Loots “Court rules and practice directives” in Chaskalson *et al Constitutional Law of South Africa* (Revision Service 5, 1999) 7.3(d) and Erasmus, Farlam & Van Loggerenberg *Superior Court Practice* (Review Service 18-2002) C4-69.

cause or otherwise incontrovertible; or are of an official, scientific, technical or statistical nature capable of easy verification. Although the High Court and Magistrate's Court Rules do not contain a similar provision, these courts should allow similar evidence.<sup>140</sup>

#### 6 2 2 3 4 The difficulties caused by a heterogenous society

The difficulties of deciding on public policy in a heterogeneous society has always existed and will always exist, yet contract law demands policy decisions, most notably in the context of legality. A realistic model of adjudication, acknowledging that judges are not just value-neutral applicators of the law, and a representative judiciary in a democratic political system, are important prerequisites (but not guarantees) for sensitivity to communal values and goals.<sup>141</sup> Judges must therefore attempt to link the reasons for their policy or value decisions to generally accepted views of what justice and common welfare demands,<sup>142</sup> and consciously guard against allowing personal preferences influencing a decision, where these are not in accordance with generally accepted views.<sup>143</sup> Reasoned and overt policy choices will do much more to eliminate the danger of adopting a policy goal not shared by society in general than an averred refusal to make any policy choices. A refusal to consider policy considerations is itself a policy choice in favour of political minimalism<sup>144</sup> and retention of the policy choices underlying the *status quo*.

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<sup>140</sup> *Cf S v Lawrence; S v Negal; S v Solberg* 1997 4 SA 1176 (CC) paras 15, 23, 24 and 68; *National Coalition for Gay and Lesbian Equality and Another v Minister of Justice and others* 1999 1 SA 6 (CC) par 88. See further Naudé "The value of life: a note on *Christian Lawyers Association of SA and others v Minister of Health and others* 1998 4 SA 1113 (T)" 1999 *SAJHR* 541.

<sup>141</sup> Lubbe 1991 *Stell LR* 131 137.

<sup>142</sup> Corbett 1987 *SALJ* 52 67.

<sup>143</sup> Van Aswegen 1993 *THRHR* 171 190-191, 194; Lubbe 1990 *Stell LR* 13 15; Lubbe & Murray *Contract* 240-241. The risk of undue reliance on personal preference always exist, regardless of whether a judge is willing to consider policy considerations.

<sup>144</sup> Cockrell 1992 *SALJ* 40.

All value judgments, including application of open concepts such as “fairness” and “reasonableness” which must necessarily be applied in the context of residual rules, remain subjective, influenced by the judge’s legal consciousness and beliefs about ethics and morality.<sup>145</sup> As long as the judge openly declares his value decisions, and because judges are bound by a process of dialogue and rational argument aimed at persuasion, this subjective influence is not to be decried: it aids in the avoidance of unfair application of norms in atypical cases.<sup>146</sup>

#### 6 2 2 3 5 No precise hierarchy of principles and policy considerations

Is there a hierarchy or system of underlying principles and policy considerations setting out the relative values which each must carry? Firstly, a claim that courts must decide hard cases only with reference to underlying principles of law and not with reference to policy considerations (in a narrow sense) must be treated with suspicion. Dworkin is often understood to be a proponent of this argument.<sup>147</sup> He has defined arguments of *principle* as arguments for a right that do not “necessarily” advance a desirable economic, political or social goal, but serve some moral aim such as fairness or justice. Arguments of *policy* are arguments for a collective goal of the community as a whole.<sup>148</sup> However, as Dworkin himself points out, there is no clear distinction between these categories: a principle can be stated as a policy and a policy as a principle.<sup>149</sup> If that is possible, it undermines the argument that courts

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<sup>145</sup> Weber 1992 *Archiv des civilistische Praxis* 516 561.

<sup>146</sup> *Ibid* 563-564.

<sup>147</sup> See, for example, Van Aswegen 1993 *THRHR* 171 177. *Taking Rights Seriously* 294 *et seq*; 363 (*inter alia*) does seem to support this interpretation. But see Mureinik “Dworkin and Apartheid” in Corder (ed) “Essays on law and social practice in South Africa” (1988) 181 for a different interpretation.

<sup>148</sup> *Taking Rights Seriously* 22-23.

<sup>149</sup> *Taking Rights Seriously* 22, 96, 100, 295. Bell *Policy arguments in judicial decisions* 22-23, describes policy arguments as either ethical or goal-based. They are ethical if they appeal to an ethical standard such as fairness, and goal-based if they advocate advancement of some social goal. In fact, there is considerable overlap between these two supposedly separate “categories” of policy considerations. The promotion of ethical or moral values is a desirable goal of collective social

must decide hard cases only with reference to principles and not with reference to policy.<sup>150</sup> Dworkin clearly concedes that policy considerations should at least be taken into account when a rule is uncertain, as he allows their use as arguments to determine the existence and scope of individual rights.<sup>151</sup> What Dworkin therefore really warns against is an untrammelled adjudication on the basis of policy considerations that have not already been recognised in the legal system (they are therefore not legal principles recognised in existing rules), without sufficient regard for consistency and coherence within the legal system.<sup>152</sup> Such necessary checks on the courts' power to make law based on policy considerations will be discussed further below.

In any event, the general welfare of the community *is* a general legal principle underlying our contract law and arguably a value underlying the Bill of Rights.<sup>153</sup> The "public interest" certainly functions as a principle affecting the legality of contracts,

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welfare, and "rightness reasons ultimately depend on general-welfare considerations" (Eisenberg "The Theory of Contracts" 228).

<sup>150</sup> Bell *Policy Arguments in Judicial Decisions* 74-75 agrees that fairness arguments as well as judgments about the collective welfare plays an important part in the decisions judges make. Neels 1998 *TSAR* 702 705 also distinguishes between moral and ethical values (which is concerned with "fairness") on the one hand, and desirable goals of collective social welfare (which is concerned with "reasonableness") on the other. Once again this distinction is not watertight. Reasonableness is certainly also a moral or ethical value and can relate to the conduct expected, ethically and in fairness, from an individual, apart from communal policy goals. However, like Bell, Neels does not use this distinction to argue for a lesser role for "collective social welfare goals" and criticizes Dworkin's distinction as an argument for excluding policy arguments (Neels 1998 *TSAR* 702 709).

<sup>151</sup> *Taking Rights Seriously* 294 *et seq.*

<sup>152</sup> Cf Mureinik "Dworkin and apartheid" 199 *et seq.*; Dworkin *Taking Rights Seriously* 297 ("The difference between an argument of principle and argument of policy... is a difference between two kinds of questions that a political institution might put to itself, not a difference in the kinds of facts than can figure in an answer").

<sup>153</sup> On the relevance of values in constitutional adjudication, see for example *S v Zuma* 1995 2 SA 642 (CC) paras 17-18; *S v Makwanyane* 1995 3 SA 391 (CC) par 9; *De Lange v Smuts NO* 1998 3 SA 785 (CC) paras 31, 43-48, 56, 59; Kentridge "Interpretation" in Chaskalson *et al Constitutional Law of South Africa* (Revision Service 5, 1999) 11-23 *et seq.*; Naudé "The value of life: a note on *Christian Lawyers Association of SA and others v Minister of Health and others* 1998 4 SA 1113 (T)" 1999 *SAJHR* 541.

or indeed as a black letter open norm. *Edouard v Administrator Natal*,<sup>154</sup> for example, refers to “collective welfare” as one principle operating in this context. Sub-principles of “collective welfare” already recognised in our law include the protection of the weak against oppression, the desirability of the free alienability of property and the desirability of freedom of trade.<sup>155</sup> All three, especially freedom of trade, can also be regarded as constitutional values, so that the legislator has indeed vested them with the highest authority.<sup>156</sup> In this sense any policy consideration which can be linked to a constitutional value would not fall foul of Dworkin’s test, as he allows judges to reflect political decisions of the past, but not oppose them.<sup>157</sup> As constitutional values have the highest authority in our law, one cannot relegate policy arguments based on constitutional values to second-rate arguments which rank somewhere below generally recognised underlying principles of contract law.<sup>158</sup> The only policy considerations that must be excluded, even in Dworkin’s own terms, seems to be those that conflict with the Constitution.

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<sup>154</sup> 1989 2 SA 368 (D) 379.

<sup>155</sup> On freedom of trade, see *Magna Alloys and Research (SA) (Pty) Ltd v Ellis* 1984 4 SA 874 (A). The desirability of the free alienability of property is partly informed by the fundamental principle (and “ethical postulate”) of individual autonomy, but also by the collective interest in increased income generated by property transactions. That individual autonomy is an ethical postulate has been pointed out by Lubbe 1991 *TSAR* 1 13.

<sup>156</sup> Freedom of trade, occupation or profession is expressly guaranteed in s 22 of the Constitution. The protection of individual rights and freedoms in the Bill of Rights shows the importance of protection of individual autonomy (Cameron JA in *Brisley v Drotzky supra* 35E par 94; Neels 1999 *TSAR* 484 485). As such the individualistic value of individual autonomy is also a community value, which should not be vilified and thrown out together with the bath water of extreme individualism.

<sup>157</sup> *Taking Rights Seriously* 87.

<sup>158</sup> Derek van der Merwe “*Iudicis est ius dicere*” 227 also considers that the Constitution’s imperative that the common law be developed to reflect the spirit or values of the Constitution relegates the importance of the nice distinction between legislative considerations of policy and judicial consideration of principle to “a secondary, if not wholly minor role.” See also Hart *The Concept of Law* 274 *et seq* for criticism on Dworkin’s objections to judicial law-making by reference to policy goals. Cf Phang “*The Concept of Law revisited*” 1995 *TSAR* 403 419 for a discussion of Hart’s views.

A precise hierarchy of principles and policy goals, with a promise of more predictability in application, seems an impossible ideal.<sup>159</sup> What can be said with certainty is that the values underlying the Constitution carry the highest authority. The more pervasive any (other) underlying principle of contract law, that is, the more rules underpinned by it, the more weight it probably carries in arguments about what rules should be. Past judicial referral to policy considerations and principle increases the weight carried by these arguments and, to some extent, allows a comparison of the weight allocated to different principles.<sup>160</sup> The more concretely a principle or sub-principle is stated, that is the more it approximates the concrete rules flowing from it, the more weight it carries in an argument on what (residual) rules should be. This is because the more general any concept, the more unfixed its meaning, the less it says. The spectrum of rules that are clearly inconsistent with a principle is conversely related to the breadth of the principle.<sup>161</sup> For example, “fairness” or “good faith” is so open-ended that mere references to them are bound to carry less weight than more concrete expressions thereof, such as the reasonable reliance principle or the principle of reciprocity or justice-in-the-exchange.<sup>162</sup> A generally stated reference to reasonable reliance is less weighty than its more concrete expression that a person who has reasonably acted to his detriment in reliance on another’s action, should be protected

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<sup>159</sup> Cf Esser 1972 *Archiv des civilistische Praxis* 97 113-114; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 223 and especially at 304; Hart *The Concept of Law* 275; Eisenberg “The Theory of Contract” 244.

<sup>160</sup> Cf Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 232.

<sup>161</sup> *Sinnentleerung* is said to take place: the wide concept becomes emptied of meaning.

<sup>162</sup> Cf Nieuwenhuis *Drie Beginselen* 7 who states that the weight of an appeal to the most general valuational concepts like fairness and good faith in a debate on the binding force of agreements is nil. He refuses to regard fairness and good faith as arguments, but sees them as “vooronderstellen argumenten” (presuppositions of arguments). See also Gordley *The philosophical origins* 234 (“The principle of fairness is thus like a clothes hanger on which one can hang a system of contract law after someone else makes it. It does not explain what the rules should be.”) Although I agree that the principles of fairness and good faith are very vague and should be fleshed out in argument, it is an overstatement to say that these principles carry no weight whatsoever. These principles are not so wide that no conduct or result could ever fall foul of them. Most people recognise gross unfairness or bad faith. If these principles are too wide to explain what rules should be, at least they are sometimes clear enough to show what it should not be, in other words to show up existing rules which must be changed for allowing clearly unfair results and bad faith conduct.

or compensated.<sup>163</sup> Although past application concretises constitutional values, underlying principles and policy considerations to some extent, they remain open-ended ideals.

Because contract law serves such vague and open-ended ideals, which are, moreover, often pulling in different directions, there is in fact no magic formula that guarantees an uniquely right answer for every situation.<sup>164</sup> More than one defensible optimum is often likely. The demands of each particular situation are also too variable for a prospective *in abstracto* ordering of principles and policy considerations into a hierarchy, to be of much help.<sup>165</sup> Each principle or criterion must be tested anew in every factual situation for its relevance, meaning and weight within that context.<sup>166</sup>

Zweigert & Kötz have said that:

“Most probably there will always remain in comparative law, as in legal science generally, let alone in the practical application of law, an area where only sound judgment, common sense, or even intuition can be of any help. For when it comes to evaluation, to determining which of the various solutions is the best, the only ultimate criterion is often the practical evidence and the immediate sense of appropriateness.”<sup>167</sup>

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<sup>163</sup> On the other hand, the more general principles are stated the more they equal generally accepted basic ethical postulates and requirements of justice. In a sense their persuasive power increase for that reason with respect to conduct or rules that unmistakably conflict with them.

<sup>164</sup> Cf Van Aswegen 1993 *THRHR* 171 193. Dworkin insists that there is always, in principle, “one right answer” (for example, in *A Matter of Principle* 119 *et seq* (part 2)) so that interpretation is not a pointless exercise. However, “it does not follow that we can always discover that answer, or even that we can ever discover it. Nor does it follow that when we have discovered it, we can be certain of that fact. We may be unwitting custodians of the truth, and we may be unwitting dupes of our firmest convictions.” (Mureinik “Dworkin and Apartheid” 186.) Dworkin admits that in instances of judicial discretion more than one answer is possible (*A Matter of Principle* 122). As the balancing of all relevant principles involves application of an open-ended standard, and therefore a discretion, more than one answer is possible. Dworkin’s one answer can in such a case be described as the fairest answer, perhaps an elusive ideal.

<sup>165</sup> Cf Esser 1972 *Archiv des civilistische Praxis* 97 114; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 224, 231-232.

<sup>166</sup> *Ibid.*

<sup>167</sup> 33.

A court's "immediate sense of appropriateness" is moreover not a guarantor of a correct solution. As stated before, one's immediate sense of appropriateness or "*regsgevoel*" also depends on one's knowledge of the policy considerations and principles at stake.<sup>168</sup> Moreover, as I will show more clearly below, a judge's "immediate sense of appropriateness" or *regsgevoel* does not always point to only one possible compromise between the conflicting ideals at stake.

This relative indeterminacy of the optimal solution should not stop us from establishing the range of fair solutions, and imagining and considering as many arguments and policy implications as possible on all sides to approximate the best solution for a legal problem.<sup>169</sup> Legal writers, with more time for reflection than courts, can play an important role in this regard. For their part, courts should set out fully the process of weighing of interests and principles.<sup>170</sup> An in-depth investigation of case law aimed at discovering the influence of principles and their concrete implications would be helpful to give guidelines as to development of rules at the hand of principles.

### **6 2 3 The demands of legal certainty**

The call to consider the tenability of default rules in the light of all the possibly relevant policy considerations and tenets of justice is bound to elicit the objection that it would lead to utter uncertainty and unpredictability of the law, which has already been described as unfair in itself.

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<sup>168</sup> As noted above, Van Aswegen 1993 *THRHR* 171 179 considers that the judicial hunch or legal sense ("*regsgevoel*") can be partially ascribed to actual experience of applying the law and ingrained knowledge of legal rules and standards.

<sup>169</sup> The provisionality of answers is a reality for all sciences, and is not an argument for giving up the pursuit (Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 315).

<sup>170</sup> Cf *Edouard v Administrator Natal supra* 379C-F; Lubbe 1990 *Stell LR* 13 *et seq*; Lubbe 1991 *TSAR* 1 14; Neels 1999 *TSAR* 484 487.

On the other hand, a measure of uncertainty is inevitable in a number of areas in law where standards of reasonableness and fairness apply. In the oft-quoted words of Botha J in *Rand Bank v Rubenstein*:<sup>171</sup>

A judge must often, in the exercise of his judicial function, move about in areas of relative uncertainty, where he is called upon to form moral judgments without the assistance of precise guidelines by which to arrive at a conclusion... The application of broad considerations of fairness and justice is almost an everyday occurrence in a court of law... I do not see why a judge should shirk from performing this kind of task, however difficult it may seem to be.<sup>172</sup>

The capacity for change in policy considerations should also not be overstated: many of the underlying principles of our contract law, which are simultaneously policy ideals, have been recognised for centuries in many legal systems. The capacity for change often relates rather to the “secondary value judgments”, namely the concretisation and balancing of principles.<sup>173</sup>

#### 6 2 3 1 *The role of precedent*

In any event, precedent plays a stabilising role to some extent. It should be presumed that the existing, authoritative position is fair.<sup>174</sup> The precedent system does not, however, preclude the recognition of exceptions to existing rules, by a process of distinguishing the instant case from the authoritative one.<sup>175</sup> A Provincial or Local Division of the High Court may also depart from its own prior decision if it is convinced that it was clearly wrong.<sup>176</sup> Due to the wide acceptance in case law that

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<sup>171</sup> 1981 2 SA 207 (W) 215E-F.

<sup>172</sup> See also Neels 1998 *TSAR* 702 704 for instances where reasonableness or fairness is a direct source of our law.

<sup>173</sup> Cf Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 315.

<sup>174</sup> Cf Van Aswegen 1993 *THRHR* 171 194-5, quoted with approval in *Payen Components SA Ltd v Bovic Gaskets CC supra* 476.

<sup>175</sup> Vorster “The bases for the implication of contractual terms” 1988 *TSAR* 161 181; Vorster *Implied Terms* 40-41, 158.

<sup>176</sup> See, for example, *Harris & Others v Minister of the Interior & another* 1952 2 SA 428 (A) 453; Hahlo & Kahn *The South African Legal System and its Background* (1968) 248; Kerr “Judges and

residual rules must be responsive to changing circumstances and notions of fairness, a prior decision on a residual rule could be wrong for the reason that certain important policy considerations were not brought to the attention of the court when the rule was originally laid down, or because the policy considerations upon which a rule was based no longer apply or is outweighed by contrary policy considerations.<sup>177</sup>

### 6 2 3 2 *Judicial restraint*

Judicial restraint in respect of adaptation of the law in this manner is always called for and to be expected.<sup>178</sup> Judges are and should generally be wary of making sweeping reforms in the form of general statements transcending the facts at hand as such decisions may have effects which the judge is unable to foresee and evaluate on the information before her.<sup>179</sup>

In a “hard case” apparently regulated by clear rules, a court must first establish the *prima facie* legal position according to precedent, and then consider whether it may justifiably depart therefrom.<sup>180</sup> Only clear injustice, unfairness or inappropriateness should justify departure from an existing rule,<sup>181</sup> although flagrant or extreme injustice

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academic lawyers on the relative values of justice and certainty should they conflict, and on the hierarchy of authority” 1985 *SALJ* 403-405.

<sup>177</sup> As residual contract law rules are affected by changing considerations such as notions of public policy, courts may depart from pre-Constitution decisions on these rules if they no longer reflect the values of society, including the constitutional values. See *Afrox Health Care Limited v Strydom supra* which holds that the principle of *stare decisis* still binds courts to apply pre-Constitution decisions on a common law rule, *unless* the rule conflicts with the Constitution or depends on changing considerations such as the *boni mores* or public interest.

<sup>178</sup> Cf Neels 1998 *TSAR* 702 706; Van der Merwe “*Judicis est ius dicere*” 229; Joubert 1992 *TSAR* 213 216.

<sup>179</sup> Bell *Policy Arguments in Judicial Decisions* 228-229.

<sup>180</sup> Neels 1999 *TSAR* 256 267.

<sup>181</sup> See the authorities cited by Neels 1999 *TSAR* 256 267 n 201 and 269 n 208. In the Netherlands, the concept “marginal testing” (*marginale toetsing*) is often used to denote the court’s function of excluding the application of a rule due to a conflict with the demands of reasonableness and justice. See Neels 1999 *TSAR* 256 269 and 1999 *TSAR* 484 484. With marginal testing is meant examination of the *prima facie* legal position for its consistency with fairness and reasonableness, but with restraint.

or inappropriateness should not be required.<sup>182</sup> Courts should therefore generally act with caution and circumspection before they extend, adapt or modify residual terms.<sup>183</sup> As stated earlier, detailed reasons for doing so must be given.<sup>184</sup> Legal certainty, we have seen, is an important ideal in contract law, especially in the context of commercial contracts.<sup>185</sup>

A more basic reason for requiring clear injustice for a departure from the present position is that opinions can legitimately differ on the fairness of rules, that is, on the proper balancing of opposing principles, policy considerations and ethical postulates.<sup>186</sup> When considered separately from the fairness ideal of legal certainty, there is often a spectrum of possibilities for “fair residual rules.”<sup>187</sup> Many of the residual terms of South African sales contracts, for example, could be both defended and criticised on “fairness” grounds. One could argue that it is unfair towards buyers that any consequential loss caused by a latently defective *merx* is not compensable by a non-expert, innocent seller, on the basis that the seller is in a better position to ascertain the defect and should bear the risk of selling a defective thing which may cause damages. On the other hand, one could defend our Roman law based rules due to the balancing of interests of innocent sellers and innocent buyers which it affords: innocent buyers will get some, but not unlimited compensation from innocent sellers. The qualification placed by *Kroonstad Westelike Boere Ko-operatiewe Vereniging Bpk v Botha*<sup>188</sup> on the so-called “Pothier rule” concerning the extended liability of traders for latent defects has been criticised by some as too narrow and unfair to consumers, and by others as too wide and unfair to traders.<sup>189</sup> In

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<sup>182</sup> Neels 1999 *TSAR* 256 270.

<sup>183</sup> See Neels 1999 *TSAR* 256 271. For this reason modification, for example by recognition of exceptions, should be attempted before a rule is totally “overruled.” As stated before (at n 175 *supra*), *stare decisis* does not prohibit recognition of exceptions to existing rules, whereas overruling a prior decision is only allowed under limited circumstances.

<sup>184</sup> See text at n 44 *supra*.

<sup>185</sup> Cf Neels 1999 *TSAR* 256 268.

<sup>186</sup> See also Neels 1999 *TSAR* 256 271; Van Dunné *Verbintenissenrecht* 20.

<sup>187</sup> Cf Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 316.

<sup>188</sup> 1964 3 SA 561 (A).

<sup>189</sup> See for example, *Langeberg Voedsel Bpk v Sarculum Boerderye Bpk supra* 568J, 570C-572H.

the same manner, one could legitimately argue the fairness *and* injustice of allowing an evicted buyer who has had the use of the *merx* for a long time to claim the purchase price instead of the decreased value of the *merx* at eviction.<sup>190</sup> Ultimately the law makes a choice, perhaps an arbitrary one, from the spectrum of fair solutions. The law should stick to that choice unless a new situation or new insight into the demands of fairness demands a modification.

### 6 2 3 3 “Sharp” norms versus open-ended standards

Certainty and predictability is promoted if courts laying down a new residual rule on the basis of policy considerations, fully flesh out those policy considerations, and in addition attempt to define the rule as precisely as possible so that its application in a certain case can be determined without a full examination of value or policy considerations.<sup>191</sup> If the innumerable considerations of policy which may turn out to be relevant to a specific dispute or rule, have to be canvassed in every single case, the resultant costs, waste of time and unpredictability may in itself be unfair to parties.<sup>192</sup> There is thus a policy argument in favour of “sharp” norms which can be regarded as provisional models of justice, that is, theories about a fair solution for a specific case, which realises the relevant policy considerations, and which may later be qualified or improved. This may be done if the rule no longer leads to a fair outcome in all cases

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<sup>190</sup> See especially *Alpha Trust (Edms) Bpk v Van der Watt* 1975 3 SA 734 (A) 742A-F where the court laid down this principle, but raised the possibility of our law developing towards recognition of an exception in the case of “rapidly depreciating assets.” This suggestion was rejected in two subsequent cases for reasons which appeal to “fairness” (see *Katzeff v City Car Sales* 1998 2 SA 644 (C); *Mdakane v Standard Bank* 1999 1 SA 127 (W)). That the buyer should have some compensation on eviction is clearly fair as the minimum result intended by contracts of sale is in fact that the buyer should have the ability to use the thing free from interference by third parties with stronger title. The spectrum of fair possibilities lies in the measure of that compensation. See also the debates of the Spanish scholastics on the fairness of *naturalia* of the contract of sale discussed by Gordley *The philosophical origins* 106 *et seq.*

<sup>191</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 110.

<sup>192</sup> Cf Neels 1999 *TSAR* 484 486; Van Huyssteen & Van der Merwe “Good faith in contract: proper behaviour amidst changing circumstances” 1990 *Stell LR* 244 247.

regulated by it, does not provide a clear answer or conflicts with other rules, principles or the needs of practice.<sup>193</sup>

In areas of the law where conflicting decisions and uncertainty abound, a refusal to comprehensively consider underlying principles and other policy considerations to arrive at a fair rule deepens legal uncertainty. In respect of preference contracts, I have shown that the system of precedents broke down repeatedly as contrary decisions were disregarded and wrong or questionable interpretations of prior decisions and historical authorities were relied upon.<sup>194</sup> This is therefore certainly an area of our law where the courts would be justified in examining the policy considerations in favour of the conflicting approaches comprehensively in the interest of legal certainty. As the basic rights and duties of the parties are steeped in controversy, a court considering “specific performance” of a preference contract would not be transcending the facts if they were fully to consider the policy considerations surrounding these contracts.

Of course, the benefits of stating law in the form of open-ended “standards” (as opposed to precise rules) must also be kept in mind when a new or qualified rule is laid down.<sup>195</sup> Open-ended standards allow and force judges to fully examine the equities and relevant policy considerations of each particular case, but “on a principled basis.”<sup>196</sup> Their formulation often includes their underlying policy justification or principle and therefore prevents mere automatic deductive subsumption under the concept.<sup>197</sup> Our law, for example, takes a principled stand in favour of specific performance, which brings some certainty and predictability, but

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<sup>193</sup> Van Aswegen 1993 *THRHR* 171 180-8, especially at 188 n 65; Lubbe 1991 *TSAR* 1 14; Van der Merwe, Lubbe & Van Huyssteen “The *exceptio doli generalis: requiescat in pace – vivat aequitas*” 1989 *SALJ* 235 241; Corbett 1987 *SALJ* 52 67-68; Van Zyl “Aspekte van billikheid in die reg en regspleging” 1986 *De Jure* 110 278; Neels 1998 *TSAR* 702 710; Smits *Het vertrouwensbeginsel* 64; Larenz *Methodenlehre der Rechtswissenschaft* (1975) 113.

<sup>194</sup> See chapter 2 *supra*.

<sup>195</sup> Cf Cockrell 1992 *SALJ* 40 43.

<sup>196</sup> They are well-suited to regulate factual developments which are unforeseeable at the time of their creation.

<sup>197</sup> Cf Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 285.

still allows an equitable discretion to refuse this on the basis of all the facts and relevant policy considerations. Usually a number of factors, sub-rules or categories of cases evolve that bring greater predictability to application of the open-ended standard.<sup>198</sup> Even where a choice is made to formulate a rule as a sharp norm, the purpose served by the rule must always be kept in mind in its application.<sup>199</sup> Concepts must continually be reevaluated for their appropriateness. Courts must always be aware of the danger that the rule was too widely stated, encompassing situations that are not properly regulated by it on a comparison of the situation and the justification for the rule. A suspicion that the rule is unfair, does not provide a clear answer, conflicts with other rules, principles or needs of practice, should not merely be dismissed by branding the situation at hand as a “hard case,” but should immediately raise questions as to the desirability of qualifying or amending the rule itself. Hard cases may disclose bad law.<sup>200</sup>

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<sup>198</sup> Esser 1972 *Archiv des civilistische Praxis* 97 117. See also Naudé & Lubbe “Cancellation for ‘Material’ or ‘Fundamental’ Breach: A Comparative Analysis of South African Law, the UN Convention on Contracts for the International Sale of Goods (CISG) and the Unidroit Principles of International Commercial Contracts” 2001 *Stell LR* 371 for identification of some factors informing application of the open-ended standard of “material breach” which justifies cancellation of a contract. A similar process has taken place in the law of delict where the *boni mores*, an open-ended standard, remains the ultimate criterion for unlawfulness, but specific sub-rules have concretised this criterion so that it is only really applied in new situations, borderline cases or to adapt existing rules. (Neethling, Potgieter & Visser *Delict* 4<sup>th</sup> edition (translated and edited by Knobel) (2001) 46 *et seq.*, especially at 48; Van der Walt & Midgley *Delict: Principles and Cases* (1997) 56; Boberg *The Law of Delict: Vol I Aquilian Liability* (1984) 56; *cf McMurray v HL & H (Pty) Ltd* 2000 4 SA 887 (N) 905.) See also Neels 1999 *TSAR* 256 263. In this context, many of the sub-rules are not in the form of factors, but comprise *Fallgruppen*, that is, groups of cases with a common characteristic. Once again, a balance between the apparently conflicting but interlinked aims of certainty and justice in the particular case should be attempted. If the open-ended concept is totally superseded by sub-rules on how it should be applied it no longer serves the goal of sensitivity to each particular case, and a new kind of formalism may develop. (*Cf Weber* 1992 *Archiv des civilistische Praxis* 516, 529, 535; Beater “Generalklauseln und Fallgruppen” 1992 *Archiv des civilistische Praxis* 82 *et seq.*)

<sup>199</sup> Esser 1972 *Archiv des civilistische Praxis* 97 112; *cf Larenz & Canaris Methodenlehre der Rechtswissenschaft* (1995) 312.

<sup>200</sup> Steyn “Oor die taak van regbank en regs fakulteit” 1967 *THRHR* 101 104 (“Hard cases disclose bad law”); Neels 1998 *TSAR* 702 711.

6 2 3 4 *The role of doctrine*

An attempt to fit a new rule or set of rules into the existing conceptual structure and to reconcile it with other rules and underlying principles of law, also has a stabilising effect.<sup>201</sup> On the other hand, courts and legal writers should guard against imbuing doctrine and concepts with a life of their own.<sup>202</sup> As noted before, all doctrine or concepts provide a provisional framework for understanding rules and should be adapted or supplemented when it does not adequately serve its purpose.<sup>203</sup> The purpose served by concepts and legal institutions in legal reality, including the needs of practice and the ideal of an individually and communally just solution, should always be kept in mind.<sup>204</sup> Default rules are in danger of becoming removed from reality and therefore unfair if they are considered to be simply logically deductible from existing concepts, such as "the legal nature" of a specific type of contract. Whether a solution fits with existing abstract theory is not a test for its suitability or correctness.<sup>205</sup> I therefore do not argue at all that a rule arrived at on the basis of policy considerations should be disqualified for not fitting the present conceptual structure or system. The system itself may have to be re-interpreted, developed or amended to make provision for the new rule. This possibility of system adaptation should always be kept open. However, in the interests of coherence and consistency, such adaptation should *as far as possible* be justified with reference to existing legal

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<sup>201</sup> Cf Van Aswegen 1993 *THRHR* 171 191, 195. Her comments were approved of in *Payen Components SA Ltd v Bovic Gaskets CC supra* 476. See also Lubbe 1991 *Stell LR* 131 135 n 34 ("sisteemkoherensie [is] van groot belang in dogmatiese denke"); Lubbe "Sessie in *securitatem debiti* en die komponente van die skuldeisersbelang" 1989 *THRHR* 485 461, 490; Neels 1998 *TSAR* 702 711, 717; Neels 1999 *TSAR* 484 490; Nieuwenhuis *Drie Beginselen* 4; Esser 1972 *Archiv des civilistische Praxis* 97 103-104.

<sup>202</sup> Corder & Davis *supra* 2 *et seq*; Lubbe 1991 *Stell LR* 131 135 *et seq*. On the limits of a doctrinal system, see further Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 317.

<sup>203</sup> See the text after n 31 *supra*.

<sup>204</sup> Lubbe 1997 *Acta Juridica* 246 271.

<sup>205</sup> Corder & Davis *supra* 2 *et seq*; Lubbe 1991 *Stell LR* 131 135 n 34; Esser 1972 *Archiv des civilistische Praxis* 97 111, 124. Esser 125 points out a number of well-known "doctrines" which do not fit nicely into existing conceptual structures, but which are nevertheless recognised due to the demands of practice and justice.

rules or principles underlying existing rules.<sup>206</sup> An attempt to harmonize the proposed solution and the existing conceptual structure enhances coherence and consistency, as the proposer is forced to consider and deal with the effect of the proposed solution on the system and to search for alternatives where it creates contradictions or inconsistencies in the system (whether this means an alternative new rule or qualification of the existing rules or concepts).<sup>207</sup> Inconsistency is unfair, as it is a basic postulate of justice that like cases must be treated alike.<sup>208</sup> Consistent and coherent rules are important to realise the central constitutional right of equality before the law.<sup>209</sup> Coherence in the legal system means that the system is understandable. This enhances predictability, and therefore fairness itself.<sup>210</sup> Doctrine as a conceptual system of rules or principles lessens complexity.<sup>211</sup> A conceptual system of rules and principles allows a systematic overview of the whole

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<sup>206</sup> Cf Dworkin *Taking Rights Seriously* 340. For an example of such an approach, see Lubbe 1991 *TSAR* 1 13 *et seq.* This is what judges usually do when faced with a gap in the law or “hard case” (Hart *The Concept of Law* 274).

<sup>207</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 14, 113; Esser 1972 *Archiv des civilistische Praxis* 97 104. Cf Martinek *Moderne Vertragstypen* 301; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 279-280. Time constraints and other limitations of the adjudication process (such as insufficient argument by counsel) may sometimes cause an “illogical” deviation from accepted doctrine in the name of fairness or policy considerations (an instance of hard cases making bad law). Commentators and courts in subsequent cases have the opportunity to consider reformulation of the rule or existing doctrine, or to show that the new rule is in fact consistent with underlying legal principles. In this manner legal certainty is enhanced (Lubbe 1991 *Stell LR* 131 133. Cf Joubert 1992 *TSAR* 213 218; Neels 1998 *TSAR* 702 713-714).

<sup>208</sup> Lubbe 1991 *Stell LR* 131 136; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 280, 113, 155. Cf Fuller *The Morality of Law* (revised edition 1969) 38-39.

<sup>209</sup> Section 9(1) of the Constitution, 108 of 1996.

<sup>210</sup> Mureinik “Dworkin and Apartheid” 195; Lubbe 1991 *Stell LR* 131 136, 139; Lubbe “Sessie in securitatem debiti en die komponente van die skuldeisersbelang” 1989 *THRHR* 485 461, 490; Lubbe “The Law of Contract in South Africa by RH Christie” 1981 *Acta Juridica* 177 178, 180; Lubbe 1997 *Acta Juridica* 246 246; cf Cockrell 1997 *Acta Juridica* 26 38, 39; Van Aswegen 1993 *THRHR* 171 195; Neels 1998 *TSAR* 702 717; Smits *Het vertrouwensbeginsel* 39; Fuller *The Morality of Law* (1969) 38-39; Zweigert & Kötz *Introduction to Comparative Law* 2.

<sup>211</sup> Lubbe 1991 *Stell LR* 131 136; Larenz *Methodenlehre der Rechtswissenschaft* (1975) 121; Bydliński *Juristische Methodenlehre und Rechtsbegriff* 2<sup>nd</sup> edition (1991) 111; Esser 1972 *Archiv des civilistische Praxis* 97 124.

body of rules, which makes it easier to arrive at the apposite rule for a problem.<sup>212</sup> A conceptual system rationalises law by norm reduction, which makes it unnecessary to repeat the whole body of rules and their justification in each situation.<sup>213</sup> Another function of the framing of concepts is to prevent those taking part in the debate on the appositeness of a solution from talking past one another.<sup>214</sup> As was noted before, a coherent system of contract law rules formulated in the abstract gives future courts the benefit of previous courts' experience and insights in attempting to reach a fair (and predictable) conclusion.<sup>215</sup> Although an uncodified system like ours allows considerable opportunity for deviation from the existing doctrinal structure,<sup>216</sup> coherent doctrine must be valued for its role in realising the fairness ideal.<sup>217</sup> As long as one guards against formalism by decrying claims of value-neutral deductive necessity from abstract concepts, and always consider the reality behind concepts, coherency and consistency are two worthy ideals.

The unpacking of policy considerations, underlying legal principles and fairness arguments relevant to a legal problem as well as doctrinal explanation of the proposed solution are likely to benefit from comparative legal study.<sup>218</sup> Even if the foreign jurisdictions studied do not clearly reveal the policy considerations, underlying principles and fairness arguments supporting their particular solutions, at least they posit model solutions that may surpass the local one,<sup>219</sup> and force the researcher to consider the principles and policies that might justify the foreign system's different solution. In this manner, comparative study encourages "the abandonment of deadly

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<sup>212</sup> Bydlinski *Juristische Methodenlehre* 111, 118. Ross *On Law and Justice* (1958) 171 points out that a statement of the law merely as a collection of rules "would be so unwieldy as to make it practically worthless." (Quoted by Lubbe 1997 *Acta Juridica* 246 265 n 152; 1991 *Stell LR* 131 136 n 39 and 1981 *Acta Juridica* 177 178.)

<sup>213</sup> Bydlinski *Juristische Methodenlehre* 111, 118; Martinek *Moderne Vertragstypen* 11.

<sup>214</sup> Nieuwenhuis *Drie Beginselen* 51.

<sup>215</sup> Smits *Het vertrouwensbeginsel* 46.

<sup>216</sup> Lubbe 1991 *Stell LR* 131 139.

<sup>217</sup> See also Lubbe 1991 *Stell LR* 131 136.

<sup>218</sup> Zweigert & Kötz *Introduction to Comparative Law* 4; 46.

<sup>219</sup> Zweigert & Kötz *Introduction to Comparative Law* 15.

complacency, and the relaxation of fixed dogma.”<sup>220</sup> A historical study of a legal rule or institution can do the same. It aids understanding of the justification for the present rule, and may also force abandonment of complacency about its correctness. This is the result when historical research reveals that authority hitherto relied on was wrongly interpreted, or that contrary historical authority exists, or that the rule’s rationale or underlying principle is no longer accepted in modern law.<sup>221</sup>

### **6 3 The preconditions for recognition of a specific type or sub-type of contract**

I agree with Vorster that a contractual arrangement need not be of common occurrence before a set of residual rules can be recognised for it and before it can therefore be designated or recognised as a “type” of specific contract. If there is a possibility that a type of contract may be concluded by other parties, it is helpful to treat the implication of terms for situations not provided for by the parties not as mere interpretation in the sense of identifying tacit terms, but as legal incidents so that “an exasperating goose chase after non-existent contractual meaning” and the resort to fictional intention is avoided in favour of a reasoned consideration of all relevant policy considerations and a fair balancing of any conflicting interests.

Are there any prerequisites for the formulation of classificatory features before a type of preference contract, or indeed any type of contract, can be recognised as such? In other words, is there any formula that the classificatory criteria of a type of contract must comply with? The classificatory criteria of the sub-types of preference contracts listed in the previous chapter are as yet unsettled.

The key question for the process of classification of contracts is to find a method according to which it can be determined which common characteristics of different contracts justify the application of the same norms to all contracts displaying those characteristics.<sup>222</sup> If classification occurs on the basis of too few characteristics, it

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<sup>220</sup> Zweigert & Kötz *Introduction to Comparative Law* 3; 21-22, 33-34.

<sup>221</sup> See further chapter 3 *supra*.

<sup>222</sup> Joubert *Die Finansiële Huurkontrak* 67.

may lead to injustice by reason of the application of inappropriate norms to some of the wide variety of transactions that may be gathered under a single contract type.<sup>223</sup>

The traditional methodological approach to the classification of contracts described in South African textbooks is to distinguish the various specific contract types from one another by a list of characteristic rights and duties, the so-called *essentialia* of the contract.<sup>224</sup> The classification process is generally portrayed as a simple matter of establishing whether the transaction under consideration contains all the *essentialia* or not.<sup>225</sup> The *essentialia* are generally regarded to comprise the purpose of the contract, that is, the most important result or economic end intended by the parties, as well as the most important terms on which there must be *consensus*.<sup>226</sup> For example, in the case of lease, the *essentialia* is an agreement that the one party will be granted the temporary use of an object against payment of a sum of money or a percentage of the proceeds of land leased, agreement on that sum of money and on the object to be leased. There must be agreement, or reasonable reliance of agreement on all these aspects for the contract to be a valid lease contract. The *essentialia* therefore do not only serve as classificatory characteristics, but also flesh out the certainty requirement in respect of each type of contract. The *essentialia - naturalia* approach to classification can be described as “conceptual”, as the question whether the contract can be classified as a particular type of contract is determined exclusively with reference to a closed number of elements making up the concept.

With regard to preference contracts, the question therefore arises whether the classificatory criteria for each sub-type identified must be formulated in terms of clear and definite *essentialia* before it can be validly recognised as a separate type of

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<sup>223</sup> *Ibid.*

<sup>224</sup> *LAWSA vol 5: Contract* First Reissue (1994) par 183; Lubbe & Murray *Contract* 416; Van Jaarsveld (ed) *Suid-Afrikaanse Handelsreg* 22; Joubert *General Principles of the Law of Contract* 23. See also Pothier *A Treatise on the Law of Obligations* translated by Evans sections 5-6.

<sup>225</sup> *Ibid.*

<sup>226</sup> Joubert *General Principles* 23.

contract with its own set of *naturalia* or residual rules.<sup>227</sup> Or may other and perhaps vaguer characteristics, which are not in the form of *essentialia*, be sufficient?

Consider, for example, Henrich's criterion for classifying transactions into the *Angebotsvorhand* construction, in terms of which the holder has a right to an offer upon a manifestation of a desire to sell. The classificatory criterion is that the preference contract predetermines the price at which the eventual contract may be concluded. This criterion is not in the form of an *essentiale*: it cannot be said that it is an essential term for the validity of preference contracts that the price at which the eventual contract may be concluded must be predetermined. Neither does it have a clear and direct bearing on the basic contractual purpose of this type of contract. Yet classifying the transaction into that type of preference contract on the basis of that criterion makes logical sense: if the preference contract predetermines the price, there is no justification for the grantor to enter into any negotiations with third parties whatsoever, and any manifestation of a desire to conclude the eventual contract should enable the holder to enforce performance of the eventual contract at the predetermined price. Should the fact that the classificatory criterion is not in the form of an *essentiale*, make it unacceptable for South African contract law?

### **6 3 1 The inadequacy of the *essentialia-naturalia* model**

The *essentialia-naturalia* model certainly has merit. It rationalises the law by norm reduction, which mediates understanding and application of the legal rules involved. This it does by identifying a set of residual terms (*naturalia*) applicable as a matter of course to transactions falling within the parameters of the *essentialia*, unless inconsistent with the parties' agreement.

It also facilitates a differentiated treatment to the separate types of contract identified in terms of this model, based on the typical party interests and purpose and special policy considerations involved. As such it provides a valuable corrective to the

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<sup>227</sup> The common denominator of or classificatory criterion for preference contracts as a genus has been described at 190 *supra*.

general principles of contract law that may not be suitable or sufficient to arrive at a fair solution for a conflict of interests in a specific case. The interrelationship between specific contract law rules and the general principles of contract law will be considered further in par 6 4 *infra*.

On the other hand, the *essentialia-naturalia* model is problematic. Firstly, its philosophical basis has been rejected. It stems from the Aristotelian metaphysical concept that each thing had a nature or essence, and changes when it changes its essence or substance but not when it changes its accidents.<sup>228</sup> The Aristotelian metaphysics of essences fell from favour in the seventeenth century.<sup>229</sup>

This concept of “essences” was applied to contracts by, amongst others, the medieval commentator, Baldus, who concluded that each type of contract had a nature or essence from which certain obligations followed “naturally”.<sup>230</sup> This justified reading terms into the contract, absent express provision by the parties. The nature or essence of an agreement depended on its end, and its natural terms were means to that end.<sup>231</sup> Thus a party who desired the end would also desire the means.<sup>232</sup> These ideas were later applied by the Spanish natural school (the Spanish scholastics), and through their influence, accepted by Roman Dutch writers such as Grotius.<sup>233</sup> Although Baldus and later writers claimed to find the distinction between *essentialia* and *naturalia* in Roman texts, they would not easily have arrived at it but for the influence of Aristotle and Thomas Aquinas who endorsed Aristotle’s view.<sup>234</sup>

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<sup>228</sup> Gordley *The philosophical origins* 61, 7. See also Gordley “Natural Law Origins” especially at 386. This metaphysical concept is related to the presupposition of Aristotelian philosophy that there was an implicit order in any just human society that the mind could discover, a notion developed by Thomas Aquinas, an ardent follower of Aristotle.

<sup>229</sup> Gordley *The philosophical origins* 111 et seq.

<sup>230</sup> *Ibid* 61 et seq.

<sup>231</sup> Gordley *The philosophical origins* 63.

<sup>232</sup> Gordley “Natural Law Origins” 418. In the sense that “a person who buys a car wants a camshaft even though he has never heard of one: He wants whatever the car must have to make it do what it is supposed to do.” (Gordley “Contract Law in the Aristotelian Tradition” 325.)

<sup>233</sup> Gordley *The philosophical origins* 102 et seq, especially at 105.

<sup>234</sup> Zimmermann *The law of Obligations* (1990) 234; Gordley *The philosophical origins* 102 et seq.

What cannot be faulted in this approach is the emphasis on the parties' purpose or end to define contract types used for classifying transactions and for the identification of essential and residual terms.<sup>235</sup> However, it is problematic as well. The notion that the implied *ex lege* terms "flow naturally from the essence of the contract" suggests incontestable immutability and a process of logical value-neutral deduction from the definition of the contract.<sup>236</sup> As argued above,<sup>237</sup> only some of the basic residual rules flow naturally or logically from the purpose or end, for example, the seller's duty to give undisturbed possession and to pay compensation on eviction. That obligation is in fact so intertwined with the basic contractual end that it is in fact invariable according to our law.<sup>238</sup> But "the devil is in the detail." Many of the more detailed

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<sup>235</sup> See also Gordley *The philosophical origins* 241; Kerr *Contract* 122. By contractual purpose is meant the main end which the parties seek to achieve. Their *ipse dixit* is of course not decisive in this respect. The contractual purpose is used to identify the body of rules applicable to the transaction. This body of rules includes the constitutive rules that determine whether it is a valid contract, most importantly, the essential terms on which there must be sufficiently certain agreement to give effect to the contractual end (*essentialia*). The emphasis on the contractual end is especially clear from the courts' treatment of simulated contracts or contracts misnamed in good faith. Courts will ignore apparent agreement on the *essentialia*, such as a purchase price and identification of an object as the *merx*, in the classificatory process, if it appears that the parties' actual purpose is to conclude a different type of contract. See *McAdams v Fiander's Trustees & Bell NO 1919 AD 207 223-224* "The question...always is what is the true nature of the transaction and this is not necessarily determined by what the parties may conceive the contract...to be. Parties may honestly think that they are entering in to a contract of purchase and sale, which turns out to be one of pledge.... There can be no contract of purchase and sale without the *animus emendi* on the part of the purchaser, and the *animus vendendi* on the part of the seller...." The court accordingly placed emphasis on the contractual purpose, namely to buy and to sell or rather, to provide permanent undisturbed possession and to ultimately transfer all the seller's rights in the property against payment, and not on the *essentialia*, which would include agreement on the price and property involved. See also Joubert *General Principles* 91 n 152 and cases there cited; *Vasco Dry Cleaners v Twycross* 1979 1 SA 603 (A); *Lubbe & Murray Contract* 106-107; *Kerr Contract* 122; *Christie Contract* 222.

<sup>236</sup> Cf Gordley "Natural Law Origins" 414.

<sup>237</sup> At n 190.

<sup>238</sup> See *Vrystaat Motors v Henry Blignaut Motors* 1996 2 SA 448 (A) 457D-E; *Alpha Trust v Van der Watt supra* 739A-B. According to the medieval commentators and Baldus, any provisions the parties made had to be consistent with the contract's end. The "essential" or "substantial" terms of a contract could not be taken away without a change in the essence of the contract. The essential terms are the "original root" of the contract, and the natural terms are "an extension of this root to the production of

aspects of the rules, for example, how much compensation is payable on eviction, is not logically preordained by the contractual end. In many instances there is rather a spectrum of possibilities of fair and reasonable consequential residual rules that are consistent with the ends of the parties.<sup>239</sup> The existing choice of rules should remain open to change when it is shown up as clearly inappropriate for the needs of practice or clearly unfair on a proper consideration of its current policy implications and the competing principles and policy ideals at stake.

That all *naturalia* do not flow naturally or logically from the *essentialia* is demonstrated by the fact that some residual rules can also attach to a subgroup of a nominate class of contracts.<sup>240</sup> In such cases, other factors influence which default rules apply. An example is the liability of manufacturers and certain traders for consequential damages arising from latent defects in goods sold by them, which goes beyond that of other sellers. The *essentialia* for contracts of sale concluded by these types of sellers remain the same. So does the main result intended by the parties, in other words, the contractual purpose. The fact that the seller is a manufacturer or trader is an additional criterion for certain legal consequences, which criterion is not in the form of an *essentiale*.<sup>241</sup> It is considerations of public policy that cause the identity of the seller to become a criterion for certain consequences of sales

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mere qualities” (Gordley *The Philosophical Origins* 63). One could therefore argue that a term excluding the seller’s obligation to compensate the buyer on eviction is inconsistent with the contract’s end.

<sup>239</sup> See further Kerr *Contract* 316. Cf Gordley “Natural Law Origins” 418. At 416, Gordley states that “The late scholastics typically responded by accepting the Roman solution as a rule of natural law and then devising an explanation for it... They often failed to show that this rule and none other follows from these principles and the nature of the contract in question.” That parties could set aside by express agreement the terms that would otherwise be read into their contract, also shows that “the means that would be most appropriate to obtain the contractual end might vary” (Gordley “Natural Law Origins” 418).

<sup>240</sup> Vorster *Implied Terms* 75.

<sup>241</sup> Joubert *Die Finansiële Huurkontrak* 69 states that South African contract law follows a conceptual model of specific contract types (that is, the *essentialia* – *naturalia* model) with the corrective of further differentiation within a particular type of contract.

contracts.<sup>242</sup> Therefore, insofar as the *essentialia* prepare the way for application of a set of norms, it is not the only prerequisite for application of norms. The problem with the conceptual approach is that it does not always bring to light the need for further differentiation on the basis of other characteristics not in the form of *essentialia*.<sup>243</sup> Therefore one must guard against the idea that an *essentialia* analysis supplies complete answers on the *ex lege* consequences of contracts.

A related danger of the *essentialia-naturalia* model is an overly wide definition of the contractual end as the major premise of classification, coupled with *naturalia* which reflect only one possible manner in which parties may intend to realise that end. This would result in the imposition of inappropriate *naturalia* upon parties whose precise purpose merits separate treatment. All juridical analysis is necessarily language based and may suffer unwittingly from overly wide or ambiguous definitions.<sup>244</sup> For example, a definition of a “right of first refusal” as a right to first refuse an offer to be made when the grantor wishes to contract, is ambiguous. It is true that in all cases the parties’ purpose are to grant the holder a preference above third parties, but the manner in which they intend to do this may differ. However, the *essentialia-naturalia* model, when uncritically applied, tends to force a transaction into the limited mould of one type of preference contract, simply because their purpose is to grant a preference to the holder generally, even though the exact way in which they understand that end may differ.

It is also difficult to state the different possible purposes of parties to preference contracts in the form of *essentialia* as a means of distinguishing them – the only term

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<sup>242</sup> Namely, that it is fair that an expert whose business it is to sell goods and who is able to insure against the risks of latent defects should be liable for all the consequences of latent defects in the goods, whereas in the case of a normal seller, it is fairer that the seller’s liability for latent defects is limited to price reduction or reimbursement of the purchase price. Another example is the requirement in agricultural leases that the lessor consent to cession or sub-letting whereas this is not required in the case of residential leases. Once again, public policy justifies this distinction.

<sup>243</sup> Joubert *Die Finansiële Huurkontrak* 69.

<sup>244</sup> On the limits of language, specifically in relation to first refusal contracts see for example Holmes *Corbin on Contracts: Vol 3 Formation of Contracts* revised edition (1996) § 11.4.

essential for the *validity* of all preference contracts is that the parties agree that the holder will be preferred above third parties in the contracting process.

Another limitation of the *essentialia* – *naturalia* model is that it creates the impression that only existing nominate contracts can have *naturalia* or residual rules.<sup>245</sup> However, even if a specific type of contract has never been recognised before, and therefore no *essentialia* exist, there remains a practical need for *ex lege* rules to be implied. In the case of such innominate contracts, parties are unlikely to provide for all possible consequences and circumstances. Therefore if controversies or circumstances arise for which the parties did not provide, the law must make a choice either to declare the contract invalid for uncertainty or to supply a rule. The courts will be loath to declare the contract invalid as the parties clearly intended to be bound. To always search for a "tacit" or "logical" term in such cases would amount to the imputation of fictitious consent and may lead to a failure to consider rationally all the relevant considerations of fairness and public policy at play. It would be better if the court would consider the parties' purpose and all relevant policy considerations and fashion an appropriate residual rule. If a similar contract is considered at a later stage, that court will have the benefit of the earlier court's deliberations. Vorster has correctly emphasised that whether a legal incident or *ex lege* term should apply to a particular kind of contractual relationship depends on the practical and policy considerations attending such a relationship and not whether the relationship is of common occurrence.<sup>246</sup> That legal incidents can be implied into innominate contracts is sometimes overlooked by writers on South African law precisely because of a fixation on the *essentialia* - *naturalia* model. For example, Van Rensburg, Lotz and Van Rhijn in *LAWSA* state that:<sup>247</sup>

"The main reason why contracts are divided into different types is to provide for those contingencies which the parties themselves did not specifically cover in their contract. Every type of contract has its own set of *essentialia* and *naturalia*; the *essentialia* serve as a criterion for the classification of a contract, and the *naturalia* determine the consequences of a contract in accordance with its classification. Not all contracts are capable of classification. If the

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<sup>245</sup> Vorster *Implied Terms* 75.

<sup>246</sup> Vorster *Implied Terms* 75.

<sup>247</sup> *LAWSA Vol 5 Part 1: Contract* par 183.

contract does not contain the *essentialia* of any of the recognised types of contract, it is known as an innominate contract whose consequences depend exclusively on its own specific terms.”

The last phrase of this statement is clearly incorrect. Apart from the fact that certain general default rules apply to all contracts, Vorster points out that “the law would be in a sorry state if the fact that a judge is unable to classify a transaction as belonging to one or other of the well-known nominate classes, renders him powerless to imply terms as legal incidents.”<sup>248</sup>

Moreover, as we have seen, even the originators of the *essentialia-naturalia* model did not regard the *essentialia* as criteria for classification of contracts, but rather as validity rules flowing from the contractual end or purpose. The latter was used to connect a transaction to the set of rules for a specific contract type. Once the transaction had passed the validity test set by the *essentialia*, the implied terms were attached to it as a matter of course.

Therefore, the authors’ statement that “the *essentialia* serve as a criterion for the classification of a contract, and the *naturalia* determine the consequences of contract in accordance with its classification” should not be accepted.

Exclusive recognition of an *essentialia – naturalia* model which regards *essentialia* as the only possible classificatory criteria seems an unrealistic and unacceptable doctrinal straitjacket on the development of new *ex lege* terms, whether for existing or new types of contract, where this is required by policy but where the determinants of their applicability cannot be formulated in terms of *essentialia*.<sup>249</sup> Fortunately, as I will show, our law does not exclusively rely on the *essentialia – naturalia* model for the recognition of specific contract types. This is another reason why the statement quoted from *LAWSA* is incorrect.

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<sup>248</sup> Vorster *Implied Terms* 158. Kerr *Contract* 123 confirms, at least, that if a new kind of class “becomes popular”, a new class of specific contract can be formed (with reference to Inst 3 24 3).

<sup>249</sup> A strict application of the conceptual approach could lead to an inappropriate treatment of mixed contracts if a court refuses to apply legal incidents or *naturalia* of both the main types for the reason that the mixed type does not comply with *all* the *essentialia* of both types (See Joubert *Die Finansiële Huurkontrak* 68; Leenen *Typus und Rechtsfindung* 131).

### 6 3 2 The *Typenlehre* as an alternative or supplementary methodological model for specific contract types

In Germany, dissatisfaction with the *essentialia – naturalia* model or conceptual approach to specific contract types<sup>250</sup> (and with conceptual subsumption generally) has led many academics to champion a different methodological model, the *Typenlehre*, through which to view and construct specific contract rules.<sup>251</sup> Although the *Typenlehre*, or “theory of types” has been applied to other areas of law,<sup>252</sup> most controversially in criminal law and the law of persons during the Nazi period,<sup>253</sup> this study will only consider its usefulness in the field of contract law, and specifically in respect of the analysis of specific contract types.<sup>254</sup>

Adherents of the *Typenlehre* criticise the traditional understanding of specific contract types as concepts in the strict sense.<sup>255</sup> When they speak of “concepts” they refer only to those terms or concepts that can be defined by a complete enumeration of exact characteristic criteria.<sup>256</sup> Only if the case under consideration agrees with the full list

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<sup>250</sup> Leenen *Typus und Rechtsfindung* 123, 143.

<sup>251</sup> Leenen *Typus und Rechtsfindung* 78; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 290 *et seq*; Martinek *Moderne Vertragstypen* 19 *et seq*; Bydlinski *Juristische Methodenlehre* 543 *et seq*, 136-137; Weber 1992 *Archiv des civilistische Praxis* 516 533 *et seq*; Joubert *Die Finansiële Huurkontrak* 70 at n 65 and authorities there cited. It is also sometimes called the *Typuslehre*.

<sup>252</sup> See Leenen *Typus und Rechtsfindung* 17 *et seq*.

<sup>253</sup> Cf Kuhlen *Typuskonzeption in der Rechtstheorie* (Schriften zur Rechtstheorie, Heft 66) (1977) 167 n 28 and 168 n 34 and authorities there cited.

<sup>254</sup> The typological method also has other applications in contract law. For example, policy considerations and general principles of contract law can also be regarded as “types” rather than concepts capable of simple logical subsumption. (Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 293). A full consideration of the *Typenlehre* merits a thesis on its own and I therefore restrict myself to its relevance to specific contract types.

<sup>255</sup> See generally Leenen *Typus und Rechtsfindung* 162 *et seq*.

<sup>256</sup> Bydlinski *Juristische Methodenlehre* 544.

of criteria can and must it fall under the concept (“only then and then always”).<sup>257</sup> Therefore compliance with the criteria is logically compelling and conclusive, a matter of simple logical subsumption.<sup>258</sup> For example, “a contract of sale” is a concept when it is defined in terms of the traditional set of *essentialia* for sales contracts. These *essentialia* either exist in a contract under consideration or they do not. If they all exist, the contract is a contract of sale. If not all exist, the contract is not a contract of sale.

The danger of conceptual subsumption is that when conceptual criteria are applied in isolation, a juristic fact such as a contract, may be subsumed under the concept, say a category of contract, whereas its particular attributes makes it a deviating contract.<sup>259</sup> To treat contract types as concepts may lead to formalism and a mechanical insistence upon a uniform construction of all contracts falling under a specific type, whereas freedom of contract allows variation and modification of the rights and duties within the type.<sup>260</sup> Such variation and modification may occur recurrently, requiring default rules for the sub-types which come to exist. Conceptual subsumption may hide the need for further differentiation within a contract type for policy reasons.<sup>261</sup> The tendency for conceptualism to lead to formalism results from formulation of the concept in abstract terms, so that it is “emptied of meaning” and the original purpose of the concept is forgotten. This tendency of concepts is called *Sinnentleerung* by

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<sup>257</sup> *Nur dann und immer dann.* Larenz *Methodenlehre der Rechtswissenschaft* (1975) 104; Bydlinski *Juristische Methodenlehre* 544.

<sup>258</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975)104.

<sup>259</sup> Leenen *Typus und Rechtsfindung* 152-153. Cf generally Lubbe “Die verpanding van vorderingsregte en die regsdogmatiek – quo vadis?” 1991 *Stell LR* 131 137 n 48 on the dangers of abstracting conceptualism; Wicke *Vicarious Liability* 244, 247; Esser 1972 *Archiv des civilistische Praxis* 97 109. Weber 1992 *Archiv des civilistische Praxis* 516 529 warns that an uncritical conceptual method may lead to judges becoming “subsumption automatons” (*Subsumptionsautomaten*).

<sup>260</sup> Cf chapter 2 *supra* where I suggest that some judges in South Africa have paid only lip service to the possibility of parties deviating from the “normal” construction of preference contracts, whereas they do not seriously consider the possibility of parties intending one of the conflicting constructions which they typify as “wrong” for lack of historical authority.

<sup>261</sup> Joubert *Die Finansiële Huurkontrak* 69.

adherents of the *Typenlehre*.<sup>262</sup> Abstract conceptualisation emphasises the commonality between related phenomena.<sup>263</sup> This may result in functional differentiation on the basis of the actual function or operation of the phenomena being overlooked.

Adherents of the *Typenlehre* distinguish concepts from types. They point out that there are various legal terms that cannot in fact be defined by a complete enumeration of exact, strictly conceptual characteristics, the application of which is a simple matter of logical subsumption. Rather, some terms are defined by indicative or symptomatic factors that do not necessarily all have to exist and which can exist to a greater or lesser extent (their characteristic criteria are therefore gradeable).<sup>264</sup> These terms are called *Typen* or types to distinguish them from concepts. Types are not defined, but described, in terms of the aforesaid indicative factors or concrete examples.<sup>265</sup> There is some variation on the meaning of the term *Typus* or type amongst proponents of the *Typenlehre*.<sup>266</sup> What is described here is the so-called classical *Typenlehre*.<sup>267</sup> The decision whether a specific factual situation, say a contract, falls within the type, benefits from a *Typenvergleich* or “comparison of types.”<sup>268</sup> That means that the contract considered should be compared with other

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<sup>262</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 282 *et seq*; Joubert *Die Finansiële Huurkontrak* 72-73. Cf Kuhlen *Typuskonzeption* 16.

<sup>263</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 287 (with reference to Hegel’s distinction between abstract and concrete concepts).

<sup>264</sup> Cf also Weber 1992 *Archiv des civilistische Praxis* 516 526: true “general provisions” (*Generalklauseln*) are so widely or vaguely defined that they do not allow simple subsumption in terms of which the major premise is the legal norm and the minor premise the factual situation. Such subsumption presupposes that the norm must contain criteria which are sufficiently exact, which is not the case with general open-ended provisions. The general provisions can therefore be regarded as “types.”

<sup>265</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1975) 297; Bydlinski *Juristische Methodenlehre* 544.

<sup>266</sup> Bydlinski *Juristische Methodenlehre* 544; Weber 1992 *Archiv des civilistische Praxis* 516 533.

<sup>267</sup> See Bydlinski *Juristische Methodenlehre* 544.

<sup>268</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 111, 181; Leenen *Typus und Rechtsfindung* 184; Bydlinski *Juristische Methodenlehre* 548 *et seq*; Joubert *Die Finansiële Huurkontrak* 80.

contracts that were denoted as “typical” or “a-typical” in previously decided cases.<sup>269</sup> The question is whether the typical characteristics of the type are present to such a degree that the factual situation as a whole corresponds to the type.<sup>270</sup> Not all the typical characteristics need therefore be present for, say, a transaction to fall under the type. One must look to the total picture, the *Gesamtbild*.<sup>271</sup> There are no completely

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<sup>269</sup> *Ibid.* This may perhaps suggest that the typological method is the same as the *Fallgruppen* method of identifying groups of cases reflecting the application of an open-ended concept (as to which see Weber 1992 *Archiv des civilistische Praxis* 516 517 *et seq*; Beater 1992 *Archiv des civilistische Praxis* 82 *et seq*). Obvious examples of *Fallgruppen* are the sub-rules regarding delictual unlawfulness which have concretised through application of the open-ended *boni mores* standard. Actually the typological method differs from the *Fallgruppen* method. Most importantly, typological thinking remains focused on the unity of the idea (*Rechtsgedanke*) or purpose underlying the legal norm or institution, whereas *Fallgruppen* focuses on different categories of cases falling under the norm (Weber 1992 *Archiv des civilistische Praxis* 516 534). If one translates *Fallgruppen* terminology to *Typenlehre* terminology, the open-ended concept itself amounts to a “type”, and the *Fallgruppen* to sub-types. However, many *Fallgruppen* could indeed be described conceptually in terms of clear and definite markers, and are therefore not types but concepts. (*cf* Weber 1992 *Archiv des civilistische Praxis* 516 531-532). Very often they become conceptual sub-rules, which are inconsistent with the typological method. Instead, *Fallgruppen* are more closely related to the decided cases that are used to facilitate application of the factors describing the type (that is, through a *Typenvergleich*). However, *Fallgruppen* presupposes groups or categories of cases covered by the open concept. As previous cases facilitating a *Typenvergleich* are not always classified or indeed classifiable into different *groups* of cases, but remain focused on elucidating the type itself, *Typenvergleichung* cannot be perfectly equated with the identification of *Fallgruppen*. Identifying *Fallgruppen* and a *Typenvergleich* serve the same function, however: elucidating an open-ended, vague concept. See Weber 1992 *Archiv des civilistische Praxis* 516 533 *et seq* for criticism on the *Fallgruppen* method; he considers that it often impairs the flexible value judgments intended by adoption of the open-ended concept. His criticism is more apposite to a codified system where the legislator specifically creates open-ended concepts. In any event, identifying factors and *Fallgruppen* for application of an open-ended standard, if not seen as a *numerus clausus*, does much to ensure that all the relevant circumstances and policy considerations are taken into account and makes the result more predictable (Beater 1992 *Archiv des civilistische Praxis* 82 84, 87; *cf* Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 113-114). Once again a balance must be struck between the demands of legal certainty and the desirability of flexibility if the open-ended concept is to serve its purpose.

<sup>270</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 109; Bydlinski *Juristische Methodenlehre* 544; Leenen *Typus und Rechtsfindung* 28, 34 *et seq*.

<sup>271</sup> Leenen *Typus und Rechtsfindung* 123. For a practical example, see Leenen *Typus und Rechtsfindung* 143. Bydlinski *Juristische Methodenlehre* 549-550 is more in favour of the comparison

clear, fixed borders between cases that do fall within the type and others which do not.<sup>272</sup> Types are therefore more “open” than concepts. The application of the type requires a value judgment or judgment based on social experience and views in the marketplace.<sup>273</sup> The law builds the type with reference to the consequences connected to it. Therefore, when considering whether a concrete example falls under the type, one must look to the purpose why the law wants these consequences to attach to this type.<sup>274</sup> Types and typological thinking therefore force one who applies the law to always consider the purpose of legal conceptualisation and the appropriateness of a rule’s legal consequences.<sup>275</sup> The recognition of types in addition to concepts is necessary because the exact characteristics of concepts do not always cover all the cases intended by the purpose of the rule or sometimes cover more than intended by the purpose.

A factual situation that displays all the typical characteristics of the type is sometimes called a “normal type.”<sup>276</sup>

The *Typenlehre* also recognises that in commercial reality legal institutions, such as specific contract types, are not always uniform figures, but that “sub-types” and mixed types come to exist.<sup>277</sup> It allows the creation of a range of types

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of the individual characteristics of the type, even though they do not all exist, than of an “intuitive *Gesamtbild* comparison.”

<sup>272</sup> Bydlinski *Juristische Methodenlehre* 544.

<sup>273</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 104, 107; Leenen *Typus und Rechtsfindung* 138; Martinek *Moderne Vertragstypen* 19.

<sup>274</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 109; Martinek *Moderne Vertragstypen* 13; Bydlinski *Juristische Methodenlehre* 545; cf Bydlinski *Juristische Methodenlehre* 552.

<sup>275</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 110; Leenen *Typus und Rechtsfindung* 64 *et seq.*, 138, 150 *et seq.* Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 314 calls the *Typus* a *funktionsbestimmte Begriff*, that is, a concept determined by its function, which therefore refers back to its function. As such it is richer in content than comparable abstract concepts.

<sup>276</sup> See, for example, Leenen *Typus und Rechtsfindung* 96.

<sup>277</sup> Martinek *Moderne Vertragstypen* 20 *et seq.*, with examples; Leenen *Typus und Rechtsfindung* 133 *et seq.*; Bydlinski *Juristische Methodenlehre* 552.

(*Typenreihen*).<sup>278</sup> *Typenreihen* are based on the reality that types may blend into each other due to the variability of their elements. The borders between different types may therefore be fluid.<sup>279</sup> In a range of types (*Typenreihe*), closely related but still distinguishable types are strung together in such a manner that their common characteristics and distinctions and thereby also the transitional manifestations become clearer.

The typological method therefore gives expression to the complexity of the relationships which the law must deal with.<sup>280</sup> It denounces the simplistic solutions which legal concepts with clear and definite markers offer, as such concepts satisfy lawyers' love for principled clarity, but sometimes unfairly thwart parties' expectation of the legal position in a given factual situation.<sup>281</sup> It aims to deliver an adequate description of legal phenomena to be considered in order to correctly reflect legal reality and to exclude conceptual sham problems.<sup>282</sup>

However, concepts and types are not stark opposites and may show some overlap.<sup>283</sup> A concept can have one open characteristic, similar to a type. On the other hand, a type can contain some essential characteristic apart from other merely symptomatic ones and thereby approach a concept.<sup>284</sup> The description of a type can be intended as

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<sup>278</sup> Leenen *Typus und Rechtsfindung* 138; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 298.

<sup>279</sup> Interestingly, Kriek J in *Van Rensburg v City Credit (Natal) (Pty) Ltd* 1980 4 SA 500 (N) 506F-G seems to approach typological thinking when he proposed to merge the three steps laid down in *Delmas Milling Co Ltd v Du Plessis* 1955 3 SA 447 (A) on the use of evidence in interpretation. He regarded the three steps as merging into one "like the colours of a spectrum with diffused borders between the different colours." This would be an apposite description of a spectrum of types with fluid borders.

<sup>280</sup> Cf Leenen *Typus und Rechtsfindung* 137-139; Wicke *Vicarious Liability* 41.

<sup>281</sup> Cf Larenz *Methodenlehre der Rechtswissenschaft* (1975) 443ff; Leenen *Typus und Rechtsfindung*; Bydlinski *Juristische Methodenlehre* 109ff and especially at 543ff.

<sup>282</sup> Leenen *Typus und Rechtsfindung* 137, 162.

<sup>283</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 111. Critics of the *Typenlehre* such as Bydlinski *Juristische Methodenlehre* 545 also emphasise this.

<sup>284</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 111. See the text at n 294 *supra* for an example.

a preliminary stage in the process of the building a concept that correctly reflects legal reality.<sup>285</sup> Larenz, a proponent of the *Typenlehre*, recognises that in the interest of certainty, a legal term must be defined as precisely as possible.<sup>286</sup> Therefore where a lawgiver formulates rules by using a concept as opposed to a type, the adherents of the *Typenlehre* will have no problem with this if the interpreter of the rules interprets the concept teleologically.<sup>287</sup> Adherents of the *Typenlehre* recognise that where a specific transaction does not differ at all from the generally recognised normal type there is nothing wrong with using the traditional conceptual method.<sup>288</sup> However, where it is not possible to define a legal term as a concept that can be applied without a value or policy judgment, it is inevitable that a legal institution must be formulated as a type.

Applied to contract law, the *Typenlehre* defines contract types not as concepts (*Begriffen*) with defined *essentialia* as markers, but rather as *Typen* with characteristics which may be formulated more vaguely.<sup>289</sup> These characteristics are related to the end or purpose of the contract.<sup>290</sup> The “total impression” of the contract (*Gesamtbild*) is taken into account in typifying the contract. This also means that the legal rules applicable to a type of contract may be applied to a particular transaction to a lesser or greater degree where this is possible and meaningful.<sup>291</sup> The *Typenlehre* emphasises that contractual norms are open and subject to change. Specific contract types are not fixed immutable concepts – new types may develop and further differentiation within a known contract type may be required for policy reasons and to reflect commercial reality.

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<sup>285</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 111.

<sup>286</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 110.

<sup>287</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 111; Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 312; cf Bydlinski *Juristische Methodenlehre* 112.

<sup>288</sup> Leenen *Typus und Rechtsfindung* 96 *et seq.* I use the term “normal type” to refer to the type of specific contract most commonly recognised, whose residual rules are regarded as the standard residual rules for the contract type.

<sup>289</sup> See the authorities in n 251 *supra*.

<sup>290</sup> As such, they emphasise the centrality of the contractual end or purpose that initially gave rise to the *essentialia-naturalia* model and from which the *essentialia* and *naturalia* of contracts is supposed to flow.

<sup>291</sup> *Ibid.*

Types of legal relationships, including specific contract types, are described as “legal structure types” which originated in legal reality, as these types concern the structure of legal entities.<sup>292</sup>

The typological approach is not unknown to South African contract law. South African courts have correctly followed a typological approach to determine whether a contract is a contract of service as opposed to a contract of services between a principal and independent contractor.<sup>293</sup> The only necessary requirements (*essentialia*) for a contract of service are agreement on performance of some kind of work and payment.<sup>294</sup> However, these criteria are not sufficient to distinguish the relationship from that between a principal and independent contractor. A number of additional factors indicate the existence of a contract of service in the context of vicarious liability of an employer.<sup>295</sup> There is no decisive criterion.<sup>296</sup> The dominant impression is important. *Indicia* for the contract of service include the degree of control by one party over the other, the nature of the work, the freedom of action, the manner of payment, the magnitude of the contract amount, the power of dismissal, the obligation to perform the duties personally, ownership of the work facility, the place of work, duration of employment and intention of the parties, amongst others.<sup>297</sup> Some of these *indicia*, such as the control of the one party over the other, are clearly

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<sup>292</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 295; Leenen *Typus und Rechtsfindung* 78.

<sup>293</sup> Wicke *Vicarious Liability* 40 *et seq*; 248 *et seq*. This is especially clear from the decision in *Minister van Polisie en 'n Ander v Gamble en 'n Ander* 1979 4 SA 759 (A) especially 765 (“Control is not the sole *indicium*, but merely one of the *indicia*, albeit an important one”). See also *Mtewa v Minister of Health* 1989 3 SA 600 (D) 606; *cf Smit v Workmen's Compensation Commissioner* 1979 (1) SA 51(A) 53-54. See Wicke *Vicarious Liability* 41 for details of later decisions which, in conflict with previous decisions and wrongly in his view, still appear to posit control as a necessary requirement, and not only as an important *indicium*. The contract of service is also usually mentioned as an example of a type by German proponents of the *Typenlehre*. See for example, Leenen *Typus und Rechtsfindung* 148 *et seq*.

<sup>294</sup> Wicke *Vicarious Liability* 40.

<sup>295</sup> Wicke *Vicarious Liability* 248.

<sup>296</sup> *Ibid*.

<sup>297</sup> *Ibid*.

gradable characteristics, which can exist to a greater or lesser degree. Their application requires a value judgment and benefits from comparison with earlier decided cases (*Typenvergleich*).

The courts' approach towards simulated contracts also shows similarities with the typological method. Courts often ignore the fact that ostensibly a contract contains the *essentialia* of a certain type of contract, if the circumstances and exceptional *accidentalia* of the contract show that they actually intended to conclude another type of contract.<sup>298</sup> In such cases the court therefore considers the “total picture”, the *Gesamtbild* of the contract. In South African law, mixed contract forms are also sometimes grouped under a specific contract type in terms of the rather vague criterion of the intention of the parties (for which read contractual purpose) rather than the existence of the *essentialia* of that contract type.<sup>299</sup> Sometimes the courts refuse to classify mixed contracts under the crystallised contract types, and rather combine (some of) the *naturalia* of the different contract types at stake in order to achieve a fair result which accords with the purpose of the parties, or are prepared to recognise a distinct “new” contract type with its own set of residual rules.<sup>300</sup> A *Typenvergleich* or comparison of types often occurs in decisions on open, vague concepts, when courts compare the facts of the case before them with the facts of other decided cases which have been held to fall under or outside the concept.<sup>301</sup>

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<sup>298</sup> Joubert “Die regsaaard van finansiële huurkontrakte” 1989 *TSAR* 568 579.

<sup>299</sup> *Cf Wastie v Security Motors* 1972 2 SA 129 (C) on the test for establishing whether a contract is one of sale or exchange.

<sup>300</sup> See for example *Zulu v Van Rensburg* 1996 4 SA 1236 (LCC) 1260-1262. In this case the court refused to apply the “absorption theory” that would demand that the institution of labour tenancy be classified as either a lease or a service contract, but preferred the “combination theory” in terms of which the *naturalia* of the two contract types are combined. Alternatively it was prepared to accept the “*sui generis* theory” in terms of which labour tenancy is a separate type of contract with its own *naturalia*.

<sup>301</sup> *Cf* for example, the case law on negligent driving. The important concept of “material breach” is also approached typologically: no clear and definite markers are spelled out, but rather vague tests such as “the breach goes to the root of the contract.” *Cf* also *Laconian Maritime Enterprises Ltd v Agromar Lineas Ltd* 1986 3 SA 509 (D) 524-530 according to which the *lex causae* of a contract is determined with reference to a number of factors such as the place of conclusion of the contract, of performance thereof and the domicile to the parties. See Neels 1999 *TSAR* 256 263-264. Another

The typological method is also applied in other areas of our law. The concept “real right” is actually a type. A list of typical characteristics can be identified for a “normal” or “ideal” type of real right, but not all real rights need necessarily display all these characteristics.<sup>302</sup> Categories of real rights have crystallised, but they do not constitute a *numerus clausus*.<sup>303</sup> The identification of new types of real right benefits from a study of past case law.

Proponents of the *Typenlehre* in Germany also emphasise that the *Typenlehre* is not an alternative methodological model to that used by the courts, but merely describes what courts are already doing.<sup>304</sup> It is also the necessary result of contractual freedom that legal traffic will not remain content with ideal types, but bring forth new types of contract. However, supporters of the *Typenlehre* plead that courts must be aware that they are proceeding typologically, so that in classifying, say, contracts, they do so

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approach encountered in international private law is to designate a “default” rule as to the applicable law, namely the *lex loci solutionis*, but allow deviation when a variety of circumstances show that there is a closer connection with another legal system making it fair to apply that law (Neels 1999 *TSAR* 256-264-265).

<sup>302</sup> See especially Van der Merwe *Sakereg* 2<sup>nd</sup> edition (1989) 63. Van der Merwe bases his idea that there is an ideal or normal type of real right, but that not all real rights need display all the characteristics of the real right, on the view of Meijers *De Algemene Begrippen van het Burgerlijk Recht* (1948) 266-268. However, the list of characteristics mentioned by Van der Merwe are not in fact the criteria generally used for recognition of new types of real rights in respect of land. In practice, two broad criteria are used. First, the intention of the creator of the right must be to bind not only the present owner of the land, but also her successors, and second, the nature of the right must be such that registration would cause a “subtraction from the *dominium*” (*Cape Explosive Works Ltd and Another v Denel (Pty) Ltd and Others* 2001 (3) SA 569 (SCA); *Erlax Properties (Pty) Ltd v Registrar of Deeds and Others* 1992 (1) SA 879 (A); Van der Merwe *Sakereg* 70 *et seq*). Besides the fact that it is vaguely stated, this latter test is not very helpful as personal rights can also limit an owner’s free capacity to use and alienate his property.

<sup>303</sup> Van der Merwe *Sakereg* 63.

<sup>304</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 192; Bydlinski *Juristische Methodenlehre* 550.

on the basis of a justified purposive classification<sup>305</sup> and not just on the basis of a simple, logical, purely conceptual subsumption.<sup>306</sup>

The *Typenlehre* has long been subjected to criticism in Germany.<sup>307</sup> The uncertainty which it brings, “the unverifiability of its results”, is the main objection.<sup>308</sup> The objection is that it is uncertain how to establish which are typical and which are atypical cases.<sup>309</sup> In response, supporters of the *Typenlehre* point out that the actual purpose of the parties is used to decide whether the contract falls under a specific type. Moreover, a measure of certainty can be obtained by comparing the case under consideration to other cases already decided on the basis of the type. This is the so-called *Typenvergleich* or “comparison of types”, which our courts often use. Each decision elucidates or “concretises” the type, although the process is never at an end.<sup>310</sup> As more cases are decided on the basis of the type, so it becomes easier for later courts to compare a factual case with what has been decided before.<sup>311</sup>

Moreover, Joubert, who also criticises the *Typenlehre* on this basis, pleads for differentiation within contract types on the basis of other markers than *essentialia*, which arguably results in as much uncertainty as the *Typenlehre*, as he does not give fixed rules for when further differentiation may be appropriate.<sup>312</sup> In any event, certainty in the law cannot be regarded as a higher goal than the appropriateness of legal norms.<sup>313</sup> Norms that are out of step with a complex commercial and legal reality only create a false sense of legal certainty.<sup>314</sup> If the conceptual approach cannot adequately describe and provide for specific contract rules which are used and

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<sup>305</sup> See n 290 *supra*.

<sup>306</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 192.

<sup>307</sup> Joubert 1989 *TSAR* 568 578 and authorities there cited; Kuhlen *Typuskonzeption* 169. Cf also Bydlinski *Juristische Methodenlehre* 545.

<sup>308</sup> *Ibid*; Joubert *Die Finansiële Huurkontrak* 73.

<sup>309</sup> Joubert *Die Finansiële Huurkontrak* 73.

<sup>310</sup> Larenz *Methodenlehre der Rechtswissenschaft* (1975) 111, 181; Leenen *Typus und Rechtsfindung* 184; Joubert *Die Finansiële Huurkontrak* 80.

<sup>311</sup> Cf Bydlinski *Juristische Methodenlehre* 548.

<sup>312</sup> Joubert *Die Finansiële Huurkontrak* admits this at 80.

<sup>313</sup> Leenen *Typus und Rechtsfindung* 133. See par 6 2 *supra*.

<sup>314</sup> See the text after n 40 *supra*.

necessary in practice, whereas a more flexible model like the *Typenlehre* can, there is no point in keeping to the conceptual model only because it apparently provides legal certainty.

Another criticism against the *Typenlehre* is that a focus on the “total picture” of a specific contract type may lead to the application of inappropriate rules.<sup>315</sup> The argument is that, by reason of the *Gesamtbild* “test”, a transaction may inappropriately be classified as a certain type so that all the rules of that type apply even though not all the *essentialia* of the contract type exist.<sup>316</sup> However, proponents of the *Typenlehre* would respond that the emphasis on the teleological application of law central to the typological approach would prevent the inappropriate application of rules.<sup>317</sup> They do not state that as long as the total picture of a mixed contract approximates a specific type of contract all the rules of that contract type should automatically apply. They would not force all contracts into one specific type of contract just because the contract complies with some of the *essentialia* of such a contract type, nor necessarily combine existing categories.<sup>318</sup> Rather they would ask in each and every case, whether it is sensible and appropriate to apply a specific rule to a particular transaction or whether a new type with elements of other existing contracts or new rules must be recognised in the specific case.<sup>319</sup> This is very clear from Leenen’s example of contracts in terms of which an entrepreneur undertakes to install and stock vending machines in a hotel. He does not ask whether the contract as a whole can be seen as lease of a piece of ground to the entrepreneur, nor whether the contract as a whole should be regarded as a partnership, but rather suggests that due to the particular purpose of the parties, the contract should not be regarded as either lease or partnership.<sup>320</sup> Joubert’s statement that the *Typenlehre* would only allow a material deviation to result in the contract falling outside a specific type,<sup>321</sup> is therefore clearly wrong.

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<sup>315</sup> Joubert *Die Finansiële Huurkontrak* n 102 *in fine*.

<sup>316</sup> *Ibid*.

<sup>317</sup> See for example Leenen *Typus und Rechtsfindung* 164.

<sup>318</sup> Leenen *Typus und Rechtsfindung* 167, 188.

<sup>319</sup> Larenz 189; Leenen *Typus und Rechtsfindung* 171 *et seq*.

<sup>320</sup> Leenen *Typus und Rechtsfindung* 154.

<sup>321</sup> Joubert *Die Finansiële Huurkontrak* 70.

Joubert's major argument for ultimately rejecting the *Typenlehre* for South African contract law<sup>322</sup> appears to be that the typological method allows the direct application of existing legal rules to new contract types, on the basis that the "total picture" of the contract requires this. This, says Joubert, may lead to more extensive and unhampered legal development and leave more scope for a "manipulated application of legal norms."<sup>323</sup> By contrast, he considers that the conceptual method (the *essentialia - naturalia* model with further differentiation within contract types as necessary) leads to the indirect, analogous application of existing contract law rules to new types, which amounts to overt development of law, which judges will therefore necessarily do incrementally and with great circumspection and subject to the rules for creating new law.<sup>324</sup> With respect, this argument is not persuasive. As to the possibility of manipulation, Joubert does not clearly show why an analogous application of rules relating to a (different) type of contract would be less open to manipulation than a "direct" application of rules. It is not clear at all that a so-called "direct" application of appropriate norms in terms of the *Typenlehre* would differ at all in practice from an "analogous" application of appropriate norms. What would be appropriate is not clearer in the one case than in the other. Nor does Joubert clearly explain why courts that apply norms by analogy would show more restraint than judges who apply norms on the basis of the typological method. In any event, as new forms of contract develop, coherence may make it desirable that courts consider what residual rules would be suitable for that type of contract by considering the construction of the contract in its entirety, whether the conceptual or typological method is followed, which may indeed result in more than "incremental" change to the law. It is also not clear why development of law under the conceptual approach would be more overt than under the typological approach. The *Typenlehre* itself pleads for an overt development of law taking into account the appropriateness of the consequences of default rules in the light of the recurring economic purpose of the contract type.

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<sup>322</sup> Joubert *Die Finansiële Huurkontrak* 80.

<sup>323</sup> Joubert *Die Finansiële Huurkontrak* 76-80.

<sup>324</sup> *Ibid.*

Some critics of the *Typenlehre* are of the opinion that contract “types” are simply classificatory concepts that are vague or open, with their elements not connected conjunctively.<sup>325</sup> Such open-ended standards or concepts that confer a judicial discretion have long been recognised.<sup>326</sup> It has long been recognised that such discretions must be exercised for the purpose for which they are conferred, in accordance with relevant principles and with due regard to all relevant factors.<sup>327</sup> Therefore they imply that the *Typenlehre* does not add anything to the methodology of law.<sup>328</sup> Some feel that the *Typenlehre* is largely a restatement of the need for the teleological application of law, which can also apply to concepts,<sup>329</sup> and a confirmation of the usefulness of looking at previously decided cases when applying open norms.<sup>330</sup> They stress that there is nothing wrong with a system of concepts as opposed to types, as long as judges are prepared to recognise new contract types and fashion new rules for mixed types.<sup>331</sup> For them the choice lies not so much between types and concepts as between overt and covert changes to the law.<sup>332</sup>

In my opinion the choice between treating all specific contract types as “types” rather than “concepts” is not as important as heeding the warning of the *Typenlehre* against a formalistic treatment of specific contract types, blind to the demands of the users of these contract types, the complex results which they may intend and the need to differentiate between different sub-types on the basis of policy considerations and commercial reality. In a sense the essential point of the *Typenlehre* is not so much to plead for the use of types rather than concepts, but to plead for typological thinking, which amounts to teleological or purposive thinking, as opposed to purely conceptual, formalistic thinking about contract types, and to emphasise the need for the use of open concepts which require value judgments in addition to sharp, closed concepts in

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<sup>325</sup> Kuhlen *Typuskonzeption* 162, 168; cf Bydlsinski 545.

<sup>326</sup> Cf De Vos & Kelbrick 2000 *THRHR* 537 540. See also at n 195 *supra*.

<sup>327</sup> De Vos & Kelbrick 2000 *THRHR* 537 540.

<sup>328</sup> Kuhlen *Typuskonzeption* 162; Joubert 1989 *TSAR* 568 578.

<sup>329</sup> Bydlsinski *Juristische Methodenlehre* 546, 547. However, Bydlsinski clearly regards the *Typenlehre* as a valuable contribution to the methodology of law (see for example at 549).

<sup>330</sup> Bydlsinski *Juristische Methodenlehre* 548 on the value of *Typenvergleich* (“comparison of types”).

<sup>331</sup> Kuhlen *Typuskonzeption* 169; Joubert 578.

<sup>332</sup> Kuhlen *Typuskonzeption* 169; cf Bydlsinski *Juristische Methodenlehre* 546.

order to correctly reflect, explain and order the complexity of legal reality. The *Typenlehre* correctly emphasises that one must be prepared to look beyond the concept and the question whether a transaction displays the elements of that concept (the *essentialia*), to the legal reality of the contract as used in practice and consider carefully whether all the rules applicable to a specific contract type are appropriate to that transaction, or whether there should be further differentiation justified by some distinct characteristic.

This emphasis on teleological thinking and the usefulness of open concepts is especially important in the context of specific contract types, where the ideal model is held out as the *essentialia-naturalia* model, in terms of which the classificatory characteristics are often understood to be the *essentialia* of a contract, which are clearly all-or-nothing criteria. If one looks to the history of this model and its application in practice, the truth is that the contractual purpose or end is the paramount criterion for classification, with the *essentialia* simply stating the terms on which agreement must be reached to reach that end through intervention of the courts.

In my opinion, the goal should remain to construct the classificatory characteristics of model contracts as precisely as possible, in terms of *essentialia* or other clear markers open to simple subsumption where this is possible. This is consistent with the goals of efficiency through norm reduction and legal certainty.<sup>333</sup> However, where the classificatory characteristics which prepare the way for the application of appropriate default rules cannot be formulated as *essentialia*, this should not deter the recognition of a new (sub-)type of contract formulated in terms of vaguer classificatory characteristics where this is required to give effect to legitimate and real economic goals. Whether one calls the resultant concept a “type” or an “open-ended concept” is not the important issue. If this is the only option, a continuous attempt must be made to clarify the indicative features of the type as much as possible in the interest of legal certainty, which may perhaps only occur over the course of a number of court decisions<sup>334</sup> and academic contributions.

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<sup>333</sup> Larenz & Canaris *Methodenlehre der Rechtswissenschaft* (1995) 267.

<sup>334</sup> So that, in the language of the *Typenlehre*, a list of examples develop of “typical” cases falling within or without the concept, permitting a comparison of types (*Typenvergleich*).

#### **6 4 The different categories of consequential rules and their interrelationship**

The discussion so far has raised questions about the interrelationship of the various conceptual devices used to regulate the consequences of contracts according to South African law. For example, does Vorster's criticism of the officious bystander test used by our courts to imply tacit terms demand that the reach of *ex lege* terms be extended to cover situations that our courts would treat as the territory of tacit terms? Is there another category of more peculiar or *ad hoc ex lege* terms apart from *naturalia* and general residual provision that should cater for such situations, for example, where the parties' contract is an innominate one, or the situation for which the term caters is an unusual one? Where exactly is the borderline between tacit terms, supposedly based on unexpressed intention, and *ex lege* terms anyway? Although I have treated all residual consequential rules as identical in my discussion of the determinants of these rules, many South African writers draw a distinction between general residual provisions and *naturalia*. What is the relationship between these two devices and this possible extra category of residual rules?

What is the relevance of these methodological questions to a proposal for the treatment of preference contracts? The difficulty of ascertaining the parties' true intention with respect to a host of issues, raises the question whether our courts should be exhorted to do the best they can with interpretation and the implication of tacit terms aimed at discovering the different possible interpretations that parties may place on these contracts. Or should the approach rather be to combine interpretation with the recognition of *ad hoc* legal incidents or *ex lege* terms so that clearer classificatory markers and residual rules for the different types of preference contracts may eventually crystallise? These two options seem to promise great sensitivity to the actual purposes that preference contracts are required to fulfil in different economic contexts, as well as a gradual and careful process of recognition of different types. A third alternative approach would be to attempt a proposal of classificatory criteria and default regimes for all the different types of preference contract I have identified.

This appears difficult in view of the ambiguity of typical drafting formulations resorted to in practice. A fourth alternative may be the proposal of a default type or types that should apply when it is not clear which type is intended.

These options (which will be discussed in more detail below) raise questions about the difference between “interpretation” and the implication of tacit terms, on the one hand, and the overt implication of *ex lege* terms or recognition of residual rules on the other, as well as about the different types of residual rules.

The interrelationship between these various conceptual devices used to regulate the consequences of contracts merits a full study. I will only make some exploratory remarks on this topic to the extent necessary for the purposes of this study.

I will use “implied terms” in this context in a very wide sense to refer to any supplementation of the clear express terms of the contract.<sup>335</sup> It therefore includes general residual rules on matters such as the requirements for due performance and breach that apply in the absence of specific regulation and can therefore be said to supplement the parties’ contract. Because these rules apply to these situations in the absence of self-regulation, they can be described as terms implied by law. “Implied terms” in this sense also include *naturalia*, other *ex lege* terms, tacit terms and terms read into contracts to clarify ambiguous express terms.<sup>336</sup> Of course, the idea of “implication of terms into a contract” is metaphorical anyway, especially as far as *ex lege* terms are concerned. As Corbett AJA said in *Alfred McAlpine & Son (Pty) Ltd v Transvaal Provincial Administration*,<sup>337</sup> “implied terms” (which he equated with *naturalia*) is a misnomer “in that in content it simply represents a legal duty (giving rise to a correlative right) imposed by law, unless excluded by the parties, in the case of a certain class of contracts.”<sup>338</sup>

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<sup>335</sup> See also Vorster *Implied Terms* 123 who uses “implied term” in a generic sense to embrace all non-express contractual terms.

<sup>336</sup> Examples of the latter type of term is given at n 396 and n 397.

<sup>337</sup> 1974 3 SA 506 (A).

<sup>338</sup> 531G-H. See also De Wet & Van Wyk 342-343; Christie *Contract* 182-183, who point out that “term implied by law” is appropriate, because these residual rules have all the characteristics and consequences of agreed terms, and are “folded into the contract by law.”

The conclusion I draw is that the different categories of implied terms presently recognised in South African case law and legal literature, constitute a continuum or spectrum with fluid borders. In the terminology of the *Typenlehre*, the categories of implied terms are types making up a *Typenreihe*, literally, a “row of types”. They each have characteristic features, which are gradeable and can be present to a greater or lesser degree in a specific case. There are also mixed forms of implied terms displaying the typical characteristics of tacit terms as well as those of *ex lege* terms to a greater or lesser degree.

These categories of implied terms flow into each other (and are distinguished from each other in a gradual manner) in three respects.

#### **6 4 1 Fluid borders with respect to their determinants**

Firstly, their borders are fluid with respect to their determinants or bases, that is, with respect to their degree of reliance on empirical elements (namely the facts peculiar to the transaction) as opposed to the extent to which they are determined normatively, “by law.” Tacit terms (at least in a strict sense) and words implied to augment ambiguous express terms, are sometimes said to be terms implied from the facts,<sup>339</sup> or terms based on the actual but unexpressed (or ambiguously expressed) intention of the parties.<sup>340</sup> This is then distinguished from terms implied by law, that is, based on normative considerations, such as reasonableness, fairness, other underlying principles of contract law and policy considerations.<sup>341</sup> These normative considerations can be fixed in case law, which then provides a binding precedent for the situation at hand. Alternatively they could justify implication of a new or

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<sup>339</sup> Christie *Contract* 100.

<sup>340</sup> See Kerr *Contract* 331 and authorities there cited.

<sup>341</sup> That it is the law which imposes residual rules is widely accepted by our courts. See, for example, *Kroonstad Westelike Boere Ko-operatiewe Vereniging Bpk v Botha* 1964 3 561 (A) 571H-572A; *Poynton v Cran* 1910 AD 205 220-221. See also Roman-Dutch authorities such as Voet 23 2 85 and modern commentators such as Kerr *Contract* 345 and Van Jaarsveld (ed) *Suid-Afrikaanse Handelsreg* 22.

qualified *ex lege* term, arrived at through analogous reasoning based on rules, underlying principles or policy goals identified in case law, old authorities or the Constitution, or which are otherwise accepted as desirable societal objectives. Implication of *ex lege* terms is not and should not, however, be totally divorced from the facts of the transaction. Nor does or should the implication or “discovery” of actual, but unexpressed or ambiguous terms take place without involvement of legal norms or “objective standards.” I have already shown that residual rules also have an empirical element and must be related to the demands of life and therefore functional and appropriate.<sup>342</sup> One implication is that, when implying *ex lege* terms, courts should be (and are) very much attuned to the facts of the case, in order to critically evaluate whether the residual rule or proposed *ex lege* term is in fact suitable to the peculiar situation, most importantly whether there is an appropriate connection between the presupposed contractual end justifying the residual rule and the actual contractual end of the parties.<sup>343</sup> Residual rules should also not apply if they are, for any reason, inconsistent with the parties’ contract.<sup>344</sup> Express exclusion is therefore not required.<sup>345</sup> In this respect, interpreting the facts (the parties’ true intention,

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<sup>342</sup> See par 6 2 *supra*.

<sup>343</sup> Many of the *naturalia* find their justification in the contractual end used to define the specific contract type. If this major premise is not matched in the transaction at hand, the *naturalia* of that contract type are therefore not suitable to deal with it.

<sup>344</sup> *A Becker v Becker & Co supra* 415E-F; *Geldenhuis v Maree* 1962 2 SA 511 (O) 514D-E; *Poynton v Cran supra* 221, 235; *Vorster Implied Terms* 159.

<sup>345</sup> *Ibid*. It is true that some cases and writers suggest that *ex lege* terms are implied unless they conflict with the *express* provisions of the contract, in other words, in the absence of express agreement on the matter (see for example, *Alfred McAlpine & Son (Pty) Ltd v Transvaal Provincial Administration supra* 531; *Sishen Hotel (Edms) Bpk v Suid-Afrikaanse Yster en Staal Industriële Korporasie Bpk* 1987 2 SA 932 (A); *cf* *Lubbe & Murray Contract* 416-417). However, these statements in case law are mostly *obiter*. See also *Vorster* 159 who criticise cases supporting this view and *Kerr Contract* 344 who define residual provisions as provisions imposed in the absence of express or *implied* (tacit) agreement. The reasoning underlying the exclusion of parol evidence to exclude an *ex lege* term from a contract in writing is that “a term which is implied by law is as much a term of the contract as though it had been embodied in the document itself” (*Aymard v Webster* 1910 TS 123 131). As *Vorster* 159 points out, this reasoning is fallacious “as a legal incident does not form a constituent part of a contract in the same way as terms implied on the basis of unexpressed subjective consensus or the reasonable expectation principle. Furthermore, this approach is no longer followed in the country of its origin [England].”

insofar as it can be discovered) remains paramount to the process of implying *ex lege* terms.

Interpretation, or the attempt to ascertain the true meaning of express terms or the parties' actual but unexpressed intention, is also necessarily influenced by normative elements, such as notions of reasonableness and good faith. Due to the limitations of language and the influence of context and the addressee's subjective knowledge, all interpretation involves a choice between different possible meanings.<sup>346</sup> That the parties are in court disputing the proper interpretation of the contract in the first place, shows the variability in meaning.<sup>347</sup> A choice between competing meanings often involves policy choices. Even though the interpreter might think she is engaged in a value neutral activity of following the "ordinary meaning of the language used",<sup>348</sup> policy considerations and her own sense of fairness and knowledge of the law and factual context are bound to affect her choice of "ordinary meaning".<sup>349</sup> This is illustrated by the different possible meanings of "right of first refusal", "preference contract" and standard pre-emption clauses despite some writers' insistence that one interpretation is the only "logical" one. In the case of tacit terms, Kerr states that "it is necessary to show, by a preponderance of probabilities, unequivocal conduct which is capable of no other *reasonable* interpretation than that the parties intended to, and did in fact, contract on the terms alleged."<sup>350</sup> "Reasonableness," an objective standard, can and does therefore play a role in proving probable agreement on a tacit term.

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<sup>346</sup> Van der Merwe & Lubbe 1991 *Stell LR* 91 99; Van Dunné *Verbintenissenrecht* 119 *et seq.*

<sup>347</sup> Normative interpretation rests on a fundamental or basic assumption of interpretation, namely that "if two parties subjectively attach two different subjective meanings to an expression, one meaning is more reasonable than the other, and neither party knows the meaning attached by the other, the more reasonable meaning prevails" (Eisenberg "The Theory of Contracts" 233).

<sup>348</sup> According to the so-called "golden rule" of interpretation, on which see, for example, Kerr *Contract* 233 *et seq.*, Christie *Contract* 23 *et seq.*

<sup>349</sup> On the difficulties of ascertaining the true intention of parties see Van Dunné *Verbintenissenrecht* 125 *et seq.*; Lubbe & Murray *Contract* 463.

<sup>350</sup> 331 (my emphasis).

In the case of express terms, this normative aspect of interpretation is more patent. Courts will also take into account the clearly normative “secondary” or “tertiary”<sup>351</sup> rules of interpretation, such as the *contra proferentem* rule<sup>352</sup> and the presumption in favour of the most equitable<sup>353</sup> and the least burdensome interpretation.<sup>354</sup> These rules should actually also be applied to the implication of “tacit terms” insofar as courts profess to base them on the actual intention of the parties.

The process of interpretation as presently practised by our courts has a normative dimension for another reason. It is well known that an interpretation of a specific clause often becomes a standard interpretation with normative power for subsequent cases.<sup>355</sup> A term initially implied on the basis of “actual but unexpressed” intention may eventually be recognised as a *naturale* if recognised in a number of cases.<sup>356</sup>

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<sup>351</sup> Lubbe & Murray *Contract* 466 use the term “secondary rules of interpretation” in reliance upon *Kliptown Clothing Industries (Pty) Ltd v Marine and Trade Insurance Co of SA Ltd* 1961 1 SA 103 (A) 107; *Fulton v Waksal Investments (Pty) Ltd* 1986 2 SA 363 (T). Van der Merwe *et al Contract* 220, 223 prefer to call these rules the “tertiary rules of interpretation” (except for the presumption in favour of an equitable interpretation which is apparently considered a “secondary rule”).

<sup>352</sup> *Cairns (Pty) Ltd v Playdon & Co Ltd* 1948 3 SA 99 (A) 121-122; D 2 14 39; D 45 1 99; D 50 17 9; Kerr *Contract* 249 *et seq*; Van der Merwe *et al Contract* 223; Lubbe & Murray *Contract* 466. The *contra proferentem* rule entails that if wording is ambiguous, its author should be the one to suffer because he could have made his meaning plain.

<sup>353</sup> Kerr *Contract* 249 *et seq* and authorities there cited; Van der Merwe *et al Contract* 222. The justification for this “leaning towards an equitable construction” is based on the notion that all contracts are *bonae fidei* (Kerr *Contract* 250). See also Kerr *Contract* 250 on the presumption in favour of avoidance of inconvenience.

<sup>354</sup> These explicitly normative rules of interpretation are not simply aids to arrive at the parties’ true intention (Lubbe & Murray *Contract* 466-469; Van der Merwe *et al Contract* 219; Van der Merwe & Lubbe 1991 *Stell LR* 91 100). See also Van Dunné *Verbintenissenrecht* 121 *et seq*. The court in *Transport and Crane Hire (Pvt) Ltd v Hubert Davies & Co (Pvt) Ltd* 1991 4 SA 150 (ZS) 161G-162A clearly recognised the policy-based nature of the interpretation of exemption clauses in South Africa, Zimbabwe and England when it stated that “A great deal of ingenuity is expended in trying to show that these artificial interpretations are in fact true and natural interpretations. I do not think the effort is worth the candle...[These interpretations] can only be defended on the ground that they are accepted and established policy-based interpretations.” I admit that application of the secondary (or tertiary) rules do in fact point to the likely intention of typical parties to typical contracts.

<sup>355</sup> Cf for example *Roux v Schreuder* 1968 3 SA 616 (O) 620G. See Vorster 1987 *THRHR* 450 452.

<sup>356</sup> Vorster 1987 *THRHR* 450 451-452; Christie *Contract* 183.

The many cases in which the courts add normative “tests” for tacit terms to the traditional hypothetical bystander test, such as the perspective of reasonable persons or the requirement that the term must be necessary to give business efficacy to the contract<sup>357</sup> display the instinctive realisation that the implication of tacit terms is not a value-neutral, non-normative exercise.<sup>358</sup> When applied totally subjectively without any such normative additives, the bystander test can hide the reality that any interpretation of facts, also where it is aimed at implying tacit terms, involves a choice between competing meanings as well as the policy or normative dimension of that choice.

The spectrum of types of implied terms can therefore be described with reference to the degree to which they are based on factual elements as opposed to the degree on which they are based on normative elements. Tacit terms and interpretation are obviously more factual than *ex lege* terms. If the extreme left of the spectrum connotes purely factually based terms and the right connotes purely normative terms,

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<sup>357</sup> This requirement is problematic and has been heavily criticised by, amongst others, Kerr *Contract* 341-342 and Vorster *Implied Terms* 51 *et seq.* *Inter alia*, these authors show that the decisions relied on for this supposed “requirement” (such as *The Moorcock* 1889 14 PD 64) did not imply that only terms which are necessary to give business efficacy to a contract may be implied therein (Kerr *Contract* 341-343). The way in which our courts apply it as a prerequisite for a term does not tally with its use in English case law, whence it derives. For example, one group of English cases hold that a term is necessary to give business efficacy to the contract if both parties would have agreed to it had their attention been drawn to the situation at the time of contracting. This simply equates with the bystander test itself (Vorster *Implied Terms* 51; *cf Joel Melamed v Cleveland Estates* 1984 3 SA 155 (A) 165E-F). Other slightly stricter descriptions are that a contract has business efficacy if it “works perfectly well” or if it constitutes “a perfectly plausible arrangement which the parties might very well have deliberately made” without the proposed term (Vorster *Implied Terms* 51-52). Business efficacy should rather be recognised as one indication that a tacit term exists. However, if one agrees with Vorster’s misgivings about the tacit bystander test, perhaps a strict business efficacy *requirement* is a blessing in disguise: since it prevents many a tacit term to be implied, courts may feel obliged to resort to the device of *ex lege* terms to reach a fair result. This they must do on a proper and full consideration of existing authority, underlying principles and policy considerations, whereas the bystander test may allow for unreasoned speculation on what parties would have answered.

<sup>358</sup> In *Joel Melamed v Cleveland Estates* 1984 3 SA 155 (A) 165E-F Corbett JA accepted that legal policy is involved in the implication of a tacit term. See also Vorster *Implied Terms* 177 *et seq.*

tacit terms which purport to mediate the unexpressed, but actual subjective consensus of the parties are most to the left. An example would be the term implied in *Janisch v Hall*.<sup>359</sup> The term implied in that case comes close to an express term, as it is based on the pointing out of an access road by the seller. The court held that this action and the existence of an access road on a plan incorporated in the contract, justified implication of a term that the purchaser may use the road to gain access to the land.

Slightly more to the right are terms that only one party had in mind subjectively, but that binds the other on the basis of the reasonable reliance principle. In other words, one party reasonably relied thereon that the other party also had the term in mind. The subjective intention of one party is therefore supplemented by notions of reasonableness in order to hold both to the term.<sup>360</sup> An example involves tacit “renewal” of a lease. It is reasonable to assume that both parties intend that their relationship continue on the same basis as before, which must necessarily include terms that they did not specifically consider again on renewal.<sup>361</sup> Implication of these terms are not contrary to their subjective intention just because they did not specifically think of them. They thought of all the terms in general.<sup>362</sup> Another example is the situation in *Commissioner for Inland Revenue v First National Bank*.<sup>363</sup>

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<sup>359</sup> 1946 CPD 553. See the discussion of this case by Vorster *Implied terms* 127.

<sup>360</sup> A term which is necessary to give business efficacy to the contract, or which constitute the only possible rational interpretation of the situation, can also be explained on this basis. Insofar as the term was *necessary* to “give business efficacy to the contract” or to “place a rational construction” on the contract, parties *must* have “intended” the term insofar as they clearly intended an efficacious and rational contract. The specific term is therefore covered by the general actual intention of the parties. As Kerr *Contract* 337 says, “the details [are] incorporated by reference.” Gordley’s example of a buyer of a car actually intending that the car must have whatever it must have to make it do what it is supposed to do, which implies that he also wants a working camshaft, though he may never have heard of one, throws some light on terms implied upon the basis of a more general actual intention. (Gordley “Contract Law in the Aristotelian Tradition” 325. He uses the example in another context, see n 232 *supra*.)

<sup>361</sup> *Bowhay v Ward* 1903 TS 772 779; Kerr *Contract* 534.

<sup>362</sup> However, whether they intend the lease to become an indefinite lease or to apply the original provisions as to the lease period, is open to different interpretations, and our law has now laid down a residual rule that the new lease would be an indefinite one, terminable on reasonable notice.

<sup>363</sup> 1990 3 SA 641 (A) 652E-G.

The court held that payment “under protest” to Inland Revenue clearly evinces a “tacit” intention that if the amount is subsequently held to be non-payable, it would be refunded. In fact, this “tacit” term is rather the only rational interpretation of the express term of payment, namely that it is done “under protest.” Therefore the court will believe the party who alleges that he intended that to be the effect and that he reasonably relied thereon that the other party intended the same.

More to the right on the spectrum are “tacit terms” which admit to seeking the imputed intention of the parties based on more objective tests such as the terms that reasonable parties would have agreed to.<sup>364</sup> These terms are often regarded as “tacit terms” in our law as the bystander test does not require

“that the parties must consciously have visualised the situation in which the term would come into operation... It does not matter... if the negotiating parties failed to think of the situation in which the term would be required, provided that their common intention was such that a reference to such a possible situation would have evoked from them a prompt and unanimous assertion of the term which was to govern it.”<sup>365</sup>

When based on the term which reasonable parties would have agreed to, this last category of tacit terms comes closer to *ex lege* terms (if they are not indeed rather *ex lege* terms)<sup>366</sup> as they openly rely on standards of reasonableness that apply in the absence of intention.

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<sup>364</sup> See Vorster *Implied Terms* 161 *et seq* and case law there cited.

<sup>365</sup> *Techni-Pak Sales (Pty) Ltd v Hall supra*, cited with approval in *Van der Berg v Tenner* 1975 2 SA 268 (A) 277D and *Alfred McAlpine & Son (Pty) Ltd v Transvaal Provincial Administration supra* 532A-B. See also *Greenfield Engineering Works (Pty) Ltd v NKR Construction (Pty) Ltd* 1978 4 SA 901 (N) 909A-F; *Wilkins NO v Voges* 1994 3 SA 130 (A) 136I and the numerous cases cited by Vorster *Implied Terms* 161.

<sup>366</sup> Vorster *Implied Terms* 191 point out that implication of terms based on the hypothetical consent of the parties and legal incidents overlap. *Cf Kerr Contract* 340. A number of cases appear to support the proposition that a tacit term can only be implied if the parties subjectively intended it to form part of their contract. See Vorster *Implied Terms* 161 at n 11 and cases cited there. For example, in *South African Mutual Society v Cape Town Chamber of Commerce* 1962 1 SA 598 (A) 606B the court stated that “’n stilswyende bepaling alleen...in ’n kontrak ingelees sal word wanneer die Hof oortuig is dat daar inderdaad ’n bedoeling was dat die betrokke bepaling in die kontrak opgesluit lê en dat al die partye tot die kontrak sodanige bedoeling gehad het.” This suggests that any term implied on the

On the other hand, the mere fact that the court assumes that the parties are “typical men of affairs, contracting on an equal and honest footing, without hidden motives and reservations” does not mean that the court cannot be seeking to ascertain the actual intention of the parties. The court may assume that in order to ascertain their actual intention in the absence of contrary evidence.<sup>367</sup> Especially where the court takes into account “special knowledge on the part of one party which would probably have a bearing on his state of mind”, the term does remain factual, or “tacit”, despite the fact that the court applies the reasonableness standard as well.<sup>368</sup>

As far as *ex lege* terms are concerned, terms which are openly implied on the basis of policy considerations, underlying principles of contract law and ethical postulates, but which also rely on the peculiar circumstances of the specific transaction (such as its other terms, the specific knowledge and particular actions of the parties), are more to the left than *naturalia* or general residual provisions.<sup>369</sup> The latter lose their dependence on these peculiarities due to their status as generally accepted implied terms whose major premises, or criteria for application, can be more widely or abstractly stated. Both *naturalia* and general residual rules are openly residual *rules* – they are laid down by law to regulate the relationship between the parties in the absence of contrary agreement.

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basis of “imputed intention” is in fact a term implied by the court (by law) and not a tacit term. Cases which hold that an imputed intention is sufficient for the implication of a tacit term include *Wilkins NO v Voges* 1994 3 SA 130 (A) 136I; *Techni-Pak Sales (Pty) Ltd v Hall* 1968 3 SA 231 (W) 236-237; *Van den Berg v Tenner* 1975 2 SA 268 (A) 277D.

<sup>367</sup> *Administrator (Transvaal) v Industrial & Commercial Timber & Supply Co Ltd* 1932 AD 25 33; *Wilkins NO v Voges supra* 139C-D.

<sup>368</sup> Where one party did in fact contemplate the situation at hand, even if as part of a more general intention regarding the effect of the contract, consideration of what reasonable persons would have understood could be regarded as application of the “reasonable reliance” principle as one possible basis for contractual liability. The term therefore remains an “actual, but unexpressed” term, in the sense that at least one party had it in mind, and reasonably relied on concurrence thereto by the other.

<sup>369</sup> In fact, the distinction between such *ex lege* terms and tacit terms which purport to take into account what reasonable parties would have agreed in the circumstances is very fluid.

The first category of *ex lege* terms is a mixed type of term: it relies on the peculiar circumstances of the transaction as well as objective standards. As such it overlaps with “tacit terms” implied on the basis of the hypothetical consent of reasonable persons in the parties’ position, where it is admitted that the parties did not consider such a term. Neels argues for recognition of such *ad hoc ex lege* implied terms, which he distinguishes from *naturalia* and, apparently, from the general consequential rules of general contract law.<sup>370</sup> He would have courts read in terms which he calls “other” *ex lege* terms (distinct from *naturalia*) on the basis of the circumstances which may exist at conclusion, during the existence and at enforcement of a contract, “and which are not peculiar to a specific type of contract,” instead of implying terms on the basis of hypothetical consent only.<sup>371</sup> Neels quotes Van der Merwe *et al* in support of recognition of this sub-category of residual rules. In their discussion of *bona fides*, these authors state that “*stante contractu*, conduct of a particular kind and standard may be required of particular contractants because their contract is of a certain type or because certain circumstances may arise.”<sup>372</sup> Vorster also appears to understand “legal incidents” in a wide sense. He has emphasised that whether a residual rule should apply to a particular kind of contractual relationship depends on the practical and policy considerations attending such a relationship and not whether the relationship is of common occurrence.<sup>373</sup> Vorster points out that “the law would be in a sorry state if the fact that a judge is unable to classify a contract as belonging to one or other of the well-known nominate classes, renders him powerless to imply terms as legal incidents.”<sup>374</sup> He also insists that a standard interpretation of

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<sup>370</sup> Neels 1999 *TSAR* 684 697-698.

<sup>371</sup> *Ibid.*

<sup>372</sup> Van der Merwe *et al Contract* 233 quoted by Neels 1999 *TSAR* 684 697 n 93.

<sup>373</sup> Vorster *Implied Terms* 36, 106, 158.

<sup>374</sup> Vorster *Implied Terms* 158. The same point is made at 36 and 106. Kerr *Contract* 123 confirms that if a new kind of contract “becomes popular”, a new class of specific contract can be formed (with reference to *Inst* 3 24 3). The implied term recognised by the minority in *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration supra* is perhaps an example of such an “uncommon” term implied by law, which might not be regarded by all as a *naturalia* of construction contracts (in fact the majority refused to imply the particular term). Corbett AJA, for the minority identified a term implied by law that an engineer who is granted “full power and authority” to issue drawings and instructions by a construction contract is in fact “obliged to issue such drawings and give such instructions to the contractor as may be reasonably required by the contractor in order to enable him to

an express term “is indistinguishable from a *naturale*.”<sup>375</sup> This shows up his rather wide conception of *naturalia* or residual rules.<sup>376</sup>

A term could sometimes qualify as both a tacit and an *ex lege* term.<sup>377</sup> In the *locus classicus* on implied terms, *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration*,<sup>378</sup> Corbett AJA considered that the term he sought to imply would qualify both as a tacit term and as an implied (*ex lege*) term, but preferred the latter explanation as he relied heavily on underlying principles of contract law to imply it. This overlap is not surprising. As I have shown before, one ideal for residual rules must be that they conform with the likely agreement of typical parties to the type of contract in question.<sup>379</sup>

## 6 4 2 Fluid borders with respect to their scope of application

Secondly, the different types of implied terms are on a continuum with respect to their scope of application. Their scope of application depends on the commonness of the

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execute the works, as defined in the general conditions of the contract. Each such drawing and instruction shall be issued or given, as the case may be, within a reasonable time after the obligation arises.” (535E-G). The court relied on the wording of the contract itself as well as on underlying principles of law to imply the term.

<sup>375</sup> “Resolution of contractual disputes: Interpretation *versus* the recognition of novel *naturalia*” 1987 *THRHR* 450.

<sup>376</sup> Neels 1999 *TSAR* 684 697 therefore misunderstands Vorster by criticising him for only allowing the implication of *naturalia* as opposed to other *ad hoc ex lege* terms implied on the basis of fairness. It is true that Vorster’s article to which Neels refers in this regard (Vorster 1988 *TSAR* 161) does not present this wider definition of legal incidents as clearly as his thesis. In the latter article Vorster criticises “the *ad hoc* approach”, but by that he means “discretionary justice in the guise of giving effect to the intention of the parties” (182) and not an overt implication of *ex lege* terms.

<sup>377</sup> See also Vorster *Implied Terms* 105 between n 118 and 119.

<sup>378</sup> 1974 3 SA 506 (A).

<sup>379</sup> See par 6 2. Interpretation and supplying residual terms are therefore overlapping and complementary exercises (Braucher 1990 *Washington and Lee Law Review* 697 733). As was stated in par 6 3, the commentators and natural lawyers who developed the concept of *naturalia* considered that the implication of *naturalia* was consistent with the parties’ intention that their contractual purpose be attained and that *bona fides* would be protected and promoted.

type of contract into which the terms are implied, on the one hand, and on the other, on the commonness of the situation or circumstances dealt with by the implied term. The real difference between general residual provisions, *naturalia* and other *ex lege* terms or legal incidents lies in their scope of application. General residual provisions apply to all types of contract in principle. The general residual provisions, such as those on breach deal with situations arising after conclusion of the contract which are of common occurrence.<sup>380</sup> *Naturalia*, by contrast, do not apply to all types of contract, but only to specific types of contract. They may also relate to events of common occurrence that are regulated by general residual provisions, but for which the *naturalia* have a deviating or qualified solution that applies only in connection with the specific type of contract. For example, *naturalia* can deal with breach, but may deviate from the general residual rules on its consequences. Examples are the special rules on the remedies of a buyer who has been evicted and the special rules on a lessee's remedies for breach in the form of failure to maintain the leased premises.

This interface of general residual provisions and *naturalia* creates a tension where they appear to conflict. How should this tension be accounted for methodologically?<sup>381</sup>

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<sup>380</sup> It has been argued that breach amounts to a new delictual cause of action (Van der Merwe & Olivier *Die Onregmatige Daad in die Suid-Afrikaanse Reg* 6<sup>th</sup> edition (1989) 484-485). However, most authors regard breach as resulting in a secondary contractual obligation that replaces or supplements the primary obligation (Lubbe & Murray *Contract* 414 and authorities there cited). The rules governing this obligation are therefore residual rules of contract law. They are also "implied into the contract" in a manner of speaking.

<sup>381</sup> There is not much explicit recognition of the obvious correlation between *naturalia* and general residual rules in South African legal literature, let alone the *ad hoc* legal incidents that especially Neels argues for. Nor is there any clear motivation for keeping these categories of residual rules well apart. Joubert *General Principles of the Law of Contract* 65 is almost alone amongst South African textbook writers in his express recognition of the link between *naturalia* and general residual rules. His definition of "terms implied by law" encompasses both these categories. Cockrell 1997 *Acta Juridica* 26 n 69 appears to agree with Joubert, as he suggests that the "general rules of contract law" should be regarded as *naturalia* attaching to contracts in general. Most other textbooks mention only *naturalia*, and not general residual provisions, in their discussion of implied terms. See, for example, Kerr *Contract* 346 *et seq*; Christie *Contract* 181-184; Van der Merwe *et al Contract* 196-197; Lubbe & Murray *Contract* 416-419; 422-425; Van Jaarsveld (ed) *Suid-Afrikaanse Handelsreg* 22. For example,

Firstly, one could acknowledge that *naturalia* may conflict with the general residual provisions because of policy considerations that may require differentiation. The *naturalia* could then be regarded as providing a necessary corrective to the general principles of contract law that may be unsuitable or insufficient to achieve a fair solution for a conflict of interests in a specific type of case. The special rules on the liability of innocent sellers for latent defects and misrepresentations (*dicta promissave*) on the quality of the *merx* could be taken as one example. Our law in this arena could be defended as a fair balance of buyers' and sellers' interests. Innocent sellers are only liable for price reduction or repayment of the purchase price, but not for consequential loss caused by the defect, which is a normal consequence of breach according to the general residual provisions. Where the seller has actually warranted the quality of the *merx*, is guilty of a culpable misrepresentation, has manufactured the goods herself or has held herself out as an expert trader in the goods, different policy considerations require the seller to bear responsibility for consequential loss as well. To simply argue that general principles of contract law dictate that the normal remedies for breach of contract, including a damages claim,

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Lubbe & Murray *Contract* 422 state that the need to supply "a set of normal terms that, in the absence of a law of contract, the parties would have to negotiate expressly...is satisfied [in South African law] by the so-called *naturalia* of the various specific contracts." They do not expressly recognise that general consequential rules also fulfil the same "need". Hawthorne 1995 *THRHR* 157 170-171 also mentions only *naturalia* of sales, lease and bills of exchange contracts as examples of implied terms. Vorster and Neels apparently accept that all *ex lege* implied terms fall under one category, namely legal incidents. The definitions of "implied (*ex lege*) terms" by Corbett AJA in the *locus classicus*, *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration supra* 531E-F and 532G are wide enough to encompass general residual provisions (for example he described an "implied term" as "essentially a standardised one, amounting to a rule of law which the Court will apply unless validly excluded by the contract itself" (532G)). However, Corbett AJA seems to have had only *naturalia* in mind, as the examples he gives are all of *naturalia* and he uses the term "*naturalium*" synonymously with "implied term" (631F-H). Van der Merwe *et al Contract* 200 n 196 state rather cryptically that "The considerations which induce the development of particular *ex lege* terms for particular class of contract may conceivably lead to the implication of those consequences into contracts in general, but it is doubtful whether there would be any value in treating such general consequences as *naturalia* rather than simply as rules of law." Whether they wish to convey that it is incorrect or dangerous to treat *naturalia* and general residual rules alike as terms implied by law is unclear. Perhaps they wish to convey that the nomenclature of "implied term" or "*naturalia*" is problematic in itself.

should be available for latent defects, ignores the policy consideration that this may be unfair to innocent, non-expert sellers.<sup>382</sup> Similarly, a kneejerk reaction to the special rules on the lessee's remedies for the lessor's failure to maintain the leased premises as "conflicting with general contract law principles on breach" should be treated with suspicion, where this argument does not consider and counter any policy considerations that may favour the present approach.<sup>383</sup> On this view *naturalia* and general residual rules, although related, operate on two different levels so that *generalia* (the general residual provisions) *specialibus* (the *naturalia*) *non derogant*.

Alternatively, one could require, in the name of consistency, coherency, norm reduction and efficiency, that there be no direct conflict between general residual provisions and *naturalia*, but only allow the *naturalia* to supplement or qualify the general residual provisions. The argument would be that the basis of classification for the importation of terms should be as wide as possible in the interest of norm reduction and efficiency. On this view, any conflict between the general residual rules and *naturalia* would indicate a systemic failure, requiring rectification by adaptation of the *naturale* or general residual rule in question. For example, the aedilician actions may seem like an exception to the general scheme of remedies for breach of contract, namely specific performance, the *exceptio non adimpleti contractus*, cancellation or compensation for all foreseeable damage. Similarly, the limitation on the lessee's entitlement to full compensation for consequential loss caused by defective premises to instances of culpable conduct or a guarantee by the lessor, has also been decried as an exception to general principles.<sup>384</sup> Perhaps the general rules on remedies for breach need to be developed to make provision for these exceptions, occurring as they do in two very common types of contract. This could be done by recognising a general remedy of proportionate reduction in contract price (or counter-performance) for defective performance in the absence of fault or a

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<sup>382</sup> This is not to say that opinions may differ on how best to balance the parties' interests.

<sup>383</sup> Cf Kleyn "Die reg van die huurder op skadevergoeding vir skade gely weens 'n gebrek in die saak" 1982 *De Iure* 197; Cooper *The South African Law of Landlord & Tenant* 2<sup>nd</sup> edition (1994) 108-110 who criticise the principle on this ground, but also maintain that it is too harsh and lacks authority. Cf by contrast, Zimmermann *The Law of Obligations* 365-367; Kahn *et al Principles of the Law of Sale and Lease* (1998) 57-58.

<sup>384</sup> Kleyn 1982 *De Iure* 197; Cooper *Landlord & Tenant* 108-110.

guarantee of proper performance. The *aedilitian actions* and *remissio mercedis* (proportionate reduction of rent) could be regarded as instances of such a remedy.<sup>385</sup> Liability for damages would have to be considered carefully to ascertain whether fault (probably different degrees of fault depending on the type of obligation)<sup>386</sup> should be a general prerequisite, in the absence of a warranty.<sup>387</sup>

Alternatively, one could combine these two all-or-nothing approaches. One could, on the one hand, regard these categories of residual rules as operating on different planes. This facilitates the correct approach of refusing to regard doctrinal fit with general rules as a straitjacket for the development of new *naturalia*, and similarly to snub arguments for the incorrectness of existing *naturalia* based only on their conflict with general rules. On the other hand, consistency between the *naturalia* and the general principles could simultaneously be regarded as a worthy but not essential ideal, due to the ethical postulate of treating like cases alike. Where policy considerations point to a special solution for a specific type of contract that apparently conflicts with the general residual provisions, it may prove beneficial to re-examine the general provisions to see whether they should be developed to provide for that exceptional *naturale*.

Granted their different field of application, an emphasis on the common functions and determinants of all residual rules or terms implied by law might lessen our courts' reluctance to use terms implied by law to arrive at a fair solution for a situation that, although not particularly common, may likely occur again. The link between *naturalia* and general residual provisions demonstrates that if not courts, then at least, "the law" *does* make contracts for parties by implying terms into contracts. Courts

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<sup>385</sup> The Supreme Court of Appeal in *Thompson v Scholtz* 1999 1 SA 232 (SCA) 248 rejected the notion that *remissio mercedis* simply amounts to application of the *exceptio non adimpleti contractus* with a claim to a "*quantum meruit*", but rather saw it as a separate common law remedy.

<sup>386</sup> Cf Stoop "Contractual liability in the Roman and modern South African law" in Van Wyk (ed) *Nihil Obstat: Feesbundel vir WJ Hosten/Essays in Honour of WJ Hosten* (1996) 163 179 who pleads for the retention of fault as a requirement for breach of contract, but on the basis of different degrees of care depending on the nature or type of contract involved.

<sup>387</sup> But see *Thoroughbred Breeders' Association v Price Waterhouse* 2001 4 SA 551 (SCA) 559B-C per Marais JA, Farlam JA and Brand AJA (par 8); *Administrator, Natal v Edouard* 1990 3 SA 581 (A) 597.

already “make contracts for parties” by applying general dispositive contract law, and they have modified and added to these rules over the years. If so, why should “the law” (or courts) also not consider new or amended *naturalia* or “*ad hoc ex lege* terms” where there is a clear need for it?<sup>388</sup> As Van der Merwe and Lubbe have said, if it is not the court's function to create legal incidents, the question is who then is to take the initiative.<sup>389</sup> In any event, a refusal to recognise an *ex lege* term also has policy implications.<sup>390</sup>

So much for the relationship between general residual provisions and *naturalia*.

“Other *ex lege* terms” which depend much on the particular circumstances of the peculiar transaction are more uncommon than *naturalia* and therefore do not have such a wide scope of application. Apart from *naturalia* that have already been

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<sup>388</sup> Courts are reluctant to “make contracts for parties.” See especially the *locus classicus* on implied terms - the judgment of Corbett AJA in *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration supra* 532H. Of course, Corbett AJA was ultimately prepared to imply an *ex lege* term into the contract, although the majority disagreed. Cf *Videtsky v Liberty Life Insurance Association of Africa Limited* 1990 1 SA 386 (W) 390G. The platitude that “courts do not make contracts for the parties” may explain the courts’ general reluctance to recognise a fair novel term implied by law, whereas they would rather ground the term in the imputed intention of the parties. Ostensibly, recognition of a tacit term does not amount to making a contract for the parties: their unexpressed intention is merely interpreted. The benefits of explicit recognition of the normative features of implying terms and the dangers of the traditional application of the officious bystander test have already been discussed. In addition, the requirement that the officious bystander’s question must evoke “a prompt and unanimous assertion of the term” (see for example, *Techni-Pak Sales (Pty) Ltd v Hall supra* 237A) would often deter courts from recognising a tacit term where justice demands some term to be implied. If the court is also unwilling to imply an *ex lege* term, the law remains incapable of providing a just solution. *Sweets from Heaven (Pty) Ltd & another v Ster Kinekor Films (Pty) Ltd* 1999 1 SA 796 (W) is arguably an example of such an injustice. Kerr “The need to use words with different meanings to describe different categories of provisions of contracts” 1999 *SALJ* 711 and Hawthorne “Sishen revisited: the decline and fall of the ‘gemenereg’” 2000 *THRHR* 668 have also criticised the court’s refusal to imply a term into the contract.

<sup>389</sup> 1991 *Stell LR* 91.

<sup>390</sup> Cf *ibid.* For example, the result of the *Sweets from Heaven* case *supra* is uncertainty about the precise limits of the rule laid down in *Sishen Hotel (Edms) Bpk v Suid-Afrikaanse Yster en Staal Industriële Korporasie Bpk supra*.

recognised in Roman and Roman-Dutch law, *naturalia* often achieve their status as “automatically implied terms” through being recognised in a number of decisions as terms that are fair and reasonable to balance the interests of the parties in the specific case or indeed as actually intended tacit terms.<sup>391</sup> When a court implies a term to deal with an uncommon or “new” situation relating to a nominate contract, it may initially be regarded as a tacit or perhaps an *ad hoc ex lege* term, but when the same situation is considered again, it will have normative force for that situation and often come to be regarded as incidents of that contract type, in other words as *naturalia*. When implied terms deal with innominate or new types of contract, they may also initially be regarded as tacit terms, but if a similar contract is considered again, the contract type may eventually acquire nominate status with its own set of *naturalia* based on earlier decisions on similar situations. This process is due to the generally accepted desirability of treating like cases alike. This is where the borders between tacit terms and *ex lege* terms or *naturalia* are once again fluid. The difference between the different categories of implied terms, is therefore the perception of each category’s normative power for future transactions, which perception may change over time. The more decisions that follow an interpretation, the more that interpretation is perceived as a residual rule.

The different types of implied terms therefore also flow into each other over time.

Is the present approach of our courts to implied terms satisfactory, given that it results in a blurring of borders between tacit and *ex lege* terms?

### **6 4 3 Vorster’s four categories of terms**

Vorster argues that four separate categories of implied terms must rather be recognised.<sup>392</sup> He groups the first three together as “terms inferred by construction.” First, he says, South African courts imply words or terms in contracts to give effect to an unexpressed but actual subjective *consensus*. Such terms are proved by

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<sup>391</sup> Vorster 1987 *THRHR* 450 451-452.

<sup>392</sup> *Implied Terms* 125; 1988 *TSAR* 161 161 *et seq.*

circumstantial evidence.<sup>393</sup> Secondly, Vorster identifies terms implied to protect the reasonable (actual) belief of one contracting party that the term was tacitly agreed upon. The reasonable reliance principle therefore “augments unexpressed subjective consensus as a basis for the implication of terms in the same way that it augments subjective consensus as the basis for the formation of contracts.”<sup>394</sup> Thirdly, Vorster identifies terms which are implied in order to place a rational construction on the contract. He says that these terms become relevant when the parties had no intention regarding a matter which later turned out to be the subject of litigation between them.<sup>395</sup> Vorster argues that where the pleadings treat the dispute as turning on the true construction of the contract, the court should usually choose the “most rational of the competing constructions.” This exercise involves the reading in of words “to give effect to the inferences drawn from the meaning of the express words.”<sup>396</sup> Often there is more than one logically valid alternative way of resolving the dispute and the court then chooses the more rational one in view of all the relevant propositions of law and fact, including the openly normative secondary rules on interpretation.<sup>397</sup> Fourthly,

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<sup>393</sup> 1988 *TSAR* 161 161.

<sup>394</sup> 1988 *TSAR* 161 163.

<sup>395</sup> *Ibid.*

<sup>396</sup> The words read into the contract in *Van den Berg v Tenner supra* 276A is an example. The court stated that: “Die enigste uitwerking van klousule 2 van die ooreenkoms...op die verpligting van die verweerder om die bedrag van R10 000 aan die eiser te betaal, was om nakoming van daardie verpligting uit te stel tot na die datum van afhandeling van die verkoper deur die verweerder van die [maatskappy]...of totdat dit duidelik geword het dat daardie [gebeurtenis] weens omstandighede nie kon plaasvind nie.” The last phrase was not expressed in the contract in question. The court read it into the contract in determining the “true meaning” of clause 2, whilst conceding that the parties never thought about the situation for which it caters (at 277C). For a full discussion see Vorster 1988 *TSAR* 161 164-165.

<sup>397</sup> Other examples mentioned by Vorster 143 include *Haak's Garages v Van Wyk* 1933 TPD 370 in which a hire-purchase agreement entitled the seller to recover instalments in arrear on cancellation. Although there was no express provision to that effect, it followed as a necessary consequence that the seller was entitled to retain instalments already paid. The court reasoned that “if this provision is not implied there would be no inducement to the seller to claim instalments, until they are all in arrear; and again assuming that all but one instalment has been paid, then on cancellation by the seller, he would only be entitled to recover the last instalment, but would have to refund the other instalments.” The court therefore considered the read in words to be the only rational construction although strictly

Vorster recognises legal incidents or *naturalia* of particular kinds of contractual relationships.<sup>398</sup> He emphasises that courts can and do make law by recognising new *naturalia*, for nominate as well as “new” or innominate contract types. The court then evaluates policy considerations relevant to a contractual relation of the kind before the court. However, in most cases there will be a precedent or custom that may be applied directly or by analogy, so that the cases where courts could justify a rule solely on a policy analysis will be rare.

Vorster argues that “the Moorcock doctrine”, that is, the bystander test coupled with the “business efficacy” test, should be jettisoned. On the one hand there is no necessary connection between these two tests and the actual tacit intention of the parties. On the other, these tests serve to mask policy choices in the implication of terms, which should rather be made openly and in a reasonable manner.<sup>399</sup> Unlike English law which spawned these tests, South African law does not need such fictions. English law did not receive the device of *naturalia contractus* (implied on the basis of the contractual purpose and *bona fides*) from Roman law, and therefore used the fiction of intention to evolve residual rules for specific contract types.<sup>400</sup> All terms implied on the basis of the Moorcock doctrine can be explained by the four bases which Vorster identifies.

Vorster also argues that where the words used do not bear directly on the dispute, one should generally first determine whether the transaction belongs to a class of

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speaking, two possible readings were logically possible. See also *Marine and Trade Insurance v Van Heerden* 1977 3 SA 553 (A).

<sup>398</sup> Vorster 1988 *TSAR* 161 166 *et seq.*

<sup>399</sup> As Vorster 1988 *TSAR* 161 173 points out, the courts have accepted that it is artificial to base the choice of applicable law on the imputed intention of the parties (as was customary under the approach confirmed by the Supreme Court of Appeal in *Standard Bank v Efroiken* 1924 AD 171). Decisions like *Improvair v Etablissements Neu* 1983 2 SA 138 (C) and *Laconian Maritime Enterprises v Agromar Lineas* 1986 3 SA 509 (D) have moved away from this “imputed intention approach” towards an approach seeking the legal system with the closest connection to the contract.

<sup>400</sup> Vorster 1988 *TSAR* 161 178 and authorities there cited. See also *CSIR v Fijen* 1996 2 SA 1 (A) 9H-10A where the court stated that “It does seem to me that, in our law, it is not necessary to work with the concept of an implied term. The duties referred to [that is, the reciprocal duties of trust and confidence between employer and employee] simply flow from *naturalia contractus*.”

contracts to which a legal incident which may be decisive of the dispute usually attaches.<sup>401</sup> This averts the danger of using “orthodox construction” as a mask for implying unclear and badly motivated legal incidents on the basis of non-existent presumed intention alone.<sup>402</sup> If the contract cannot be classified as a nominate contract, this does not mean that no legal incidents can be attached to it. If there is a possibility that the type of contract may be concluded by other parties, it is helpful to treat the implication of terms for situations not provided for by the parties not as mere interpretation in the sense of identifying tacit terms, but as the determination of legal incidents so that “an exasperating goose chase after non-existent contractual meaning” and the resort to fictional intention is avoided.

#### 6 4 4 Normative interpretation

An alternative approach to Vorster’s is to treat all cases where there is no *existing naturale* or general residual provision, as calling for normative interpretation. By “normative interpretation” I mean an approach to interpretation that does not regard “the intention of the parties” as the ultimate end of interpretation, but is premised on the filling of gaps in a manner consistent with the terms of the agreement and in accordance with business efficacy and fairness.<sup>403</sup> Factual elements are therefore openly combined with normative elements to reach a solution that is fair, and which can then serve as a precedent for a similar situation. Policy considerations are openly taken into account. Although the term eventually implied is based on an interpretation of the specific transaction, it becomes a residual rule for such situations

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<sup>401</sup> *Implied Terms* 105.

<sup>402</sup> *Ibid.*

<sup>403</sup> Normative interpretation is interpretation aimed not at establishing the subjective will of the parties, but rather the legal meaning of a factual act. On normative interpretation see Van Dunné *Verbintenissenrecht* 124 *et seq*; Lubbe & Murray *Contract* 463-464; Van der Merwe *et al Contract* 219. According to Van der Merwe *et al Contract* 219 the modern approach to interpretation is to combine the “psychological-historical” approach aimed at ascertaining the parties’ actual intention with the “objective” approach, in terms of which the conduct of the parties is placed within the context of legal policy, including the demands of good faith. At present, our law professes, in principle, to place the focus on the intention of the contractants.

should they ever arise in future. If a number of cases confirm the interpretation, it in effect becomes a *naturale* of the kind of transaction before the court. On this approach, the difference between terms implied on the basis of normative interpretation and residual rules such as *naturalia* and general residual provisions, is not that their determinants differ, as Vorster seems to suggest by his distinction between terms implied by construction and terms implied by law.<sup>404</sup> In fact, terms implied on the basis of normative interpretation as well as residual rules are justified by notions of fairness and policy considerations and both have empirical elements and should be consistent with the parties' or typical parties' intention.<sup>405</sup> As stated before, the real difference is rather the perception of each category's normative power for future transactions, which perception may change over time. Normative interpretation does not, therefore, exhort courts to lay down abstractly stated legal incidents from the start when faced with a new situation. It allows them to interpret the particularities of the situation in the light of normative ideals and to imply a fair term, which may later be regarded as a residual rule if more decisions confirm that interpretation and show that the situation is a recurring one.

“Normative interpretation” is not foreign to South African legal practice. Our courts have indeed at times used the implication of tacit terms to give expression to communitarian standards such as the underlying principle of good faith.<sup>406</sup> The “objective application” of the bystander test approaches normative interpretation, provided that the court gives reasons why it considers one interpretation as more reasonable than another, instead of merely stating that reasonable persons in the position of the parties would have answered that the term should apply.

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<sup>404</sup> *Supra*. However, Vorster's third category of terms, those implied to place a rational construction on a contract, approximates terms implied through normative interpretation, in that Vorster considers that the court chooses the more rational interpretation in view of all the relevant propositions of law *and* fact. See at n 397 *supra*.

<sup>405</sup> See par 6 2 *supra*.

<sup>406</sup> Cockrell 1992 *SALJ* 40 53; Hawthorne 1995 *THRHR* 157 172; Neels 1999 *TSAR* 684 695-696; *cf* Neels “Regsekerheid en die korrigerende werking van redelikheid en billikheid (deel 2)” 257; Vorster *Implied Terms* 167 *et seq*; Kerr *Contract* 335 *et seq*; Van der Merwe *et al Contract* 199 and cases there cited.

If normative interpretation is recognised, the distinction between the process of interpretation as far as the recognition of tacit terms is concerned, and the implication of *ex lege* terms remains blurred. In the Netherlands, the doctrine of normative interpretation apparently entails that no rigid distinction is made between interpretation and supplementation of the agreement with the aid of good faith.<sup>407</sup> The slogans of its proponents in the Netherlands are that “words are never clear” and that “interpretation is supplementation.”<sup>408</sup> They object to a separate treatment of supplementation and interpretation of terms, as this implies that interpretation fulfils a different function, namely ascertainment of the parties’ actual intention, which they consider to be generally impossible.<sup>409</sup>

A detailed consideration of normative interpretation and especially its impact on the traditional distinction between interpretation and supplementation of terms is beyond the scope of this study. The benefits of calling all supplementation of a contract “normative interpretation” instead of working with the two categories of tacit terms and novel *naturalia* or *ad hoc ex lege* terms (in addition to recognised residual rules) requires further consideration elsewhere.

What is certainly correct is that interpretation cannot be merely “factual” but is instead always normative (thus a legal-*cum*-factual question),<sup>410</sup> so that it allows no place for unreasoned policy decisions behind pronouncements on the unexpressed intention of parties in the implication of terms. A failure to openly consider the policy considerations and ethical postulates at stake can therefore find no

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<sup>407</sup> Van Dunné *Verbintenissenrecht* 127, 143. In the words of Scholten: “iedere interpretasie tevens is aanvulling en de tegenstelling eene is van meer of minder, niet van scherp te scheiden dingen.” (Scholten *Uitlegging van testamenten* 350 cited by Van Dunné *Verbintenissenrecht* 128).

<sup>408</sup> Cf Van Dunné *Verbintenissenrecht* 120, 124.

<sup>409</sup> Van Dunné *Verbintenissenrecht* 119 *et seq.* Cf Gordley *The philosophical origins* 244.

<sup>410</sup> Van Dunné *Verbintenissenrecht* 160 regards the distinctions interpretation – supplementation and factual question – legal question as distinctions that are difficult, if not impossible, to uphold in practice. He denies that interpretation of a contract is simply a factual question that can therefore not be appealed against, although he agrees that the question of interpretation involves a consideration of the facts.

justification. In a sense, even interpretation therefore amounts to “making a contract for the parties.”

One dubious utilitarian advantage of an insistence that the implication of new terms remains “normative interpretation” (as opposed to the creation of rules) is that it may encourage courts to consider terms not actually intended, but required by fairness and reasonableness in the light of the particular circumstances, and therefore consistent with the reasonable expectation of the parties. In Cockrell’s words, it allows courts to achieve a communitarian standard whilst remaining true to the language of individualism.<sup>411</sup> Implication of the types of (*ad hoc*) “legal incidents” or “*ex lege* terms” argued for by Vorster and Neels (and more cryptically, by Van der Merwe *et al*) to be implied due to the special circumstances of the transaction even when it is not of common occurrence, may be easier for courts to swallow.<sup>412</sup> Regarding the process as interpretation may lead to greater sensitivity to the particular realities of each situation, coupled with more general notions on the demands of underlying principles of contract law and policy goals.

One would then simply distinguish between three categories of implied terms according to the generality of their application. General residual rules would *prima facie* apply to all contracts, *naturalia* to contracts falling within a certain class and other implied terms to particular transactions and situations that may not be of common occurrence, but which are implied due to the special circumstances surrounding the transaction and the demands of fairness and justice. General residual rules would then be triply residual: they could be excluded by contrary *naturalia* of a specific contract type, or by *ad hoc* implied terms or by express agreement. *Naturalia* could, in turn, be excluded by *ad hoc* implied terms or by express agreement.

On the other hand, although “normative interpretation” of contracts has been recognised in many decisions of the highest court in the Netherlands,<sup>413</sup> it apparently

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<sup>411</sup> Cockrell 1992 *SALJ* 40 54.

<sup>412</sup> *Supra* at n 370 *et seq* and n 372 *et seq*.

<sup>413</sup> The *Hoge Raad*. See Van Dunné *Verbintenissenrecht* 133 *et seq* and cases discussed by the author.

remains somewhat controversial there.<sup>414</sup> Use of the term “interpretation” with its traditional connotation of decoding terms that already exist arguably obscures the true nature of the implication of terms in cases where the parties did not even consider the situation at hand.<sup>415</sup> No wonder then that our courts profess to be declaring the intention of the parties when implying tacit terms, yet generally do not call this process “interpretation”, a term limited to the elucidation of express terms.<sup>416</sup>

When normative interpretation amounts to supplementing the contract, it is criticised as a fiction by which an intention is ascribed to the parties that they never had.<sup>417</sup> On the other hand, it creates the danger of ignoring the parties’ actual intention, and therefore the important value or principle of party autonomy, on the basis of other policy goals. The distinction between interpretation and the implication of *ex lege* terms is so firmly entrenched in our law that it is doubtful that South African courts could be persuaded to regard all implication of novel terms as “interpretation”.<sup>418</sup> Nevertheless, further reflection on this controversial issue may perhaps persuade courts to regard all implication of terms, including the implication of “tacit terms”, as a “normative” process. This may facilitate the recognition of suitable terms on the basis of underlying principles such as good faith and other policy considerations or at least promote reflection on the policy justifications and repercussions of the tacit and *ex lege* terms that courts imply or refuse to imply.

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<sup>414</sup> Van Dunné *Verbintenissenrecht* 123, 125 *et seq* gives an overview of critical academic contributions and contrary decisions. Although lately the flag of normative interpretation seems to be flying at the top, to use his metaphor, some confusion still exists. On the latest decisions and academic contributions as from 1985 see 159 *et seq*.

<sup>415</sup> The famous Dutch jurist, Meijers, was a strong supporter of a distinction between interpretation and supplementation of an agreement, and vehemently criticised cases following the “normative interpretation” approach for this reason. *Cf* Van Dunné *Verbintenissenrecht* 135-136.

<sup>416</sup> Van der Merwe *et al Contract* 219.

<sup>417</sup> *Cf* Houwing’s criticism against the decision of *rederij Koppe* (1949) (1950 *NJ* 72) cited by Van Dunné *Verbintenissenrecht* 140.

<sup>418</sup> The distinction drawn between tacit and *ex lege* terms emphasised by Corbett AJA (as he then was) in *Alfred McAlpine & Sons (Pty) Ltd v Transvaal Provincial Administration supra* has been quoted with approval in numerous subsequent cases. Legal writers such as Kerr have also repeatedly criticised decisions which have blurred this distinction. See n 8 *supra*.

In my opinion, what courts should be exhorted to do when faced with a contractual gap is to seek to ascertain the true intention of the parties. Giving effect to the principle of party autonomy is an important aspect of the fairness ideal, where this does not result in oppression of one of the parties, or clearly conflicts with other communal goals. However, courts must also realise the limitations of language and of unreasoned reliance on “logic” in seeking to ascertain the parties’ intention.<sup>419</sup> They must realise that there is often a variety of logically valid interpretations that can be placed on a situation, so that the choice between them should be done on normative or fairness grounds. Courts must in addition not pretend to find an intention when none exists. They must also realise the normative effect of their interpretation and the term implied and therefore consider the decision’s relationship with and effect on existing authoritative rules and principles of law, whilst attempting to achieve coherency, consistency and legal certainty. For the same reason, the policy implications of their decisions must be taken into account. It is probably too presumptuous for legal writers to prescribe, in addition, that courts must seek to rather imply *ex lege* terms or *naturalia* than factual or tacit terms, or to state that these categories be kept strictly apart. Courts should always be responsive to the facts (the actual intention of the parties) and the requirements of the law and justice when implying terms and these empirical and normative aspects of adjudication cannot be rigidly separated. Ultimately, it is not so important for a court implying a novel term to categorise it as a general residual provision, *naturale*, *ad hoc ex lege* term, standard interpretation or *ad hoc* tacit term, as long as the court did follow all the guidelines mentioned above. The new term’s normative status will depend not so much on whether it is normative or empirical in origin as on the commonness or level of abstraction of the situation which led the court to imply it and the commonness of the type of contract into which it was implied. The soundness and persuasiveness of the court’s reasoning, and therefore the reaction of later courts to the decision, will be of decisive importance.

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<sup>419</sup> The bystander test sanctions unreasoned reliance on logic (“of course” arguments) to some extent.

## **6 5 Four possible approaches to the multiplicity of preference contracts**

The classification of preference arrangements resorted to in South African practice into the different types identified in chapter 5 is problematic. The incidents of preference agreements are often not negotiated to any great extent and the agreements are mostly worded very cryptically indeed. Very often one party simply states that she grants the other a right of pre-emption or first option. It is therefore often difficult to establish the basic purpose or contractual end of a preference contract, which is of course central to classification of contracts under both the conceptual and typological approaches. As mentioned above, the arrangement could be used either to place a mere *obligatio non faciendi* on the grantor, or, on the other hand, to grant the holder an enforceable right to performance of the eventual contract (or at least to conclusion thereof) upon the occurrence of any of a number of events.

The best solution for the problem is to prevent disputes by clear drafting. Drafters of preference arrangements in contracts, wills and statutes should bear in mind that the simple, one line formulations generally encountered in the case law may very well lead to protracted disputes on their proper interpretation. The extra costs attendant upon the careful drafting of preference contracts are justified by the prevention of costly disputes resulting from the uncertain legal rules governing these contracts.<sup>420</sup>

The typology of preference contracts set out in chapter 5 could serve as an aid to the drafting process. That chapter contains a catalogue of possible constructions that drafters may use in an attempt to reflect the actual intention of the parties before them. It highlights certain aspects that are presently unclear and suggests solutions on these matters. These include the exercise of the right by the holder, what constitutes breach

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<sup>420</sup> The problem of hasty drafting of rights of first refusal are not unique to South African practice. Several writers in other jurisdictions urge practitioners to draft these clauses more carefully. See for example, Platt "The right of first refusal in involuntary sales and transfers by operation of law" 1996 *Baylor Law Review* 1197 1210; Siviglia "Helpful Practice Hints: Rights of first refusal" 1994 *New York State Bar Journal* 56.

and what remedies are available on breach and on termination of the holder's right. The choice of rules on these matters should be clearly provided for in the preference contract if disputes are to be avoided.

A consideration of drafting proposals is beyond the scope of this study. Instead, I will focus on the situation where the preference contract is not clearly drafted, resulting in ambiguity as to the basic rights and duties of the parties. Four possible approaches for dealing with the variants that might have been intended will be considered here.

Firstly, one could insist that the precise construction of a preference contract is always a matter of interpretation, of teasing out the tacit agreement of the parties on the main consequences intended by them. This could be called the *ad hoc* interpretation approach.

Secondly, a set of guidelines for an *ad hoc* interpretation process could be developed, together with a check list of relevant policy considerations for the formulation of legal incidents in situations where the parties' consensus or reasonable reliance thereof cannot be fathomed.

Thirdly, classificatory criteria for each type of preference contract could be established, as well as a set of default terms (*naturalia*), which apply upon the classification of a contract into a specific type. These classificatory criteria could be either in the form of *essentialia*, that is, clear, all-or-nothing criteria, or in the form of "symptomatic features" or "indicative factors" which point to a "total picture" based on the contractual purpose, as sanctioned by the *Typenlehre*.

Fourthly, a default type or types that apply unless a court finds that a different type was intended, could be recommended.

### **6 5 1 *Ad hoc* interpretation approach**

In terms of the first approach, the *ad hoc* interpretation approach, the court must look to the facts of each case to establish the parties' expectations. This approach may be favoured for its flexibility, which allows courts to do justice in each particular case. A typology of preference contracts, such as that suggested in chapter 5, is helpful in this attempt as it should caution courts that parties may have very different consequences in mind.

However, the *ad hoc* interpretation approach is unhelpful on its own, mainly because reliable evidence of what the parties intended would often be lacking. This problem is exacerbated by the typically sparse formulations of preference agreements. The "interpretation" of a contract and the establishment of "tacit terms" would therefore often amount to pure guesswork as to the parties' intentions under cover of the "officious bystander" test.<sup>421</sup> As argued before, where the parties' actual intention cannot in fact be ascertained, the law should rather aim for the rational development of guidelines for solutions of particular problems which includes policy reasons and thereby contribute to the predictability of law.<sup>422</sup> This difficulty of establishing the basic result intended, also means that simply formulating the classificatory characteristics in terms of *essentialia*, which traditionally centre around the parties' main contractual purpose, is not helpful. The only contractual purpose which is common to all types of preference contracts is that the holder must be preferred before others when the grantor contracts. However, there are still very different ways in which the holder may be preferred, and it is often unclear whether the holder's preference was intended to be a bare preference or rather an enforceable right to contract on the occurrence of a certain event. Simply stating that the court must ascertain on the facts which consequence was intended, would lead to too much uncertainty in many cases.

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<sup>421</sup> The limitations and dangers of this test have been clearly set out by Vorster *Implied Terms in the Law of Contract in England and South Africa* unpublished PhD thesis, St John's College, Cambridge (1987) (see par 6 2 *supra*).

<sup>422</sup> Par 6 2 *supra*.

## 6 5 2 Normative interpretation, or, *ad hoc* interpretation and formulation of legal incidents

The second approach attempts to meet the shortcomings of a purely *ad hoc* interpretation approach, whilst still leaving scope for a multiplicity of types of preference contracts and the gradual development of residual rules. In instances where the parties' intention cannot be ascertained, the second approach enjoins courts to formulate *ad hoc* legal incidents for each specific relationship on the basis of policy considerations and in an effort to arrive at a fair solution in the specific case. This flexible approach seems to correlate with the variation in purpose and economic context in the use of preference contracts. Eventually rules and principles would crystallise to assist courts in linking the transaction with the appropriate residual rules. A list of relevant policy considerations, factors and guidelines for interpretation could be given to assist the courts in arriving at a fair solution in each case. The following considerations could be relevant:

- i. The desirability of the free alienability of property, in the interest of maximisation of wealth.
- ii. The economic sector in which the preference contract is used and the actual or typical bargaining position of the parties.
- iii. Whether the preference contract was concluded against consideration of any kind.
- iv. Who the most sophisticated party is, so that the burden of clear communication should be placed on him.
- v. Whether the preference contract predetermines the price at which the eventual contract may be concluded.
- vi. Whether the preference contract was granted at a time when the grantor had already manifested an intention to conclude the eventual contract.
- vii. Whether the holder was not interested in concluding the main contract, but rather viewed the preferential right as a mechanism entitling her to ward off third parties.

These considerations will briefly be discussed hereunder.

The desirability of the free alienability of property is a policy consideration in favour of the limited construction of preference contracts, which would leave the grantor as free as possible to obtain the highest possible price for her property. Our courts have often confirmed that preference contracts should be strictly construed as they amount to restraints on alienation.<sup>423</sup> This consideration means that preference contracts should not lightly be interpreted to mean that any manifestation of a desire to sell would trigger a right to contract. It is also an argument in favour of an assumption that a bare preference contract has been concluded. In cases where the court holds that a conditional right to contract is intended, it is also an argument in favour of the proposition that if the grantor no longer wishes to contract at all, he should not be forced to do so, arguably even after the holder has exercised her right.<sup>424</sup>

The economic sector in which the preference contract is used should be considered to ascertain the typical bargaining positions of the grantor and holder. The need for protection of either of the parties against exploitation of a disparity in bargaining power must then be considered. For example, if the preference contract is used in the publishing or recording industry, there are policy reasons for construing it as narrowly as possible in the artist's favour as the artist is up against powerful publishing or recording corporations and it is in the interest of the promotion of art that an artist be as free as possible to have her works published or recorded as she chooses. Moreover, in sectors where preference agreements are common, such as the publishing industry, third parties would not be willing to negotiate at all should the preference contract be construed as a right to contract upon the manifestation of a desire to sell in the form of serious negotiations. Therefore a bare preference construction, which does not force the author to contract with the holder publisher if theirs is the highest offer, but simply restrains her from contracting with any other

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<sup>423</sup> See, for example, the majority decision in the *Owsianick* case at 321; *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 188; *Edwards (Waaikraal) Gold Mining Co Ltd v Mamogale NO & Bakwena Mines Ltd* 1927 TPD 288; *Ah Ling v Community Development Board & Others* 1972 4 SA 35 (E) 37G-38A.

<sup>424</sup> In *Wissekerke v Wissekerke* 1970 2 SA 550 (A) it was common cause that the grantor could withdraw a voluntary offer before acceptance thereof. The court decided that this could not be done where the holder still intended to contract with a third party.

publisher unless the holder has refused to publish at the price offered by a third party publisher, would be most suitable to give effect to these considerations. The fact that a publishing or recording contract involves a continuous, close relationship between the parties may be a factor that could sway a court to rather hold that the preference contract creates only an *obligatio non faciendi* enforceable by prohibitory interdict, with breach only entitling the holder to damages or a prohibitory interdict. On the other hand, where there is no possibility of exploitation, it should be taken into account that grantors of rights of pre-emption in respect of property are generally in a stronger bargaining position than the holders, and that rights of pre-emption are often granted gratuitously to holders, without any oppression of the holders. In such cases, it is therefore legitimate to argue for a default construction which limits the grantor's freedom to deal with his property as little as possible, as this is what grantors would most likely have agreed to and what holders would most likely have been forced to accept, without this amounting to exploitation of holders.<sup>425</sup>

If the preferential right was granted gratuitously, it is fair that the grantor's capacity to alienate should be restricted as little as possible. This could be justified with reference to the ideal of contract law of the "substantial equivalence of exchanges."<sup>426</sup> The contract price is an indication of the risks deliberately imposed and accepted by the parties.<sup>427</sup> If you do not pay for a performance, you cannot demand too much.<sup>428</sup>

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<sup>425</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* (1965) 305.

<sup>426</sup> Vorster *Implied Terms* 20.

<sup>427</sup> Vorster *Implied Terms* 158.

<sup>428</sup> It is a venerable principle of contract law that one who acts for free should be set lower standards of care than one who contracts for a counter-performance (Van Dunné *Verbintenissenrecht Deel 1: Contractenrecht* 2<sup>nd</sup> edition (1993) 21.) It could accordingly be argued that the policy goal of "justice-in-exchange" would be promoted by a strict construction of preference contracts which leaves the grantor as free as possible to deal with her property, and to give the minimum possible logical meaning to the holder's preference. In the context of contractual powers, Cockrell "Second-guessing the exercise of contractual power on rationality grounds" 1997 *Acta Juridica* 26 51 states that this policy goal requires that "a contracting party should not, by the exercise of a unilateral power, be able to destroy the reciprocity in consideration that formed part of the original bargain". "[T]he aim is ...to prohibit one contractor from securing a distributive distortion by the unilateral exercise of a contractual power". Applied to preference contracts, the fact that no consideration is often received by the grantor in exchange for the right of first refusal, is a policy argument in favour of a default rule limiting the

It is fair that the burden of full communication should be placed on the most sophisticated party.

Predetermination of the price at which the main contract may be concluded, for example by providing for valuation by a third party, is a strong indication of a grant to the holder of a right to contract should the grantor manifest an intention to conclude the eventual contract. Agreeing to a price evidences that the grantor eschews the opportunity of obtaining the best possible price by sounding out the market.

If the preference contract was granted when the grantor had already manifested an intention to conclude the main contract, negotiations with third parties should not readily be held to trigger a right to contract. To hold that the manifestation of a serious desire to conclude the main contract triggers the holder's right would be ludicrous as there was already a clear desire to conclude the eventual contract at the time of granting the preferential right to contract.

Whether the holder was not interested in obtaining a substantive contract with the grantor, but viewed the preferential right merely as a mechanism to ward off third parties, should perhaps also be taken into account. Some German, Austrian and Swiss writers stress that the holder's principal interest may sometimes be only an *Abwehrinteresse*, an interest to ward off unwanted third parties.<sup>429</sup> In other situations she may have an *Erwerbsinteresse*, an interest in actually acquiring the object of the right of pre-emption.<sup>430</sup> In the former case, the holder's interest could perhaps best be reconciled with the grantor's interest to have his freedom of disposal impaired as

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holder's right as much as is logically possible in order to prevent a "distributive distortion" by allowing the holder too strong a right for no consideration.

<sup>429</sup> Schurig *Das Vorkaufsrecht im Privatrecht* (1975) 15-16. This interest is called a "prohibitive purpose" by Swiss and Austrian writers. See for example the Swiss writer Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht nach dem schweizerischen Zivilgesetzbuche* (1918) 13 and the Austrian writer Faistenberger *Das Vorkaufsrecht: Zum Vorkauf in Österreichischen Bürgerlichen Recht* (1967) 141.

<sup>430</sup> *Ibid.*

little as possible by treating the contract as a bare preference. This means that the grantor's duty is a negative one, so that a breach would not entitle the holder to contract with the grantor, but only to a prohibitory interdict or damages. Evidence to the effect that the holder was not interested in acquiring the subject matter, but desired only the power to prevent the rights from falling into the hands of a specific competitor,<sup>431</sup> could be an indication that the parties intended to create an *obligatio non faciendi* only. Whether this is an acceptable guideline for interpretation will be considered more fully below in the discussion of the third approach.

An approach along these lines would be more amenable to the "rational development of guidelines for the resolution of disputes" than the first one. With the focus remaining on interpretation and *ad hoc* implication of terms where necessary, this approach will probably facilitate appropriate solutions sensitive to the needs of each particular transaction. According to Martinek, the determination of the legal nature of contract types and their legal consequences invariable entails an extended process of development and pluralistic discursive communication.<sup>432</sup> If courts are prepared to consider the aforesaid guidelines for interpretation and the recognition of residual rules and resist the temptation of prematurely laying down a default regime for all preference contracts, the resultant development of preference contract types will benefit from the sensitivity shown to differentiated contexts.<sup>433</sup>

This manner of proceeding would, however, remain an *ad hoc* approach that, in addition to interpretation, focuses on the policy considerations relevant to each specific case to imply any legal incidents that may be necessary for a fair solution. It is true that the application of some of the guidelines and policy considerations

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<sup>431</sup> See, for example, *Dithaba Platinum v Erconovaal* 1985 4 SA 615 (T) 621C-D.

<sup>432</sup> 29.

<sup>433</sup> Differentiation between different economic contexts may be a good idea in respect of other aspects of first refusal transactions. For example, taking into account the typical importance of the identity of third party contractants in the specific economic context may lead to appropriately differentiated residual rules on the reach of transactions prohibited by the preference contract. In the context of close corporations or small companies, for example, there is a more persuasive argument to be made for extending the trigger event to involuntary sales than in the case of preference contracts in other contexts. For such an argument see Platt 1996 *Baylor Law Review* 1197.

indicated above would lead to the crystallisation of at least some types of preference contracts with a predictable set of residual rules, such as “the preferential right to conclude a publishing or recording contract”, “the gratuitous preferential right to buy land which does not predetermine the eventual price” and “the conditional right to contract when the preference contract predetermines the eventual price”. Such types are likely to crystallise because the same policy considerations would apply to all contracts within each of these types.

The proliferation of such idiosyncratic sub-types may be repugnant to South African lawyers and judges trained in a predominantly civilian system of private law, who because of a tendency to regard abstraction at the highest possible level as an important goal of jurisprudence, may be inclined to lay down uniform rules for all instances which appear to come within the parameters of an institution.<sup>434</sup> In the case of contracts, the typical approach would be to recognise or construct a uniform contract model with one set of *naturalia* irrespective of the economic context. However, such an attitude, which is essentially formalistic, is precisely what proponents of the *Typenlehre* object against, and with good reason.

A more concrete and weighty objection against this *ad hoc* approach is the uncertainty and unpredictability that would result in the interim, that is, before the eventual crystallisation of preference contract types (or the recognition by drafters of the importance of a clear formulation of the contractual purpose). It is therefore unlikely that courts would choose this route as a solution on its own.

### **6 5 3 Formulation of classificatory criteria for each type**

A third alternative approach, aimed at giving more guidance to courts and parties, would therefore be to spell out more definite classificatory criteria for each possible type of preference contract, without specifically distinguishing amongst types according to the economic sphere in which they are used. It would be very difficult, if not impossible, to formulate classificatory characteristics in the form of *essentialia*

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<sup>434</sup> Cf also Hutchison “When rigs do roam: Relational Economic Loss in Table Bay Harbour” 2001 *SALJ* 651.

or similar definite, all or nothing criteria for all the main types of preference contracts listed in the typology in Chapter five.

Definite classificatory markers can, however, be formulated for two types of preference contracts.

Firstly, predetermination of the eventual price in the preference contract, either by fixing a price or by establishing an external standard, is a clear indication that the holder has a right to conclude the eventual contract upon any manifestation of a desire to contract by the grantor, including the commencement of negotiations with third parties.<sup>435</sup> Only where the agreement clearly provides for a different trigger event, is this classification excluded. Examples are agreements that refer to the market price, the grantor's usual price, a reasonable price or a price to be determined by a third party. The justification for treating such contracts as productive of rights to contract conditional upon any manifestation of a desire to sell, is that a grantor who is prepared to agree on a definite price or an external mechanism for ascertainment of the price, has no interest in negotiating with third parties or sounding out the market in any other manner. He has clearly agreed to grant the holder the right to contract at the price provided for as soon as he manifests a desire to contract.

The desirability of free negotiation by the grantor means that doubts as to whether the grantor has an interest in sounding out the market should be resolved in her favour. For example, where the preference contract indicates that the price to be offered is in the discretion of the grantor but that, after such an offer was made, any dispute as to the applicable price should be settled by a third party, the grantor arguably still has an interest in sounding out the market before she decides on the offer she wishes to

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<sup>435</sup> It is clear that this classificatory criterion is not in the form of an *essentiale*, as the contract would not be invalid in the absence of a price provision. It would only make it a different form of preference contract. By definition, *essentialia* indicate the essential terms on which the parties must agree for it to be a valid contract.

submit to the holder.<sup>436</sup> Such preparatory steps should therefore not trigger the duty to make an offer in such cases.

Also, where the parties refer to a price which the grantor is prepared to accept from a third party or a *bona fide* price, one cannot draw the inference that the grantor has no *bona fide* interest in first sounding out the market and negotiating with third parties to establish the price at which he wishes to contract. Accordingly, the classificatory criterion of a predetermined price does not encompass a reference to “the terms which the grantor is prepared to accept from a third party” or “a bona fide price” or any similar vague formulation.

Secondly, where the preference agreement does not prohibit a contract with a third party, but simply entitles the holder to contract on the same terms as agreed with a third party, the construction of the preference contract is also clear. It operates like the *BGB Vorkaufsrecht*.<sup>437</sup> It can be understood as an option to contract upon the same terms as agreed with the third party which is conditional upon the grantor actually contracting with a third party. In this case the classificatory criteria are therefore the absence of an *obligatio non contrahendo cum tertii* and an indication that the holder has the right to contract upon the same terms as agreed with a third party.

I turn now to the remaining types of preference contracts listed in chapter 5. Would it be possible to formulate classificatory characteristics for these types in the form of a “Gesamtbild” based on the contractual purpose of each type, together with “symptomatic features” or “indicative factors” sanctioned by the *Typenlehre*?

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<sup>436</sup> *Cf Ah Ling v Community Development Board & Others supra*. The right of pre-emption in question was created by art 15(5)(a) of the Community Development Act, 3 of 1966, which provided for a price to be agreed between the Board and the owner concerned, and, failing agreement, to be fixed by arbitration. The court held that not even an offer to the holder at a specific price should be regarded as entitling the holder to insist on a price being fixed by arbitration, in spite of the reference to this manner of resolving a dispute on the price in the statutory provision. It must be remembered that the court had even more reason to construe the right of pre-emption restrictively as it involved a statutory deprivation of an existing right (see at 37H-38A).

<sup>437</sup> See par 4 1 1 *supra*.

The problem is that the traditionally cryptic drafting of preference clauses does not clearly reveal the parties' choice between the variable but related purposes that could be served by preference contracts. The parties are likely to dispute their exact contractual purpose when litigating over a preference contract and it would be difficult to decide *ex post facto* how they actually intended to structure the preferential right, especially because preference contracts are traditionally not extensively negotiated.

One hypothesis is that whether the preference contract amounts to a bare preference contract or a conditional right to contract depends on the holder's primary interest in obtaining the preferential right. On this view, an *Abwehrinteresse* or interest to ward off unwanted third parties, is an indicative feature of the bare preference contract, whereas an *Erwerbsinteresse* or desire to actually conclude the substantive contract is a symptomatic feature of conditional rights to contract. The hypothesis could also be formulated to the effect that a "dominant impression" that the preference contract stems from the holder's interest in warding off undesirable third parties would categorise the contract as a bare preference contract.<sup>438</sup>

Evidence in *Dithaba Platinum (Pty) Ltd v Erconovaal Ltd*<sup>439</sup> to the effect that the holder was not interested in acquiring the mineral rights, but desired only to prevent them from falling into the hands of a specific competitor,<sup>440</sup> could therefore provide the basis for a finding that parties intended an *obligatio non faciendi* only.<sup>441</sup>

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<sup>438</sup> Schurig *Das Vorkaufsrecht* 76 *et seq* and Burkert "Die Reichweite des § 506 BGB" 1987 *NJW* 3157 have argued for differentiation based on the holder's primary interest. For example, Burkert suggests that an *Abwehrinteresse* should lead to a "teleological reduction" of § 506 *BGB*, so that it does not apply where the holder has only an *Abwehrinteresse*. Article 506 *BGB* provides that an agreement with a third party that the sale would be conditional upon non-exercise of the *Vorkaufsrecht*, is ineffective against the holder, so that she may still exercise her right upon conclusion of such a sale.

<sup>439</sup> 1985 4 SA 615 (T).

<sup>440</sup> 621C-D.

<sup>441</sup> In *Dithaba Platinum (Pty) Ltd v Erconovaal Ltd supra* the grantor did not rely on this evidence in support of such an interpretation, but rather to argue that the event triggering the holder's right to

However, this hypothesis is problematic.

Several German writers have recently criticised attempts to argue for different sets of default terms for the *Vorkaufsrecht* according to whether the holder's primary interest is an *Abwehr-* or *Erwerbsinteresse*.<sup>442</sup> Many commentators have pointed out that the motivation for obtaining a preferential right is often unclear,<sup>443</sup> that both interests are often present, and that a holder's interest may change between conclusion of the contract and enforcement thereof.<sup>444</sup> To some extent their objections are based on the fact that the *Vorkaufsrecht* is regulated by statute. They argue that a judge may not deviate from the statutory regulation of the *Vorkaufsrecht* on the basis of a mere guess as to the holder's initial motive, whereas the parties could have specifically agreed on a deviation, but did not.<sup>445</sup> Nevertheless, these writers' objections ring true, even where preference contracts are not regulated by statute. A resort to non-communicated circumstances in interpretation has always been regarded as suspect.<sup>446</sup> Moreover, even where the holder's primary interest is clearly an *Abwehrinteresse*, she has an interest in acquiring the thing upon breach of the preference contract to protect

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contract had not occurred because the third party was a member of the same group of companies as the grantor.

<sup>442</sup> See for example, Westermann *Erman: BGB Handkommentar* 10<sup>th</sup> edition (2000) § 504 RdNr 8; Mader in Honsell (ed) *J von Staundinger's Kommentar zum Bürgerliches Gesetzbuch mit Einführungsgesetz und Nebengesetzen 2: Recht der Schuldverhältnisse §§ 433-534* 13<sup>th</sup> edition (1995) Vorbem zu §§ 504 ff RdNr 2; Huber in Mertens (ed) *Bürgerliches Gesetzbuch mit Einführungsgesetz und Nebengesetzen Kohlhammer-Kommentar begründet von Hs Th Soergel & W Siebert 3: Schuldrecht II (§§ 433-515) AGB-Gesetz, AbzG, EAG, EKG, UN-KaufAbk* 12<sup>th</sup> edition (1991) (hereafter cited as *Soergel & Siebert* (Huber)) Vor § 504 RdNr 5; Westermann & Klingberg "Vorkaufsrechte im Gesellschaftsrecht" in Westermann & Rosener (eds) *Festschrift für Karlheinz Quack zum 65. Geburtstag* (1991) 545 547.

<sup>443</sup> *Ibid.*

<sup>444</sup> *Soergel & Siebert* (Huber) Vor § 504 RdNr 5. This makes it more difficult to ascertain what the initial interest was.

<sup>445</sup> *Ibid.*

<sup>446</sup> Cf Macneil "Contracts: Adjustment of Long-Term Economic Relations under Classical, Neoclassical and Relational Contract Law" 1978 *Northwestern Law Review* 854 893 cited by Braucher "Contract versus Contractarianism: The Regulatory Role of Contract Law" 1990 *Washington and Lee Law Review* 697.

her interest, also against future cynical breaches. Concluding the main contract with the grantor is the manner in which the holder wants to assert her prohibitive interest.

In Austria and Switzerland, commentators also recognise that preference contracts often serve merely a prohibitive purpose, that is, where the holder intends to exclude a specific unwanted person from contracting with the grantor.<sup>447</sup> Still, this does not affect their view that the holder should always be able to obtain the thing upon breach by the grantor.<sup>448</sup> In fact, a Swiss writer has argued that a primarily prohibitive interest should extend the reach of the *Vorkaufsrecht*, so that it is also triggered by exchange, donation and succession, as such transactions would also impair the interest of the holder to ward off unwanted third parties.<sup>449</sup>

Once a prohibitive purpose as a marker of the bare preference construction is rejected, it is hard to imagine what other indicative feature could clearly distinguish bare preference contracts from other preference contracts, apart from a provision in the contract which limits the holder's remedies to damages and remedies aimed at restoring the *status quo ante*.

#### 6 5 4 Designating a default type or types of preference contracts

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<sup>447</sup> Faistenberger *Das Vorkaufsrecht* (1967) 141 (on Austrian law); Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht nach dem schweizerischen Zivilgesetzbuch* (1918) 13 (on Swiss law).

<sup>448</sup> *Ibid.* These writers argue that the holder's purpose should affect other questions surrounding preference contracts, such as whether the name of the third party should be disclosed to the holder, or only the terms of the contract. See for example, Faistenberger *Das Vorkaufsrecht* 141. Cf also the position in the US, where preferential rights to contract granted to allow exclusion of undesirable third parties, are also "specifically enforceable" in the sense that transfer of the object may be claimed. For clear recognition of these two main purposes of preference contracts, see Conine "Property provisions of the operating agreement - interpretation, validity, and enforceability" 1988 *Texas Tech Law Review* 1263 1317.

<sup>449</sup> Allgäuer *Vorkaufs-, Rückkaufs- und Kaufsrecht* 121-128. See also Platt 1996 *Baylor Law Review* 1197 1208 who discusses the argument in favour of extending the meaning of the trigger event that "shareholders in a closely-held corporation, especially those corporations owned by a single family, 'are greatly concerned about the identity of their (business) associates.'"

A fourth alternative approach would be to propose a default type or types to apply in the absence of a finding by a court that, on a balance of probabilities, a different construction was intended. Such a proposal amounts to coupling the *ad hoc* interpretation approach (see par 6 5 1) with a default type or types chosen on the basis of policy considerations. In addition, courts should keep in mind some of the guidelines for interpretation and policy considerations mentioned in the second approach (see par 6 5 2 above).

The extremely cryptic formulations of rights of pre-emption and the variety of ways in which preference contracts may be construed, makes a default regime highly desirable. A coherent default regime, justified by informed policy decisions and consistent with other rules of contract law, will promote judicial economy and reduce the costs of contracting.

The implicit approach of the current case law and academic writers on preference contracts is that there is but a single default construction.<sup>450</sup> The reliance on historical authority and case law by judges shows that they aim to find the terms implied by law into preference contracts generally. The debates between the various judges in *Owsianick*<sup>451</sup> and *Oryx*<sup>452</sup> and academic writers on the “correct” construction and the fact that they all finally choose one set of rules reveal the supposition that only one construction can be right, absent clear contrary provision by the parties. Designating a default construction or constructions with reasonably clear markers for application is therefore also the solution most likely to be followed by our courts.

The choice of default type or types should be made on the basis of justified policy considerations, particularly on the basis of a fair balancing of typical parties’ interests and fairness towards the community’s expectations as to its welfare as well as the need to reflect legal reality balanced against the demand for legal certainty. The

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<sup>450</sup> See also ch 1 *supra*. Cf for example, Floyd “Die Voorkoopreg” 1986 *THRHR* 253 257 and Du Plessis *Die spesifieke nakoming van voorkoopregte en ander verwante regte in die Suid-Afrikaanse en Franse Reg* unpublished LLM dissertation, University of Stellenbosch (1997) 14.

<sup>451</sup> *Owsianick v African Consolidated Theatres* 1967 3 SA 310 (A).

<sup>452</sup> *Associated South African Bakeries (Pty) Ltd v Oryx & Vereenigde Bäckereien (Pty) Ltd* 1982 3 SA 893 (A).

choice of default regime cannot be based merely on historical authority or precedent (which is in any event unclear in the present context) or unsubstantiated claims that one set of default terms is more logical or commercially useful than another. When rules are chosen as the default regime, these rules must, as far as possible, be reconciled with the existing conceptual structure of our law<sup>453</sup> to prevent contradictions and inconsistencies in the system.

## **6 6 Conclusion**

Contract law rules on the consequences of contracts serve diverse and often conflicting ideals, which are moreover vague and open-ended. An important ideal is to balance the apparently conflicting aims of legal certainty and the necessary flexibility that allows justice to be done in the particular case.

Courts must be prepared to give up the present position or solution when it is shown to be out of step with applicable policy considerations and notions of justice, as well as the typical purposes of typical parties to such contracts. Policy considerations need to be unpacked when a rule is unclear or conflicts with others, as is the case with preference contracts. Precedent plays a stabilising role in this endeavour, as the existing legal position is regarded as provisionally fair. The need to connect a new residual rule with the existing conceptual structure, or at least other rules and underlying principles, also promotes legal certainty.

If there is a possibility that other parties may resort to a type of contract concluded in a specific case, it is helpful to treat the implication of terms for aspects not provided for by the parties not merely as part of the process of interpretation in the broad sense. Courts should rather consider the policy implications of their willingness or refusal to recognise a tacit term. This they could achieve through a process of openly normative interpretation, or by laying down legal incidents, so that “an exasperating goose chase after non-existent contractual meaning” and the resort to fictional

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<sup>453</sup> Either by translating and fitting the rules into the conceptual structure of the system or, where necessary, to adapt the conceptual system to cater for the rule. See further par 6 2 *supra*.

intention is avoided in favour of a reasoned consideration of all relevant policy considerations and a fair balancing of any conflicting interests.

The *essentialia-naturalia* model of specific contract types is problematic. It creates the illusion that the application of a set of default rules, the *naturalia*, depends entirely on the existence of the criteria encompassed by the *essentialia* whereas this is not true in practice. Legal incidents can also attach to a subgroup of a nominate class. In such cases, other factors, based on policy considerations, influence which default rules apply. The *essentialia – naturalia* model furthermore creates the illusion that only nominate contracts should have residual rules. By contrast, Vorster has correctly emphasised that whether a legal incident should apply to a particular kind of contractual relationship depends on the practical and policy considerations attending such a relationship and not whether the relationship is of common occurrence.

The essential point of the *Typenlehre* is not so much to plead for the use of types rather than concepts, but to plead for typological thinking, which amounts to teleological or purposive thinking, as opposed to purely conceptual, formalist thinking about contract types. It also emphasises the need for the use of open concepts which require value judgments in addition to precisely defined, closed concepts in order to correctly reflect, explain and order the complexity of legal reality. The *Typenlehre* correctly proposes that one must be prepared to look beyond the concept and the question whether a transaction displays its elements (the *essentialia* in the present context), to the legal reality of the contract as used in practice. What must be carefully considered is whether all the rules applicable to a specific contract type are appropriate to that transaction, or whether there should be further differentiation justified by some distinct characteristic. In my view, the goal should remain to construct the classificatory characteristics of model contracts as precisely as possible, in terms of *essentialia* or other clear markers open to simple subsumption. This is consistent with the goals of efficiency through norm reduction and legal certainty. However, where the classificatory characteristics which prepare the way for the application of appropriate default rules cannot be formulated as *essentialia*, this should not deter the recognition of a new (sub-)type of contract formulated in terms of vaguer classificatory characteristics where this is required to give effect to legitimate

economic goals. Whether one calls the resultant notion a “type” or an “open concept” is not the important issue. If this is the only option, a continuous attempt must be made, with a view to legal certainty, to clarify the indicative features of the type as far as possible in academic and judicial discourse.

The very cryptic way in which rights of pre-emption are normally drafted makes it difficult to even identify the main purpose of the parties to the contract. It is therefore not easy to classify preference contracts into the different types identified in chapter 5, whether on the basis of *ad hoc* interpretation, or on the basis of measuring each transaction against a set of *essentialia* or typological “symptomatic features” or a “dominant impression”. The development of a set of guidelines for interpretation and a check list of relevant policy considerations for the formulation of *ad hoc* legal incidents may be helpful, but still result in uncertainty before the eventual crystallisation of preference contract types. It is therefore unlikely that courts will choose this route as a solution on its own. A default regime is therefore highly desirable in the interest of legal certainty.

I have already argued for two default regimes that should apply in cases where the preference contract predetermines the price or contains no *obligatio non contrahendo cum tertii*, respectively. A default construction should therefore be chosen for preference contracts not falling within these two categories. The latter type of preference contract is the most common kind.

The choice of the default construction should be made on the basis of recognised policy considerations, particularly on the basis of an equitable balancing of typical parties interests and in view of communal interests balanced against the demand for legal certainty. The choice of default regime cannot be based merely on historical authority or precedent (which is in any event unclear in the present context) or unsubstantiated claims that one model is more logical or commercially useful than another. When rules are chosen as the default regime, these rules must, as far as

possible, be reconciled with the existing conceptual structure of our law to prevent contradictions and inconsistencies in the system.<sup>454</sup>

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<sup>454</sup> Either by translating and fitting the rules into the conceptual structure of the system or, where necessary, to adapt the conceptual system to cater for the rule. See further par 6 2 *supra*.

## 7 Preference Contracts: Proposals for Reappraisal

In choosing a default type, two main types of preference contracts should be distinguished. The first is those rare preference contracts (rare in South Africa, in any event) where the parties make their intention clear that no *obligatio non contrahendo cum tertii* is intended, but that the holder would be preferred if she can match the terms agreed with the third party (7.1 below). The second is those preference contracts creating an *obligatio non contrahendo cum tertii* (7.2 below). I will argue that the default rule should be that an *obligatio non contrahendo cum tertii* exists.

Under this second type, I will show that two default types should be recognised, each with a clearly delineated field of application.<sup>1</sup>

### 7.1 Preference contracts that allow the grantor to contract with a third party

Typically such contracts provide for a right to match the terms agreed with a third party. The grantor is therefore allowed to contract with a third party so that there is no *obligatio non contrahendo cum tertii*. These contracts are preference contracts, as the holder must be preferred above the third party if she matches the latter's terms. Clearly, an enforceable right to contract is intended. The *Vorkaufsrecht* of the *BGB* is constructed in this manner.

This type of preference contract can plausibly be regarded as a conditional option. The holder has an option to contract upon the grantor concluding a contract with a third party and on the same terms. The notion that a mere unilateral declaration by the holder could bring the main contract into existence fits this explanation.

The price is sufficiently ascertainable to comply with the requirements for a valid option. At fulfilment of the condition, the price is absolutely clear. The price at

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<sup>1</sup> By default types I mean the body of rules which should apply in the absence of a contrary intention.

which the contract may be enforced can therefore be determined without further reference to the parties.<sup>2</sup>

As argued before, the condition (“conclusion of a contract with a third party”) is also not an objectionable potestative condition. Liability does not turn on the mere *ipse dixit* of the grantor, but depends on an action of the grantor, namely the conclusion of a third party contract.<sup>3</sup>

Also unfounded is the related, but theoretical objection that an intention to be bound is of the essence of an offer, so that the grantor, absent an intention at the conclusion of the preference contract, cannot intend an option. Any condition added to an option or a contract implies an intention not to be fully bound *at that point*, but only once the condition is fulfilled. Such conditional options or contracts bind the party in whose favour a suspensive condition is inserted pending fulfilment of the condition.

The normal rules on options apply.<sup>4</sup> A pre-emption contract in respect of land must be in writing and signed by or on behalf of the grantor in order to comply with the Alienation of Land Act, 68 of 1981. Upon fulfilment of the condition, the holder may submit a valid acceptance of the option, which must also comply with the prescribed formalities.

Rules unique to this type of conditional option might be required to cater for situations where the third party contract embodies personal obligations. However, as

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<sup>2</sup> This is the test for determinability of the price laid down in *Burroughs Machines Ltd v Chenille Corporation of SA (Pty) Ltd* 1964 1 SA 669 (W) 670C. See further *Hartland Implemente (Edms) Bpk v Enal Eiendomme BK & Andere* 2002 3 SA 653 (N); *Shell v Corbitt* 1986 4 SA 523 (C) 526B; *Dharupal Transport (Pty) Ltd v Dharupal* 1964 (1) SA 707.

<sup>3</sup> See par 5 2 2 2 and par 4 1 1 2 *supra*. Such an objection is raised by, *inter alia*, Van der Merwe *et al Contract: General Principles* (1993) 67.

<sup>4</sup> See further on this type of preference contract, par 5 2 2 2 (I) *supra*.

this type of preference contract is so rare in South African practice, I will not consider it in any further detail here.<sup>5</sup>

## **7 2 Preference contracts that do not allow the grantor to contract with a third party first**

It is more difficult to choose a default type for the usual case where the preference contract does contain an *obligatio non contrahendo cum tertii*, or where the holder is simply granted “a right of pre-emption” or “right of first refusal” without indicating whether the grantor may legitimately contract with a third party first.

Two default types should be recognised in such situations, each with a clearly delineated field of application.

Firstly I will show that “preference contracts” that stipulate a price for the main contract, or mechanism for ascertaining the price, should be construed as conditional options to contract at a predetermined price. Thereafter, I shall consider a default regime for all other preference contracts, that is, those preference contracts that do not fix the main price nor provides for a mechanism for ascertaining it.

### **7 2 1 Conditional options to contract at a predetermined price**

Where the preference contract predetermines the main price, either by fixing a price or by establishing an external standard or mechanism for its determination, the preference contract is in fact an option conditional upon any manifestation of a desire to contract by the grantor. The commencement of negotiations with third parties is therefore sufficient to trigger the right.

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<sup>5</sup> The implication of such personal obligations for exercise of the holder’s right will be considered further below in par 7 3 2 2 1 and the discussion there could be applied *mutatis mutandis* to the present type of preference contract.

Stipulation of a price clearly indicates that the grantor has no interest in sounding out the market, for example by negotiating with third parties. It must therefore be the parties' intention that, as soon as the grantor evinces an intention to contract, the holder will have a right to contract with her on the terms determined in the preference contract.

Once again, the price is sufficiently certain or ascertainable for such a contract to be regarded as a conditional option.<sup>6</sup> The condition, "any manifestation of a desire to contract", is also not an objectionable potestative condition. Liability depends on the actions of the grantor that manifest a desire or intention to contract and not on the grantor's mere *ipse dixit*. This aspect has already been fully canvassed.<sup>7</sup>

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<sup>6</sup> See especially *Shell v Corbitt supra* 528A. The preference contract in question obliged the grantor to buy all the petrol it needed from the holder at the holder's usual price, whereas the grantor could terminate the agreement if the holder refused to match a lower price of a competitor. The court stated that it was unnecessary to decide whether the agreement was a sale or option or more in the nature of a pre-emption agreement or a contract known in English law as a *solus* agreement. "The important point is that, even if it is to be regarded as an agreement of sale or an option agreement, the price aspect has been agreed upon with sufficient certainty to save it from being void for vagueness." The conditional option explanation has been supported by Reinecke & Otto "Voorkope en ander voorkeurkontrakte" 1986 *TSAR* 18 24 *et seq* and Lubbe 1985 *Annual Survey* 137-138 in respect of all preference contracts. Lubbe have also stated that "Grants specifying the pre-emptive price or, expressly or tacitly, incorporating the price at which the grantor is prepared to sell to a third party, will have to be recognized as more akin to option contracts than previously thought." See also Van der Merwe *et al Contract* 67. The view that *all* preference contracts may be regarded as conditional options was implicitly rejected by the Supreme Court of Appeal in *Hirschowitz v Moolman* 1985 3 SA 729 (A) 765F-G and *Soteriou v Retco Poyntons (Pty) Ltd* 1985 2 SA 922 (A) 932E, but these decisions did not specifically reject this juridical explanation in respect of the narrower category of preference contracts which does predetermine the price, not including reference to a price which the holder is prepared to accept from a third party.

<sup>7</sup> See paragraphs 7 2 and 5 2 2 2 *supra*. Whether *Wissekerke v Wissekerke* 1970 SA 2 550 (A), which did not deal with a similar contract, should allow the grantor to cure the breach, will be discussed further in par 7 2 2 1 1 *infra* at n 29 *et seq*. Allowing the grantor to cure the breach, would contradict the normal characteristic of an option that the grantor must keep the offer open.

The normal rules on options apply.<sup>8</sup> Upon fulfilment of the condition, the holder may submit a valid acceptance of the option, which must comply with any formalities prescribed for the main contract, for example those set by the Alienation of Land Act, 68 of 1981.

Preference contracts which provide for an offer at “a price which the grantor is prepared to accept from third parties,” do not fall under this category. This “price criterion” does not establish that the grantor has no interest in sounding out the market by negotiating with third parties. Therefore he should remain as free as possible to do so. Negotiations should therefore not trigger the holder’s right.

Reference to a “usual price” or a “reasonable price” is sufficient to bring the preference contract under the present type.<sup>9</sup> So are provisions that the holder will have a right to buy at a price to be agreed, and failing agreement, to be ascertained by a third party.

In view of this overlap of options and preference contracts, it is not too surprising that the distinction between options and rights of pre-emption is not, as Christie points out, always apparent to those who make contracts.<sup>10</sup> The present type of “preference contract” gives the holder a right to contract at a specified price despite a better offer by a third party. The primary obligation of the grantor is therefore not merely to

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<sup>8</sup> See further on this type of preference contract, par 5 1 1 *supra*.

<sup>9</sup> Where no price, not even a price “which the grantor is willing to accept”, is referred to whereas a usual price exists, it will be a matter of interpretation whether the parties intend a right to contract at the usual price. Uncertainty as to their intention should lead to a narrow interpretation, that is, in favour of a true preference contract and not a conditional option to contract at the usual price. Certainly, the courts’ apparent readiness to depart from the established rule that a sale for a reasonable price is invalid for uncertainty (*cf Genac Properties Jhb (Pty) Ltd v NBC Administrators CC 1992 1 SA 566 (A)*) should not lead to implication of a reasonable price in pre-emption contracts which do not refer to a price. For argument on these matters see par 7 2 2 1 1 *infra*.

<sup>10</sup> *The Law of Contract in South Africa* 4<sup>th</sup> edition (2001) 61. Two of the cases to which Christie refers do in fact concern conditional options to buy at a specified or predetermined price (*Van Pletzen v Henning* 1916 AD 82 and *Cohen v Behr* 1947 CPD 942). Of course, there are other cases where drafters have referred to a “first option” when they actually mean an outright option, such as *Stewart v Breytenbach* 1986 3 SA 47 (N) 52-53.

prefer the holder above third parties, all things being equal, as is the case in other types of preference contract. If a “preference contract” to contract at a specified sum when the grantor desires to contract should be included in the term “preference contracts”, any option is also a preference contract, as an option holder also has a right to contract at a specified price, so that she has the “first refusal” to contract at that price. Likewise, the option grantor may only contract with a third party after the holder’s failure to declare her intention to contract at that price. The only difference is the condition suspending the right to contract.<sup>11</sup> Therefore, “preference contracts” or “first refusal contracts” could be an umbrella term for options *and* contracts traditionally described as “first refusal” or “pre-emption” contracts.

Perhaps academic writers concerned for retention of the distinction between options and rights of pre-emption<sup>12</sup> would criticise typifying certain rights of pre-emption as options. However, there is of course no inherent virtue in retaining a dogmatic distinction for its own sake.

## 7 2 2 Ordinary preference contracts

The second default type should provide for all other cases where there is an *obligatio non contrahendo cum tertii*. This is the type of preference contract most widely used in South Africa. The parties indicate that the holder should have the first chance to contract with the grantor, but they do not specify a price or external standard for ascertainment thereof, apart from perhaps a reference to the price that the grantor would be prepared to accept from third parties.

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<sup>11</sup> See also Reinecke & Otto 1986 *TSAR* 18 33; Van der Merwe *et al Contract* 67. It is therefore not surprising that the court in the English case of *Pritchard v Briggs* [1980] Ch 339 (CA) suggested that a pre-emption agreement that specified the terms of the main contract is a conditional option contract.

<sup>12</sup> Cf Van der Merwe *et al Contract* 68 who suggest that maintaining the distinction between options and rights of pre-emption is an advantage of regarding the *Oryx* mechanism as a power to create legal relations or *Gestaltungsrecht*. Cf Janisch “Maintaining the distinction between options and pre-emption agreements” 1990 *Responsa Meridiana* 434.

To distinguish it from the two other main types discussed in the previous paragraphs, I shall refer to such contracts as “ordinary preference contracts”, as they are the type most often encountered in modern South African practice. Such contracts only oblige the grantor to “prefer” the holder above interested third parties if the holder matches the terms offered by them, whereas at least the previous type which also incorporates an *obligatio non contrahendo cum tertii* actually gives the holder a right to contract at a specified price despite a better offer by a third party.

The two most important issues that a default type for ordinary preference contracts must settle are:

1. What manifestation of a desire to contract should be regarded as breach, which would trigger the holder’s remedies?
2. What remedies should be available on breach? Most importantly, may the holder ultimately enforce performance of the main contract?

Proposals on these issues will be made after examination of the relevant policy considerations. I will thereafter investigate whether the proposed solution has found some recognition in South Africa or other legal systems.

Thereafter I will propose default rules on some other basic aspects of normal preference contracts, such as exercise of the holder’s right and termination thereof.

I will thereafter consider how these default rules could be fitted into the existing conceptual structure of South African contract law. In this regard, I will consider possible coherent juridical explanations of the proposed body of rules. As the validity requirements, most notably the applicability of formalities legislation, could depend on the juridical explanation of true preference contracts, these will be discussed in conjunction with the choice of juridical explanation.

7 2 2 1 *Two central issues*

7 2 2 1 1 Should any conduct short of a third party contract breach or trigger the holder's right?

The default rule should be that nothing short of a valid offer to or contract with a third party amounts to breach by the grantor. An offer by the grantor should be regarded as breach, as it is also an undertaking to contract with a third party. An *obligatio non contrahendo cum tertii* implies that the grantor's first offer should be made to the holder, and not to a third party. No lesser manifestation of a desire to contract should trigger any remedy for the holder (apart from a prohibitory interdict), not even where the preference contract provides that "upon the grantor *desiring* to contract, he shall offer to contract with the holder." Only if the parties make it clear that the holder shall be entitled to enforce the preference contract at a lesser manifestation of a desire to sell, should the default rule be excluded.

The policy reasons in favour of this default position have already been canvassed.<sup>13</sup>

They are that the grantor should be left as free as possible to negotiate with third parties in order to sound out the market and to ultimately obtain the best possible price. This promotes maximisation of wealth and economic efficiency, to the benefit of society as a whole.<sup>14</sup> As noted by the court in *Ah Ling v Community Development Board*<sup>15</sup> any lesser trigger than the conclusion of a contract (or a valid offer) would cause the grantor to "always be acting at his peril in land deals", compelling him "to move with clandestine caution" and to "constantly...be on his guard against statements or conduct on his part which could possibly provide evidential material

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<sup>13</sup> Paras 4 1 2 5 and 7 1 2 *supra*.

<sup>14</sup> The respect for the policy goal of maximisation of wealth is justified in the present context. No oppression or exploitation of the holder is involved and there are no other policy considerations at stake justifying disregard of this policy goal, such as the demands of the environment or the landless poor.

<sup>15</sup> 1972 4 SA 35 (E).

pointing to a desire to dispose of his property.”<sup>16</sup> The grantor would not even be able to conduct open and free negotiations with the holder as a result.<sup>17</sup>

Grantors are typically most likely to agree to such a limited burden on their contractual freedom; all the more so because preferential rights are often granted gratuitously on the assumption that they do not make any real difference to the grantor’s position.<sup>18</sup>

In sectors where preference agreements are common, such as the publishing industry, third parties would not be willing to negotiate at all should serious negotiations trigger a right to contract to the obvious detriment of the holder.<sup>19</sup>

Furthermore, defining the trigger event as some earlier manifestation of a desire to contract creates uncertainty. Efforts to narrow down the trigger event to “initiating the execution of the decision to alienate”<sup>20</sup> or “the display of a willingness, here and now, to contract with a specific person”<sup>21</sup> or “entering into serious negotiations with third parties” are insufficient to dispel this uncertainty in cases where the grantor has not actually contracted or offered to contract with a third party.

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<sup>16</sup> 40A-D.

<sup>17</sup> *Ibid.*

<sup>18</sup> Cf Van Dunné *Verbintenissenrecht Deel 1: Contractenrecht* 21. In fact, the right of first refusal can be costly for the grantor because it may reduce the amount that can be obtained from the sale of the property. The existence of a preemptive right may deter potential buyers from making offers because it reduces their expected return from the costs they incur in negotiating and making an offer (Mitchell “Can a Right of First Refusal be Assigned?” 2001 *University of Chicago Law Review* 985).

<sup>19</sup> See par 6 5 2 *supra*. The existence of rights of first refusal already tends to chill the interest of potential third party contractants (Cross “The ties that bind: preemptive rights and restraints on alienation that commonly burden oil and gas properties” 1999 *Texas Wesleyan Law Review* 193 195). Therefore there is a good argument for a limited default construction to prevent a total disinterestedness from third parties.

<sup>20</sup> In the words of Larenz “Die rechtliche Bedeutung von Optionsvereinbarungen” *supra* 210 (my translation). See also Nipperdey “Über Vorhand, Vorkaufsrecht und Einlösungsrecht” 1930 *Zeitblatt für Handelsrecht* 300 301.

<sup>21</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* (1965) 340.

There would also be uncertainty regarding the contract price. A right to contract, conditional upon a mere manifestation of a desire to contract, would be meaningless unless the law lays down a standard for the contract price. Prior to an offer or a contract, the grantor has not yet indicated clearly what terms he is prepared to accept from third parties. The criterion cannot therefore be “the terms which the grantor is prepared to accept from third parties.”<sup>22</sup> Ultimately, vague and disputable criteria such as fairness and reasonableness, or “a good faith offer” will of necessity have to be employed. However, the grantor never agreed to be limited to a fair or market price.<sup>23</sup> She has only agreed not to contract with a third party at a price that the holder might be willing to pay. Clearly, some third party may be prepared to pay a higher price than the fair or market price.<sup>24</sup> It is also not in the interest of society as a whole that she be limited to a fair price. Therefore the grantor should be allowed to freely sound out the market to ascertain the highest price at which she could contract and to refrain from contracting at all if it turns out that the market price is not high enough.

This proposed default interpretation of preference contracts is in accordance with the *quod minimum* rule of interpretation that holds that words of doubtful meaning must be construed so as to impose the least possible burden on the debtor.<sup>25</sup>

I therefore submit that the approach in *Soteriou v Retco Poyntons (Pty) Ltd*<sup>26</sup> should not be followed. The majority there held that “‘refusal’ imports an offer”, and that,

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<sup>22</sup> Cf *Soteriou v Retco Poyntons supra* 932H; 933F.

<sup>23</sup> See also Floyd 1986 THRHR 253 260.

<sup>24</sup> Cf *Soergel & Siebert* (Huber) Vor § 504 Rd Nr 4 who recognise the legitimate interest of the owner to obtain as high a price as possible.

<sup>25</sup> *Cairns (Pty) Ltd v Playdon & Co Ltd* 1948 3 SA 99 (A) 122 *et seq*; *Kliptown Clothing Industries (Pty) Ltd v Marine & Trade Insurance Co of SA Ltd* 1961 1 SA 103 (A) 107; Van der Merwe *et al Contract* 223; Lubbe & Murray *Farlam & Hathaway's Contract: Cases, Materials and Commentary* 3<sup>rd</sup> edition (1988) 466-467. The rule is found in D 50 17 9: “semper in obscuris quod minimum est sequimur.” The rationale for the rule is that “we ought to be more inclined towards freeing from an obligation than towards imposing a burden, and for that reason more ready to diminish than to increase an obligation; it is consistent with humanity to favour rather the debtor than the creditor.” (Averanius *Interpretatione Juris* 4 17 3 cited by Wessels & Roberts *The Law of Contract in South Africa I* 2<sup>nd</sup> edition (1951) par 1961).

<sup>26</sup> 932H, 933F.

while the clause was silent as to the method of determining the rental to be stated in the offer, the grantor was not free to fix any rental it pleased; it had to act *bona fide*. The rental and conditions had to be those upon which the lessor would offer the premises to other would-be lessees in the event of the holder not being willing to exercise his right. In the absence of an actual third party contract showing at what price the grantor was prepared to contract, these standards are too vague and unfairly limit the grantor to a reasonable price. The grantor has a *bona fide* interest in obtaining as high a price as possible, as opposed to merely a reasonable price, as long as the holder is ultimately preferred above third parties. This means that the grantor should be free to offer any price whatsoever to the holder if he so pleases, as long as he does not contract on better terms with another before these terms have also been submitted to the holder.

This approach is consistent with the accepted general principle that preference contracts, as restraints on alienation, should be strictly construed.<sup>27</sup>

A rule that a preference contract only terminates once the grantor actually contracts with and performs to a third party on terms that the holder had an opportunity to match, sufficiently protects the holder against a *mala fide* attempt to shake off the holder by an outrageously high offer. This rule will be considered further below.<sup>28</sup>

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<sup>27</sup> See, for example, the majority decision in the *Owsianick* case *supra* at 321; *Robinson v Randfontein Estates Gold Mining Co Ltd* 1921 AD 168 188; *Edwards (Waaikraal) Gold Mining Co Ltd v Mamogale NO & Bakwena Mines Ltd* 1927 TPD 288; *Ah Ling v Community Development Board & Others* 1972 4 SA 35 (E) 37G-38A; *Davids v Goodwood Municipality & Others* 1969 3 SA 21 (C). This principle is also followed in other jurisdictions. See for example, *Roebuck v Edmunds* 1992 *Scots Law Times* 1055 1056; Platt 1996 *Baylor Law Review* 1197 1199 *et seq* (the latter in respect of the position in the United States of America). Therefore the broad statement in *Soteriou v Retco Poyntons supra* that “refusal imports an offer” and that the grantor is obliged to make a *bona fide* offer on terms which he would be prepared to accept from a third party, should not mean that the grantor has an enforceable duty to make such an offer upon any manifestation of a desire to sell. In any event, on the facts of that case, the grantor had already concluded a contract with a third party. The remarks on the position prior to conclusion of such a contract are, strictly speaking, *obiter*.

<sup>28</sup> See par 7 2 2 2 3 *infra*. See also paragraphs 5 1 1 (II) and 5 2 2 1 1 (III) *supra*.

Presumably, the main argument for a lesser manifestation as a trigger event, would be the protection this affords against losing the benefit of the main contract to a *bona fide* third party who has commenced negotiations with the grantor. However, society's and the grantor's interest in the minimum possible limitation on his capacity to deal freely with his property is not overridden by a need to protect the holder in this regard. Prior to actual breach of the *obligatio non contrahendo cum tertii*, the holder's interests could be protected by prohibitory interdict, which could be served on interested third parties and, where relevant, the Registrar of Deeds.

Therefore the default rule should be that nothing short of a valid contract or offer should constitute breach of a preference contract or otherwise trigger a right to contract.

An important question that arises concerns the possibility of curing the breach by cancellation of the third party contract or withdrawal of an offer to her. If cure should be allowed, does this also apply to the period after exercise of the holder's right?

A related question concerns the effect of a condition suspending the third party contract until non-exercise of the holder's right. A similar aim is served by a *lex commissoria* in the third party contract that arises upon exercise of the holder's right. Should these mechanisms allow the grantor to restore the *status quo ante* the breach?

*Wissekerke v Wissekerke*<sup>29</sup> is often quoted as authority for a statement that the grantor of a right of first refusal is not obliged to keep an offer open, but may withdraw an offer to the holder as long as the grantor no longer wishes to contract at all.<sup>30</sup> However, the court in *Wissekerke*<sup>31</sup> was not required to decide on the revocability of offers in respect of preference contracts generally. Firstly, it was common cause that the grantor could withdraw the offer before acceptance thereof.<sup>32</sup> Secondly, the

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<sup>29</sup> *Supra*.

<sup>30</sup> Christie *Contract* 62; Reinecke & Otto 1986 *TSAR* 18 33; Floyd 1986 *THRHR* 253 259; Janisch 1990 *Responsa Meridiana* 434 444.

<sup>31</sup> *Supra*.

<sup>32</sup> 650D.

grantor's offer was made voluntarily. Other considerations may apply when the grantor has breached the preference contract by contracting with a third party.

The typical aspect of a preferential right to contract is that the grantor is totally free in her decision whether to contract. There is therefore a strong case that the grantor who does not want to contract anymore, is not obliged to contract with the holder. The proposition laid down in *Wissekerke v Wissekerke* in respect of voluntary offers to the holder should therefore certainly be accepted.<sup>33</sup> But should this also apply in the case of a contract or offer made in breach of the preference contract?

The desirability of construing restraints on alienation as narrowly as possible could, once again, be relied upon in favour of allowing the grantor to cure the breach. The holder still retains a preferential right to transact after cure, and should be content with restoration of the *status quo ante* the breach, at least as long as the holder has not exercised the right.<sup>34</sup>

On the other hand the holder may argue that withdrawal from the third party contract enables the grantor, who has cynically breached the preference contract once, to secretly contract with and give transfer to a *bona fide* third party and so thwart the holder's right.

Interestingly, Van der Keessel<sup>35</sup> states that the law in Holland was initially that upon a completed sale to a third party, the owner was bound to the *ex lege naastingsreg* and that the holder's remedies remained in spite of a purported withdrawal from the sale. However, later legislation allowed a *bona fide* withdrawal from the sale before

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<sup>33</sup> This is also the position in England and Scotland. See *Smith v Wilson* 1901 9 SLT 137 and *Stevenson v Wilson* 1907 SC 445, accepted by the House of Lords in *Lyle & Scott v Scott's Trustees; Same v British Investment Trust Ltd* 1959 AC 763 775 780 and *Roebuck v Edmunds* (OH) 1992 *Scots Law Times* 1055.

<sup>34</sup> This is the argument relied on by the Scottish Outer House in *Roebuck v Edmunds* (OH) 1992 *Scots Law Times* 1055. The grantor conceded that the holder was entitled to have the transfer to the third party set aside, and the court thereupon refused to allow an order that the holder is entitled to purchase the object at the price agreed with the third party.

<sup>35</sup> *Theses Selectae* 3 16 2.

exercise of the *naastingsreg*. Floyd<sup>36</sup> seems to have overlooked this text by relying solely on Voet 18 3 24 (on the *ex lege naastingsreg*) for his statement that the intention to sell triggers the right even where the sale to the third party is later cancelled or even where the third party sale is subject to non-exercise of the right of pre-emption. Is there any reason why this legislation which applied to *ex lege naastingsregte* should not also apply to contractual preferential rights? Perhaps it could be argued that this provision was adopted to specifically limit the application of *ex lege naastingsregte*, which came to be regarded as unfair limitations on contractual freedom,<sup>37</sup> rather than to arrive at a fair solution for all preferential rights to contract.

Turning to other jurisdictions, it appears that English law would allow the grantor to cure the breach. In the English case of *Lyle & Scott v Scott's Trustees; Same v British Investment Trust Ltd*,<sup>38</sup> the grantor did not withdraw from the third party contract on the facts. Yet the judges gave some indication that such a complete withdrawal would save the grantor from an order which allows the holder to enforce the main contract. For example Viscount Simonds stated that "I regard Scott's trustees as desirous of transferring their ordinary shares *unless and until their agreement with Mr Fraser has been abrogated*. Of this at least one acid test would be the return by them of the price they have received."<sup>39</sup>

By contrast, the German code does not allow a withdrawal from the third party contract to influence the holder's power to exercise the *Vorkaufsrecht*.<sup>40</sup> It has been

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<sup>36</sup> 1986 *THRHR* 253 258.

<sup>37</sup> Van Bynkershoek *Quaestionum Juris Privati* 3 13 stated that "every form of retraction, which is nowadays in use, ... savours of the utmost unfairness, inasmuch as it robs the purchaser of his honestly acquired right in order to prop up a policy which is of far less importance than the enforcement of contracts."

<sup>38</sup> 1959 AC 763.

<sup>39</sup> 774 (my italics). Cf also Lord Reid's statement at 782 ("and the step ordered could only be undone after that breach has ceased.") See also *Roebuck v Edmunds* 1992 *Scots Law Times* 1055 1056 (decision of the Scottish Outer House).

<sup>40</sup> § 465 (previously § 506): "Eine Vereinbarung des Verpflichteten mit dem Dritten, durch welche der Kauf von der Nichtausübung des Vorkaufsrechts abhängig gemacht oder dem Verpflichteten für den Fall der Ausübung des Vorkaufsrechts der Rücktritt vorbehalten wird, ist dem Vorkaufsberechtigten gegenüber unwirksam."

argued, however, that this provision is unfair in cases where the holder only has a prohibitive purpose and not also an interest in obtaining the object.<sup>41</sup> If the grantor cures the breach, the holder's prohibitive purpose is not thwarted.

It is submitted that breach should be curable, at least until a valid exercise of the preferential right has taken place. This is consistent with the policy goal that restraints on alienation should be restrictively construed. If the grantor is allowed to cure even after exercise of the right, this effectively means that South African law should regard the preferential right as only a negative one, as a grantor faced with the possibility of an order to transfer the property to the holder, would inevitably rely on a purported withdrawal from the third party contract. Whether the preferential right should be regarded as only a negative right will be considered under the next rubric. Certainly, allowing the holder to cure after exercise of the holder's right would cause uncertainty and prejudice to the holder who may already have prepared for performance under the substantive contract.

If the need to protect the holder against further cynical breaches should in fact favour a remedy entitling the holder to obtain performance of the main contract, the law should probably also disregard provisions in the third party contract allowing a withdrawal upon exercise of the holder's right as far as the holder's rights are concerned.<sup>42</sup> These provisions arguably leave open the possibility that the grantor would contract and perform to a *bona fide* third party the next time, so that the holder is indeed not protected.

Another issue arising in the context of breach is whether preference contracts should create an *obligatio non contrahendo cum tertii* where this is neither specifically provided for nor excluded. Should a simple grant of a "right of first refusal" or "right of pre-emption" allow or prohibit the grantor to contract with a third party first?<sup>43</sup>

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<sup>41</sup> Burkert "Die Reichweite des § 506 BGB" 1987 *NJW* 3157.

<sup>42</sup> Obviously, the grantor would be entitled to rely on such a clause vis-à-vis the third party.

<sup>43</sup> It might be argued that the terms "pre-emption" and "first refusal" by themselves point to an obligation to first allow the holder to contract. In Germany, however, rights of pre-emption or *Vorkaufsrechten* do allow the grantor to contract with a third party first, but the holder thereafter has

This issue has already been canvassed in the discussion of the advantages of the normal *Vorhand* of German law above the *Vorkaufsrecht*.<sup>44</sup> The *Vorhand* creates an *obligatio non contrahendo cum tertii*, whereas contracting with a third party is not breach of a *Vorkaufsrecht*, but is instead the necessary neutral condition for enforceability of the holder's right to contract.

The disadvantage of a preference contract with no *obligatio non contrahendo cum tertii* is that the holder cannot be forced to decide whether to exercise the right until after conclusion of a contract with a third party. Apart from the effort and costs of concluding a formally valid contract with a third party, the third party must then wait for the holder's decision, knowing that she might lose the opportunity to contract with others, for example, to buy other suitable properties that might come onto the market in the meantime. Many interested third parties might be scared off by this prospect. In other words, the existence of a pre-emptive right is likely to deter potential contractants from concluding a contract because it reduces their expected return from the costs they incur in negotiating and concluding a contract.<sup>45</sup> Owners who realise this in advance are likely to prefer a right to force a decision by the holder before a sale to a third party. Then the holder need merely be informed of the material terms on which the owner is prepared to contract. It is therefore not surprising that a number of German model contracts recommend the inclusion of both a *Vorhand* and

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the preferential right or "first refusal" to contract on the terms agreed. For South African examples of contracts which do not clearly state that the grantor should first give the holder a chance to contract, see *Cohen v Behr* 1946 CPD 942 (the agreement provided that the holder shall have the first refusal to purchase the thing for a certain period); *Aronson v Sternberg (Pty) Ltd* 1985 1 SA 597 (A) and *Soteriou v Retco Poyntons* 1985 2 SA 922 (A). In *Skinner v Goldberg* 1943 WLD 42 the court simply stated that the holder's "request... for the right of pre-emption...was granted...". Cf *Hartsrivier Boerderye (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T) (if the grantor would decide to sell the thing, the holder shall have the first right of refusal to buy) and *Dithaba Platinum v Erconovaal supra*, where a similar clause was agreed upon.

<sup>44</sup> Par 4 1 2 *supra*.

<sup>45</sup> Mitchell 2001 *University of Chicago Law Review* 985 988. This consideration may deter third parties despite an *obligatio non contrahendo cum tertio*, but the potentially wasted costs and efforts of the third party increases when he first has to conclude a contract to oblige the holder to decide on exercise.

*Vorkaufsrecht* clause, so that an *obligatio non contrahendo cum tertii* is indeed created.<sup>46</sup>

Moreover, the policy concerns of the drafters of the *BGB Vorkaufsrecht* could largely be accommodated within a construction encompassing an *obligatio non contrahendo cum tertii*. It will be recalled that the drafting commission felt, firstly, that before conclusion of a contract with a third party, there is no certain basis for the decision of the holder whether to exercise the right.<sup>47</sup> In other words, the terms on which the holder may acquire the object was considered to be too unclear if anything short of a contract triggers the right.<sup>48</sup> The drafting commission accordingly rejected proposals that the grantor should be obliged to make an offer to the holder before she has contracted with a third party.<sup>49</sup> Their concern is sufficiently met by a default rule that only a contract with (or offer to) a third party triggers the holder's right, and the absence of an *obligatio non contrahendo cum tertii* does not affect this concern. Secondly, they argued that there is a danger of the grantor faking an offer that she knows the holder would not accept if some circumstance short of a binding contract could force a decision about exercise of the holder's right. This would force the holder either to buy the property at such exorbitant terms or to waive the *Vorkaufsrecht* by failing to exercise it.<sup>50</sup> The drafters' concern about the circumvention of the holder's right by a fake offer could be addressed by a default rule that the holder's right does not terminate on the mere rejection of an offer, but

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<sup>46</sup> Par 4 1 2 *supra*.

<sup>47</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 16; Schurig *Das Vorkaufsrecht im Privatrecht* (1975) 56 with reference to *BGB Motive II* 345 *et seq.*

<sup>48</sup> That is, if a "manifestation of a desire to sell" would trigger the right, which does not amount to a contract with or offer to a third party, it would be disputable on what terms the holder would be entitled to contract with the grantor. Some vague standard such as "reasonable terms" would then be required, which would invariably lead to disputes.

<sup>49</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 16-17; Schurig *Das Vorkaufsrecht* 56; Soergel & Siebert (Huber) § 504 RdNr 17 with reference to *Protokolle II* 96 *et seq.* See also BGHZ 115, 355 (decision of the *Bundesgerichtshof* of 11.10.1991) 338 *in fine*; Hueck "Erwerbsvorrechte im Gesellschaftsrecht" in Paulus *et al* (eds) *Festschrift für Karl Larenz* (1973) 749 752, 755; Michalski "Der Mietvorvertrag" 1999 *Zeitschrift für Miet- und Raumrecht* 141 146.

<sup>50</sup> Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 19; Schurig *Das Vorkaufsrecht* 56; Weber "Der Optionsvertrag" 1990 *Juristische Schulung* 249 251.

only once the grantor subsequently contracts with a third party at the terms offered to the holder.<sup>51</sup>

In any event, it appears that the normal understanding of South African lawyers is that preference contracts indeed generally require the grantor to give the holder a chance to contract first before contracting with a third party.

To summarise, absent contrary agreement, preference contracts that do not predetermine the main price are breached when the grantor concludes a contract with a third party in breach of the preference contract, or validly offers to do so. The grantor may cure this breach, at least until exercise of the holder's right.

7 2 2 1 2      Should the holder be entitled to performance of the main contract on breach?

There are compelling policy reasons both in favour and against allowing the holder to ultimately enforce performance of the main contract upon breach.

First the policy considerations against allowing such a "positive" remedy will be considered.

They centre on the now familiar argument that restraints on alienation should be construed as narrowly as possible.<sup>52</sup> It has been shown that it is logically possible to

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<sup>51</sup> This matter is dealt with in par 7 3 2 3 *infra*. See also par 5 2 2 1 1 (II) *supra*. Henrich's proposal of this default rule was discussed in more detail in par 4 1 2 1 5 *supra*. A third concern of the drafting commission was that, as long as no binding contract with the third party has been concluded, the holder is not in danger of losing his *Vorkaufsrecht* and should therefore not be forced to decide about the exercise of his right before that point (Henrich 19, with reference to Protokolle II 96 *et seq*). However, the grantor, holder and third parties' interests are most fairly balanced if the holder can be forced to decide about the exercise of his right before conclusion of a third party contract, as long as the material terms on which the grantor intends to contract with the third party and the identity of the third party is disclosed to the holder.

<sup>52</sup> See par 7 3 2 1 1 *supra*

construe preference contracts as negative contracts only, which do not create a right to contract, but only an *obligatio non contrahendo cum tertii* terminating upon rejection of an opportunity to match a third party offer.<sup>53</sup> This is the narrowest possible construction of these contracts. Such contracts afford a real preference for the holder, and cannot be said to be economically useless. The *quod minimum* rule of interpretation would have us place the least onerous obligation on the promissor. Once the grantor's obligation is regarded as a negative one only, coherency and consistency requires that specific performance thereof consists only of a prohibitory interdict, coupled with an order setting aside any performance to a third party with prior knowledge of the holder's right.<sup>54</sup> If the holder wanted a stronger right, he should have bargained for a conditional right to contract.

Furthermore, a prohibitory interdict or order setting aside performance to a *mala fide* third party, restores the *status quo ante*, which the holder has been content with since conclusion of the preference contract.

An argument that these remedies are ineffective because of the likelihood of another cynical breach by the grantor, this time transferring real rights in the object to a *bona fide* third party, can be met by three counter-arguments. Firstly, the holder could adequately protect himself against that possibility in most cases, so that the "negative" remedies would effectively protect the holder's right to be preferred. In the case of land, the holder can register the right of pre-emption to prevent transfer to a *bona fide* third party.<sup>55</sup> In the case of company shares, no alienation contrary to the right of pre-emption in the registered statutes would be effective, not even to a *bona fide* third party.<sup>56</sup> In the case of publishing contracts, a third party publisher would probably be found to have known of the holder's preferential right, as preference agreements are widely used in that industry. A third party publisher would rarely be willing to

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<sup>53</sup> See par 5 1 *supra*.

<sup>54</sup> The latter is of course available on the basis of the doctrine of notice. See *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd supra*; *Tschirpig & Another v Kohrs* 1959 3 SA 287 (N).

<sup>55</sup> *Ex parte Zunckel* 1937 NPD 295; West "Pre-emptive rights proper and those in the form of conditions" 1997 *De Rebus* 531.

<sup>56</sup> *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 4 SA 15 (SCA) 24 par 17.

contract with a published author without confirming with the previous publisher that it holds no preferential right. In other cases, the holder could stipulate a penalty to dissuade the grantor from breaching the contract. In a number of economic contexts, holders are sophisticated parties with sufficient bargaining power to be expected to protect themselves in this manner. Franchisers, for example, often provide for rights of pre-emption in their favour in franchise contracts. Secondly, grantors would in any event very rarely contract with a third party in breach of the preferential right without making the third party contract subject to non-exercise of the preferential right. In most other cases where the grantor breaches the preference contract cynically, transfer to a *bona fide* third party would already have taken place when the holder learns of the breach, so that only damages could be claimed anyway. In other words, the holder may lose the object through cynical breach and transfer to a *bona fide* third party regardless of how the preference contract is construed and which remedies are available.

Where the holder has sold but not yet transferred to a *bona fide* third party, it could be questioned why the holder's interest in obtaining the object should be preferred above the innocent third party's right under the contract of sale.<sup>57</sup> There are valid policy arguments in favour of protecting the innocent third party above the holder. *Inter alia*, it can again be pointed out that the holder could often have taken steps to inform third parties of his right, such as registration in the deeds office in the case of immovables.

Nevertheless, with some exceptions, South African courts, including the Supreme Court of Appeal, have held that conflicting claims to the same asset based on personal rights should be resolved by application of the maxim *qui prior est tempore, potior est iure*, provided there are no personal circumstances which affect the balance of equities.<sup>58</sup> This means that the holder is entitled to an interdict prohibiting

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<sup>57</sup> This was an argument relied upon by the Austrian Supreme Court (*Obersten Gerichtshof*) as to why only damages could be granted upon breach of a preference contract in its decision of 3 October 1972 reported in 1974 *Juristische Blätter* 204 206.

<sup>58</sup> See, for example, *Botes v Botes* 1964 1 623 (O); *Barnhoorn v Duvenhage* 1964 2 SA 486 (A); *Krauze v Van Wyk* 1986 1 SA 158 (A); *Wahloo Sand BK en Andere v Trustees, Hambly Parker Trust*

performance of the conflicting contract between the grantor and third party, even in terms of the negative or bare preference construction.<sup>59</sup> In other words, South African law allows the third party's right to be trumped by the holder's in any event.<sup>60</sup>

Therefore it could be argued that protection of the *bona fide* third party is irrelevant in the choice between the negative or bare preference construction and the construction which entitles the holder to specific performance of the main contract upon breach. Neither construction protects the third party's interest to obtain performance of the contract with the grantor.

The application of the maxim *prior est tempore, potior est iure* in this context has been criticized, not only for lack of authority for the application of this maxim to personal rights,<sup>61</sup> but also because there is no theoretical foundation for the maxim in

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*en Andere* 2002 2 SA 776 (HHA); *Kerr Contract* 594-597; *Kerr Sale and Lease* 411; *Lubbe & Murray Contract supra* 94; Van der Merwe "Nemo plus iuris..." 1964 *THRHR* 300 302-303. However, there have been decisions where no preference was given to an earlier personal right, such as *Gardner v Executor of Jones* (1899) 16 SC 206, *Kohling v McKenzie* (1902) 18 SC 287, *Hofgaard v Registrar of Mining Rights* 1908 TS 650, *Ex parte De Wet* (1910) 20 CTR 305 and *Ex parte Kruger* 1936 (2) PH A 56 (C).

<sup>59</sup> Floyd 1986 *THRHR* 253 264. However, Floyd wrongly relies on *Smith v Momborg* 1895 SC 295 for his general statement that the holder may prevent delivery to the third party by interdict. On the facts, the third party was aware of the holder's prior right so that the doctrine of notice applied.

<sup>60</sup> Some writers base this result on the view that the doctrine of notice operates against a third party purchaser who may have been unaware of the prior right at conclusion of his contract, but became aware thereof before transfer. *Cf* Cooper *The South African Law of Landlord and Tenant* 2<sup>nd</sup> ed (1994) 286-7 and authorities there cited and De Wet & Van Wyk *Kontraktereg en Handelsreg vol 1* 5<sup>th</sup> ed (1992) 377-378 in the context of *huur gaat voor koop*. There is authority to the contrary (such as *Kessoopersadh v Essop* 1968 4 SA 610 (D) 614, the minority in the appeal of that case reported in 1970 1 SA 265 (A) 274 (the majority left the question undecided), *Total SA v Xypteras* 1970 1 SA 592 (T) 598 and Wille *Landlord and Tenant in South Africa* 5<sup>th</sup> edition (1956) 99), but the authority on which the cases are based have been questioned (Cooper *Landlord and Tenant* 286).

<sup>61</sup> Lubbe 1986 *Annual Survey* 145 *et seq*; Mulligan "Double Sales and Frustrated Options" 1948 *SALJ* 564; Mulligan 1953 "Double Sales: A Rejoinder" 1953 *SALJ* 299 *et seq*; Mulligan "Double, Double Toil and Trouble" 1954 *SALJ* 169. *Cf* Scholtens "Double Sales" 1953 *SALJ* 22; Scholtens "*Difficiles Nugae* - Once Again Double Sales" 1954 *SALJ* 71; Burchell "Successive Sales" 1974 *SALJ* 40; Van Zyl "Dubbele Verkopings en die Kennisleer: Word *Bona fides* Vereis ten tye van sowel

this context,<sup>62</sup> nor any persuasive argument based on fairness which favours the prior right holder.<sup>63</sup> It appears that supporters of the maxim in this context wrongly assume that the grantor's capacity to contract or indeed her ownership is limited, even against *bona fide* third parties, by a contract creating only personal rights.<sup>64</sup> As the creation of merely personal rights are not accompanied by publicity, so that the holder of the later right could not have known of the earlier one, there is no clear equity in according priority according to the chronological order of the claims.<sup>65</sup> Accordingly, it has been persuasively argued that a better approach is rather to insist on application of the normal principles on specific performance (which also applies to the claim for a prohibitory interdict, as it constitutes specific performance of an *obligatio non faciendi*).<sup>66</sup>

What are the policy reasons for not limiting the remedies for breach of a preference contract to damages and restoration of the *status quo ante*?

Even where the holder is not primarily interested in obtaining the object, but rather in the power to ward off unwanted third parties, the grantor should know that the holder has an interest in concluding the main contract on breach. The preference contract should fulfil this warding off function by allowing the holder the choice to contract with the grantor rather than allowing a third party to do so.

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Kontraktluiting as Lewering?" in Joubert (ed) *EM Hamman – Gedenkbundel* (1984); Lambiris *Orders of Specific Performance and Restitutio in Integrum in South African Law* (1989) 84-93.

<sup>62</sup> Lubbe 1986 *Annual Survey* 145 146-147;

<sup>63</sup> Mulligan 1948 *SALJ* 577.

<sup>64</sup> Van der Merwe 1962 *THRHR* 300 302-303; 305-306. This is criticised by Lubbe 1986 *Annual Survey* 145 147.

<sup>65</sup> Lubbe 1986 *Annual Survey* 145 147. Cf the *Oryx* case where the court confirmed the publicizing of a proprietary interest in an asset as a pre-condition for its operation against third parties (910H, 913E-F), and based the doctrine of notice on the satisfaction of this principle.

<sup>66</sup> Lubbe 1986 *Annual Survey* 145 147. This is also the view of the minority (per Botha AJA) in *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd supra* 922. Cf *Crundall Brothers (Pvt) Ltd v Lazarus NO* 1991 3 SA 812 (ZH) 428H; Lubbe 1992 *Annual Survey* 100 106.

Allowing the holder a right to conclusion and performance of the main contract upon breach, enables the court to arrive at a concretely fair outcome on the special facts of each case, which would not be the case if the holder is invariably limited to damages or a prohibitory interdict upon conclusion of a contract with a *bona fide* third party. The court's discretion to award or refuse specific performance means that fairness towards the third party as well as towards the holder is the primary consideration in deciding between their competing claims. For example, if there is evidence that the holder of a right of pre-emption merely wants to obtain the object to resell it, whereas the third party requires that specific object for a personal purpose, it would be fair to refuse the holder specific performance and grant damages for loss of profit on the resale.<sup>67</sup> The situation would often be reversed, for example where the third party is a trader whereas the holder has a sentimental (for example, familial) interest in obtaining the object, so that damages to the third party and specific performance to the holder would be the fairest outcome. If the court cannot enforce performance of the main contract in favour of the holder in such a situation, justice is arguably not done. The court should consider the following circumstances in exercising its discretion. Which of the parties has a personal interest in obtaining the object that cannot be compensated by damages? What could the holder have done to protect her own interests and to warn the third party of the preferential right? Why did the holder not do this? In the case of land, was the holder in occupation, for instance, under a lease? What enquiries did the third party make in such a case? Should the chronological order of the competing claims also be a factor if no other applies? This has been said to be fair as the holder of the preferential right to contract dealt with a *bona fide* seller, whereas the third party buyer "had the misfortune to deal with a *mala fide* seller."<sup>68</sup> In England, the court will not compel a defendant specifically to perform an agreement when the result would be too compel him to commit a breach of a prior agreement with another person.<sup>69</sup> Although this cannot be equated with the maxim of *prior est tempore, potior est iure*, it is based on the same principle. A similar explanation is given by Cooper as to why knowledge by a purchaser of a prior

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<sup>67</sup> For a similar situation, see the American case of *Miller v Le Sea Broadcasting Inc* 87 F3d 2241 7th Cir 1996.

<sup>68</sup> *Lambiris Specific Performance and Restitutio in Integrum* 87.

<sup>69</sup> *Willmott v Barber* (1880) 15 ChD 96.

personal right before transfer is sufficient for the operation of the doctrine of notice.<sup>70</sup>

He states that

“The correct view is that by taking transfer the second purchaser assists the seller to commit a breach of the first contract, whereby the second purchaser commits a delict, namely inducement of breach of contract.”<sup>71</sup>

An alternative approach would be to give priority to the party who initiated proceedings for specific performance first. Perhaps this fall-back position could be justified on the basis that the other party's delay indicates that specific performance is not as important to him. Both this approach and the insistence on *prior est tempore, potior est iure* as the fall-back position are in fact equally mechanical. In any event, the point of departure should remain the application of the normal principles of specific performance. This creates sufficient leeway to reach a fair solution in each specific case.

In response, it can still be argued that the availability of merely a prohibitory interdict is sufficient to achieve a fair result between the holder, the third party and the grantor whilst also serving the public interest in leaving the grantor as free as possible to deal with her property to her best advantage. Where the holder has a personal, for example familial, interest in the object, it would still be fair towards all parties to prohibit transfer to the third party, who would be awarded damages in compensation. As far as the holder is concerned, the prohibitory interdict restores the *status quo ante* the breach. It could only be regarded as unfair as between the holder and grantor if one argues that the grantor should be punished more harshly for breaching the contract, which is not generally regarded as a valid aim of contract law rules.

However, it could be argued that a prohibitory interdict or order setting aside a transfer to a *mala fide* third party does not in fact adequately protect the holder's interests by restoring the *status quo ante*. It must be remembered that the grantor's breach would in most cases be deliberate. A grantor who has deliberately breached a

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<sup>70</sup> 287.

<sup>71</sup> *Ibid.*

*non facere* duty can be expected to flout this duty again in the future. There is therefore a very great risk that the grantor may try the same with another *bona fide* third party and give transfer before the holder is able to prevent that by interdict. In this sense, a prohibitory interdict and setting aside of a *mala fide* transfer are ineffective remedies to protect the *status quo ante* and therefore the holder's interests.

Granting a stronger remedy to the holder should also not be seen as “punishment”, but as discouraging breach as conduct detrimental to the interest of society, a policy consideration which courts in South Africa have taken into account in the formulation of default contract rules.<sup>72</sup>

In response to the argument that the holder can often take steps to make the remedies aimed at restoring the *status quo ante* effective, it should be noted that there is not much a holder can do to protect his right against *bona fide* third parties in the case of movables such as family heirlooms. A preferential right to conclude a transaction other than sale can generally also not be safeguarded by registration. To expect the holder to stipulate a penalty is often unrealistic due to ignorance of this possibility or the balance of bargaining power. Proponents of the strictly bare preference construction may reply that if the grantor has the greatest bargaining power, this is even more reason to construe the preference agreement in a manner that the grantor would most likely agree to, namely so as to restrict the grantor's freedom to deal with her property as she pleases as little as possible. As such an interpretation does not give rise to exploitation of the holder, there is no good reason for departing from the likely consent of the grantor.

Proponents of the purely negative preference contract acknowledge, however, that the holder may claim damages to place him in the position that he would have been in had the grantor performed the main contract.<sup>73</sup> This acknowledges the need to protect the holder's interest in obtaining performance of the main contract. If there is not in fact

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<sup>72</sup> Vorster 157 *et seq.* See also at 30 *et seq.* for examples from England. Even Posner states that “conventional pieties” such as keeping promises reduce transaction costs (“Utilitarianism, Economics and Legal Theory” 1979 *Journal of Legal Studies* 103 123).

<sup>73</sup> See for example Henrich *Vorvertrag, Optionsvertrag, Vorrechtsvertrag* 367-368.

a duty on the grantor to conclude or perform the main contract with the holder at some point, this manner of calculating damages is difficult to explain. Therefore it is logical to allow an order that the grantor perform the main contract, subject to the courts' discretion to refuse specific performance. As was mentioned before, proponents of the bare preference construction could reply that the award of damages is not inconsistent with the absence of an enforceable duty to contract with the holder.<sup>74</sup> The claim for damages aims to place the holder in the position it would have been in had the contract not been breached. The grantor could have fulfilled the preference contract in one of two ways. Firstly by not contracting with anybody and, secondly, by contracting with the holder. As the first situation is unlikely because the breach clearly shows the grantor's wish to contract with somebody, it is more logical to compensate the holder on the basis of the second scenario. In other words, the holder claiming damages can usually prove on a balance of probabilities that if the grantor had obeyed the contract, the grantor would have contracted with the holder.<sup>75</sup>

To the arguments in favour of a remedy aimed at performance of the main contract, could be added the fact that Henrich's main authority for construing the "normal *Vorhand*" as enforceable by negative remedies only is a decision of the *Bundesgerichtshof* on a publishing contract.<sup>76</sup> However, there are special reasons for limiting a publisher to such negative remedies that do not apply in other contexts. Firstly, it would normally be too late to grant the holder a remedy which ultimately entails specific performance of the eventual publishing contract, as a transfer of the intellectual property rights often takes place simultaneously with the conclusion of the publishing contract with that third party.<sup>77</sup> As these rights are analogous to real rights, the *bona fide* third party is in a stronger position than the holder. It is therefore no wonder that such a remedy was not even considered. Secondly, if the author could be forced into a publishing contract with the holder this would jeopardise the very close working relationship that such contracts require. This could explain the courts'

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<sup>74</sup> Paragraph 5 1 *supra*.

<sup>75</sup> See paragraph 5 1 *supra* for Henrich's different explanation of this method of calculating damages in the case of the normal (negative) *Vorhand*.

<sup>76</sup> BGH 22, 347.

<sup>77</sup> See Bappert & Maunz *Verlagsrecht* (1952) § 1 RdNr 45 with reference to BGH 1962 *NJW* 1197 and RGZ 108, 58.

wariness to force the author into such a contract, instead of merely granting negative remedies or damages. Thirdly, the courts could be swayed by the vulnerable bargaining position of an author as grantor as against the publishing company to construe the preferential right as narrowly as possible. This is often not a relevant consideration in other contexts.

Accordingly, there are compelling policy reasons both in favour of and against allowing enforcement of performance of the main contract upon the grantor contracting with a third party.

In my view, all the interests and policy considerations at stake are most fairly balanced by a default rule that the holder is allowed to enforce performance of the main contract upon breach, subject to the court's usual discretion, as long as breach refers to nothing less than a valid offer to contract with a third party. The grantor's interest in the minimum possible curtailment of his freedom to deal with his property and to obtain the best possible price for it, is sufficiently protected by this definition of breach, as well as by the default rule that the grantor may cure that breach until exercise of the preferential right by the holder. This default rule provides sufficient scope for the grantor to sound out the market freely, which is the fundamental policy justification of a limited interpretation of the holder's rights. However, once the grantor has deliberately breached the preference contract, he has gone beyond sounding out the market, and the justification for a limited interpretation falls away. In such a situation, it is unfair to restrict the holder to a claim for damages or a prohibitory interdict. Damages would often not sufficiently compensate the holder, especially where she has a non-pecuniary interest in conclusion of the main contract.<sup>78</sup> A prohibitory interdict would also often be ineffective against a grantor who has already wilfully breached the preference contract and who may be antagonised even further by the preceding litigation. The innocent third party's interest in obtaining performance of her contract could be balanced against the holder's interest on the equities of each specific case under the equitable discretion of the court to refuse specific performance. This equitable discretion is also sufficient to protect grantors

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<sup>78</sup> An example would be a strong sentimental interest in obtaining a family heirloom hitherto held by the grantor on condition that family members have the first chance to buy it from him.

such as authors, who have a strong interest in not being forced into a contract with the holder against their will due to the close working relationship which such a contract requires.

Even if the policy considerations relevant to the remedies for breach are in fact rather on a par, this does not provide sufficient justification for deviating from the present position of our law on this issue.<sup>79</sup> Ever since the *Oryx* case,<sup>80</sup> South African courts have accepted that the holder may ultimately enforce performance of the main contract upon breach of a preference contract.<sup>81</sup>

However, South African law is not totally clear on what circumstances would trigger such a remedy. Firstly, the *Oryx* case did not finally decide what would trigger the *Oryx* mechanism, leaving open the possibility that a grant of an option would do so in addition to a contract with a third party.<sup>82</sup> Secondly, the Supreme Court of Appeal, other courts and commentators have left open the possibility that an order for specific performance of the duty to make an offer is still available.<sup>83</sup> As noted before, many of these commentators and courts do not specifically limit the trigger event for such a

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<sup>79</sup> Cf Neels "Regsekerheid en die korrigerende werking van redelikheid en billikheid (deel 2)" 1999 *TSAR* 256 269 and "Regsekerheid en die korrigerende werking van redelikheid en billikheid (deel 3)" 1999 *TSAR* 484.

<sup>80</sup> *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd supra*.

<sup>81</sup> See paragraph 1 1 *supra*.

<sup>82</sup> 908F-G.

<sup>83</sup> This was assumed without deciding in *Hirschowitz v Moolman supra* 764G-H. However, this assumption may have been made because the application was launched before the decision in *Oryx*. See Lubbe 1985 *Annual Survey* 139. See also *Rogers v Philips* 1985 3 SA 183 (E) 187D which held that a right of pre-emption merely gives the holder a personal right to an offer by the owner. Commentators who still see a need for a remedy of specific performance in the traditional sense include Kerr *The South African Law of Sale and Lease* (1996) 410; Cooper *Landlord and Tenant* 144-146 and Reinecke & Otto 1986 *TSAR* 18 2. Cf also Van Rensburg & Treisman *The Practitioner's Guide to the Alienation of Land Act* (1984) 70-71; Lubbe 1982 *Annual Survey* 128 130; Floyd 1986 *THRHR* 253 267; Lotz "Purchase and Sale" in Zimmermann & Visser (eds) *Southern Cross: Civil Law and Common Law in South Africa* (1996) 386. Eiselen "*Soteriou v Retco Poyntons (Pty) Ltd* 1958 2 SA 922 (A)" 1986 *THRHR* 95 99 rejects the *Oryx* mechanism and advocates a remedy of specific performance in the traditional sense only.

remedy to the conclusion of a contract with or an offer to a third party.<sup>84</sup> Some specifically argue that a lesser manifestation of a desire to sell should be sufficient.<sup>85</sup>

However, there is authority for a default construction in terms of which the holder is allowed to enforce the main contract only upon breach in the form of an offer to or contract with a third party.

The *Oryx* case itself foresees an *obligatio non contrahendo cum tertii*,<sup>86</sup> whereas the holder may unilaterally create the main contract and pray for its performance on conclusion of a contract with a third party, and perhaps on the granting of an option.<sup>87</sup> This clearly implies that a lesser manifestation of a desire is insufficient.

The majority in *Owsianick v African Consolidated Theatres (Pty) Ltd*<sup>88</sup> (per Botha JA) did not unambiguously exclude the possibility of a positive remedy upon the grantor actually contracting with a third party. In his discussion of the *ius commune* texts on *naastingsrechte*, Botha JA emphasised that none of these texts grants the holder the right to obtain the object before conclusion of a contract with a third party.<sup>89</sup> This suggests that Botha JA does not totally exclude the possibility of a

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<sup>84</sup> See the writers mentioned in the previous footnote. See also Janisch 1990 *Responsa Meridiana* 434 442-443. Cf for example *Soteriou v Retco Poyntons supra* 932H *et seq.* By contrast, Reinecke & Otto 1986 *TSAR* 18 26 state that a lesser manifestation than a valid offer to the holder should not lightly be regarded as a trigger event.

<sup>85</sup> See par 5 2 2 1 1 with reference to Floyd 1986 *THRHR* 253 258-259, 264; Wessels JA in *Owsianick v African Consolidated Theatres* 327H: "Desire, like intention, resides in the mind, and its existence, sometimes settled and sometimes ephemeral, is to be determined in the light of the available, relevant evidential material, such as considered, or even unguarded confessions or other conduct which points unequivocally to its existence." This definition is quoted with approval by Du Plessis *Spesifieke nakoming* 16.

<sup>86</sup> 904D. Cf par 4 1 1 1 *supra*.

<sup>87</sup> The latter possibility was left open at 908F-G.

<sup>88</sup> 1967 3 SA 310 (A).

<sup>89</sup> See Botha JA's statement at 321H that Van Zutphen and Berlichius state that the grantee of a conventional *ius retractus* had under certain circumstances the right to retract the subject of his rights, but that is clear that such a right only came into existence when a sale in breach of his right had in fact been concluded with third party. This point is emphasised again at 322G-H.

positive remedy upon a sale in breach of the preference contract.<sup>90</sup> On the facts, the court did not need to consider the effect of an actual option contract or sale to a third party with immediate effect, because the grantor gave the third party an option which would only take effect after termination of the lease. The majority of the court did not find this indication of a desire to sell to be a breach of the obligation not to sell to third parties during the lease period.<sup>91</sup>

Interestingly, Van Rensburg & Treisman argue in effect that the *Hartsrivier* construction (which does not force the grantor to contract on a mere manifestation of a desire to contract) should be combined with the *Oryx* mechanism, as they mention both in their discussion of the present legal position, without branding them as alternative approaches.<sup>92</sup> They also state that the *Oryx* mechanism should be available only upon conclusion of a contract with a third party.<sup>93</sup>

Such a default regime furthermore reminds one of the combined *voorcoop* and *nacoop* procedures of *ex lege naastingsrechte* in some areas in Roman-Dutch times.<sup>94</sup> Under the *voorcoop* procedure, the owner could announce his intention to sell in a public place before the sale to a third party. This could be equated with a public invitation to make an offer. A family member as holder of a *naastingsrecht* could then declare his willingness to buy. This was the *voorcoop* procedure. However, if the owner failed to follow this procedure and sold directly to a third party, a holder of a *naastingsrecht*

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<sup>90</sup> However, Botha JA also stated at 322D-E that it is not clear that the right under a conventional *ius retractus* are in all respect similar to the right under an ordinary right of pre-emption. He also stated at 323B-C that *Van Zutphen* wrongly imported, in relation to a conventional “*voorkoopsreg*”, the legal position under the Dutch law of *naesting* or the *ex lege ius retractus*

<sup>91</sup> 323H-325C.

<sup>92</sup> 70-71.

<sup>93</sup> *Ibid.* See also Reinecke & Otto 1986 *TSAR* 18 26 who denies that a more informal indication of a desire to sell should allow the holder to accept the offer which they regard as embedded in preference contract. They advocate that a valid offer to a third party is required at least. *Cf Kerr Sale and Lease* 411. *Cf Skinner v Goldberg supra* in which the court decided that the date for calculating the damages is the date of conclusion of the contract with the third party (44). The implication could be that breach only occurred at that point and that up to that point the grantor need not have made an offer. See also *Ah Ling v Community Development Board & Others* 1972 4 SA 35 (E) 39C-G.

<sup>94</sup> See par 3 4 *supra*.

could still exercise the right in terms of the *nacoop* procedure, thereby stepping into the contract concluded with the third party. This suggests a construction that the owner was actually supposed to first offer the opportunity to contract to relatives before contracting with a third party (an *obligatio non contrahendo cum tertii* or negative obligation). If the owner did not obey this duty, the holder of the *naastingsrecht* could, only upon the owner contracting with a third party, obtain performance of the main contract on the same terms.

That some contracts considered in German case law and some German model contract handbooks contain a *Vorhand* and *Vorkaufsrecht* clause in one contract,<sup>95</sup> shows a need in practice for a type of preference contract which contains both an *obligatio non faciendi* and a positive remedy which applies only upon conclusion of a contract with a third party in breach of that obligation. The *Vorhand* clause adds the *obligatio non faciendi* to the contract, whereas the *Vorkaufsrecht* clause adds the remedy by which the holder can enforce the main contract upon conclusion of a valid contract with a third party.

In Austria, some courts have in the last few decades allowed the holder of a *Vorkaufsrecht* a remedy which ultimately leads to specific performance of the main contract upon breach in the form of a contract concluded with a third party,<sup>96</sup> whereas they only awarded damages before.<sup>97</sup> The reasons for this change of attitude is therefore interesting for the present debate. The relevant provision of the code does not provide for a *Vorkaufsrecht* in the sense in which this term is used in the *BGB*.<sup>98</sup> Instead it provides that where somebody sells under the condition that the buyer must offer the initial seller the “Einlösung” when he wants to sell, the initial seller has the

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<sup>95</sup> See par 4 1 2 *supra*.

<sup>96</sup> See for example, 1986 *Juristische Blätter* 509-511 or SZ 59/54 (decision of the *Obergerichtshof* of 20.3.1986) in which the court ordered the grantor to offer the object for sale to the holder. See also for example, SZ 36/128 in which the holder was held to be entitled to conclusion of the main contract with the grantor as well as to performance of that contract. Cf 1977 *Juristische Blätter* 94 95; 1983 *Juristische Blätter* 203 205.

<sup>97</sup> SZ 1/54 (2.9.1919); SZ 6/25 (22.1.1924); 1937 *Juristische Blätter* 387; SZ 23/356 (29.11.1950); SZ 38/148 (29.9.1965) = 1966 *Evidenzblatt* 69 (Nr 52).

<sup>98</sup> § 1072 *ABGB*.

*Vorkaufsrecht*.<sup>99</sup> In German law, this figure would rather fall under the *Vorhand* category.<sup>100</sup> Admittedly, the debate on whether the holder is entitled to a remedy which would ultimately entail performance of the main contract on breach is centred largely on the wording of § 1079 of the code, which only refers to damages upon breach.<sup>101</sup> Academic writers have for a long time criticised the narrow interpretation of § 1079.<sup>102</sup> They feel it is unfair to limit the holder's remedies to no more than an interdict or damages in the case of breach. However, some courts remain adamant that damages should be the only remedy.<sup>103</sup> Unfortunately, these court decisions and writers do not thoroughly discuss the relevant policy considerations, although a few are mentioned here and there.<sup>104</sup> A more formalistic or dogmatic argument that is mentioned is the anomalous consequences of allowing specific performance if the

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<sup>99</sup> *Ibid.*

<sup>100</sup> Schurig *Das Vorkaufsrecht* 53. However, a number of Austrian writers rely on the interpretation of the *BGB Vorkaufsrecht* for their interpretation of the Austrian figure. See, for example, Gschnitzer 1966 *Juristische Blätter* 253. Cf also Aicher in Rummel (ed) *Kommentar zum Allgemeinen bürgerlichen Gesetzbuch Band I §§ 1-1174 ABGB* 3<sup>rd</sup> ed (2000) § 1072. Schurig regards the equation of the Austrian *Vorkaufsrecht* with its German counterpart as *contra legem* (53). One difference between the Austrian and German *Vorkaufsrecht* according to the writers is that in Austria, the grantor may not only make an offer to the holder immediately upon contracting with a third party (like in Germany), but may also force a decision from the holder by making an offer before contracting with a third party, as long as a binding offer from a third party exists at that stage. (See eg Ehrenzweig *System des österreichischen allgemeinen Privatrechts 2. Band* 2<sup>nd</sup> ed (1928) 419).

<sup>101</sup> 1986 *Juristische Blätter* 509 510; 1974 *Juristische Blätter* 204 205; 1966 *Evidenzblatt* 69 (Nr 52); Rummel P 1974 *Juristische Blätter* 206-207; Faistenberger *Das Vorkaufsrecht: Zum Verkauf in Österreichischen Bürgerlichen Recht* (1967) 160. § 1079 provides that if the owner had not offered the holder the *Einlösung* (pre-emption), he is liable for all the holder's damages. By contrast, § 1079 also provides that in the case of a real right of pre-emption, the alienated object may be claimed from the third party and the third party is treated according to his reasonable or unreasonable possession.

<sup>102</sup> Gschnitzer 1966 *Juristische Blätter* 254; Faistenberger *Das Vorkaufsrecht* 159 *et seq*; Rummel 1974 *Juristische Blätter* 206-207. Although article 1072 defines a *Vorkaufsrecht* only as a *pactum adiectum* to a sale between the buyer as grantor and the seller as holder, the courts have long extended the reach of the *ABGB* rules to independent preference contracts. See eg 1974 *Juristische Blätter* 204; SZ 21, 247.

<sup>103</sup> 1974 *Juristische Blätter* 204 205 (decision of the OGH of 3.10.1972); 1986 *Evidenzblatt* 622 (Nr 148). See also Dittrich & Tades *Das Allgemeine bürgerliche Gesetzbuch* 35<sup>th</sup> edition (1999) § 1079 E 2.

<sup>104</sup> See, for example, the decision of the OGH discussed in n 57 *supra*.

grantor honours the preference contract by making an offer that the holder accepts, but not if the grantor deliberately breaches the preference contract by not making an offer to the holder.<sup>105</sup> In other words, the grantor who breaches to a lesser degree (by failing to perform the contract resulting from her voluntary offer), would be better off than the grantor who totally repudiates the preference contract by not making an offer. Another argument is that in the case of a *Vorkaufsrecht* that creates a real right, it has never been doubted that the holder may enforce performance against the grantor, although the registration of the *Vorkaufsrecht* does not cause a change in the legal relationship between the grantor and holder.<sup>106</sup>

In any event, there is some recognition of the proposed default regime in South Africa and other jurisdictions.

A juridical explanation of the holder's remedy will be considered later, for example, whether it should be regarded as specific performance of a duty to make an offer or as acceptance of an offer embedded in the preference contract. At this stage some further basic default rules surrounding the holder's remedy will be considered which should apply on the basis of policy considerations, regardless of the juridical explanation of the remedy. These rules are discussed here as they may possibly affect the cogency of the different juridical explanations.

#### 7 2 2 2 Other default rules

##### 7 2 2 2 1 Breach of the preference contract

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<sup>105</sup> Faistenberger *Das Vorkaufsrecht* 159; 1986 *Juristische Blätter* 509 511.

<sup>106</sup> 1986 *Juristische Blätter* 509 511; Aicher J in Rummel *ABGB supra* § 1079 RdNr (Rdz) 3; Faistenberger *Das Vorkaufsrecht* 161. However, this is said to be the result of the wording of § 1079 *ABGB* (second sentence). An argument which is irrelevant to South African law is that in Austrian law, a damages claim is always aimed primarily at *Naturalersatz*, that is granting the holder the opportunity of obtaining the object of the *Vorkaufsrecht*. See 1964 *Evidenzblatt* 239 (Nr 162) 240; Faistenberger *Das Vorkaufsrecht* 161; Binder in Schwimann (ed) *Praxiskommentar zum Allgemeinen Bürgerlichen Gesetzbuch samt Nebengesetzen Band 4 1. Halbband §§859-1089 ABGB* (1988) § 1079 RdNr 3.

What type of contract if concluded by the grantor would constitute a breach is a matter of interpretation. Parties to pre-emption contracts should preferably clearly define the types of contract that may and may not be concluded with third parties.

Logically, a sale in execution should not be regarded as breach of a right of pre-emption, as this is not a contract concluded by the grantor.<sup>107</sup> Where the creditor or sheriff is aware of the right of pre-emption, they would probably inform the holder of the intended auction anyway, as it is likely that she would pay a good price for the property.

Absent contrary agreement, South African case law accepts that a pre-emption contract only prohibits a sale to a third party, and not a donation, testamentary disposition or exchange.<sup>108</sup> Pre-emption contracts are therefore not understood as

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<sup>107</sup> *Bodasing v Christie* 1961 3 SA 553 (A) 561A-B. In this case, the contract of pre-emption predetermined the price as £2000, whereas the court held that the curator of an insolvent estate has a duty to sell to the highest bidder at an auction sale. Cf by contrast *Van Wyk v Posemann & Another* 1915 CPD 672 (although the court described the provision in the will as a “restraint on alienation”, it amounted to a right of pre-emption); *The Trustees of the Estate of AAJ Jonker v The Executor Dative of Adolf Jonker Deceased* 1R 334. In *Van der Berg v Transkei Development Corporation* 1991 4 SA 78 (Tk) the sale in execution was held to be conditional upon the right of pre-emption. On the issues surrounding involuntary sales and transfers by operation of law see further Platt “The right of first refusal in involuntary sales and transfers by operation of law” 1996 *Baylor Law Review* 1197 and Tew “Rights of First Refusal: The ‘Options’ That Are Not Options, But May Become Options” 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-67 *et seq.* The majority of American decisions do not consider a right of pre-emption triggered by such an involuntary sale.

<sup>108</sup> *Edwards (Waaikraal) GM Co Ltd v Mamogale and Bakwena Mines Ltd* 1927 TPD 288 294-295, with reference to Voet 18 3 10; *Dithaba Platinum v Erconovaal supra* 626D-E. In the latter case the third party contract expressed the price in money, but provided that the “purchase consideration” was to be “satisfied” by the allotment and issue of shares in the first respondent to the second respondent. The court regarded the contract as a sale and, as the holder was prepared to pay the monetary consideration expressed in the contract, he was entitled to enforce performance. The same should apply where the third party contract is a so-called “trade-in” contract, and a value had been placed on the property traded in (Floyd 1986 THRHR 253 266). The statutory *Vorkaufsrecht* in Germany is also not triggered by donation or exchange, although mixed exchanges have been regarded as sales where there is some indication that non-monetary consideration was added simply to evade the *Vorkaufsrecht*. See RGZ 101,101; BGHZ 49, 8; BGH WM 57, 1164; *Erman* (Grunewald) § 504 RdNr 8; *Soergel &*

granting the holder a right to contract, which the grantor may not thwart by agreeing to donate or exchange the property, but rather as a mere undertaking that the holder would be preferred above others if the grantor should sell. These decisions are consistent with the general principle that pre-emption contracts should be strictly construed. That the grantor is under no obligation to ensure that the holder is able to “exercise his right” in the sense of obtaining the property, appears from the fact that the grantor may alter, damage or destroy the object as she pleases as long as it has not been sold to a third party.

Where the third party undertakes to deliver goods and money, general principles dictate that the contract is a sale where this was the overriding intention of the parties, or, where their intention is unclear, when the money component is the most valuable of the two.<sup>109</sup> The same principle should apply where the consideration consists partly of a service to be rendered. If the intention of the parties is unclear, one should therefore consider whether the preponderant part of the third party’s obligations consists in the supply of goods or services.<sup>110</sup>

If application of these principles shows that the third party contract breaches the right of pre-emption, the question remains whether the holder's inability to perform a subsidiary obligation personal to the third party, disqualifies him from exercising his

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*Siebert* (Huber) § 504 RdNr 5; Münchener Kommentar (Westermann) § 504 RdNr 18. By contrast, an English court has regarded a donation as breach of a pre-emption contract. See *Gardner v Couitts & Co* 1968 1 WLR 179. This shows that our law generally has a narrower view of preference contracts than English law. In any event, in *Gardner v Couitts* the holder was given a conditional option to buy at a specified price. Such a right creates a stronger right than a normal preference contract, which perhaps influenced the court’s refusal to allow the holder’s right to be terminated by a donation. In addition, the German law *Vorkaufsrecht* is not triggered when the object becomes part of partnership assets (Schurig *Das Vorkaufsrecht* 131 and authorities there cited).

<sup>109</sup> *Wastie v Security Motors* 1972 2 SA 129 (C); *Mountbatten Investments (Pty) Ltd v Mahomed* 1989 1 SA 172 (D); *Janse van Rensburg v Grieve Trust CC* 2000 1 SA 315 (C); Voet 18 1 22; De Wet 314. On German law, see for example, NJW 96, 2321, where the object was “exchanged” for a large sum of money, an inexpensive piece of land and a worthless right to use another property. The court regarded this agreement as a trigger event. Under South African law, the agreement would in any event be regarded as a sales contract and not an exchange

<sup>110</sup> Cf *Elite Electrical Contractors v The Covered Wagon Restaurant* 1973 1 SA 195 (RA).

right. Where a monetary value can be placed on the goods or services, the holder should be able to exercise his right of pre-emption if he is willing and able to pay that amount. This would not prejudice the grantor.<sup>111</sup> In such a case, the parties can be said to have intended a sale. Even where no monetary value can be placed on the goods or services, the holder should be entitled to performance where the grantor would have concluded the third party contract without that personal obligation anyway.<sup>112</sup> This would be the case where it has simply been added in an effort to evade the holder's right, or where it is an immaterial part of the contract. In the latter situation, it may be fair to increase the price to be paid somewhat.<sup>113</sup> These rules would minimise the risk of the grantor deliberately circumventing the preferential right. They should also apply to other rights of first refusal, such as a preferential right to lease where the grantor argues that the third party lessee has undertaken a personal obligation in addition to the payment of rent.

What if no monetary value could be placed on the "personal obligation" and the grantor would not have concluded the contract without that obligation? An example is an undertaking by the third party, a close relative, to allow the grantor to stay on his property and to nurse the grantor in addition to payment of the purchase price, which the relative is only prepared to do against transfer of the object of the right of pre-emption.<sup>114</sup> The grantor may show that he would not possibly consider being nursed by anyone else in other surroundings. Another example is where the third party undertakes to transfer a unique object with great sentimental value for the grantor along with monetary compensation, which the third party is only prepared to do

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<sup>111</sup> This is also the position in Germany. § 466 (previously §507) of the German code provides that a *Vorkaufsrecht* may still be exercised where the third party undertook a subsidiary personal performance (*Nebenleistung*) which the holder cannot fulfill, as long as a monetary value can be placed on that performance, which the holder must then pay to the grantor. If a monetary value cannot be placed on the subsidiary performance, the *Vorkaufsrecht* cannot be exercised, unless the contract with the third party would also have been concluded without it.

<sup>112</sup> *Ibid.*

<sup>113</sup> This is contentious in Germany. *Erman* (Grünwald) § 507 RdNr 3 (now § 466) is in favour of adaptation if the contract would only have been concluded at a higher price without that obligation, *contra* Soergel (Huber) § 507 RdNr 2 (now § 466).

<sup>114</sup> The Supreme Court of Germany (*Reichsgericht*) regarded this as too personal an obligation to place a monetary value thereon (RGZ 121, 139).

against transfer of the object of the right. A sportsman who granted a preferential right to conclude a new employment contract on termination of his fixed term contract may argue that, although the holder offers the same monetary compensation as a rival club, the holder, as an inland club, cannot offer a house or training by the sea which the rival club can do and that no monetary compensation can be placed thereon.<sup>115</sup> In the case of a right of first refusal to conclude a new lease at the end of a lease contract, the grantor may argue that the holder is unable to use the premises for the same purpose undertaken by the third party and therefore cannot exercise his right. This could be used in an attempt to shake off the holder where the latter has operated a book shop in the premises, whereas the third party contract states that the lessee may only conduct a gift shop on the premises.

Conceivably, application of the rules mentioned so far would provide an answer for many such cases. For example, if the obligation to provide services or the transfer of the unique property which money could not compensate for is the only or most important reason why the grantor decided to alienate, one could argue that the most important, or preponderant part of the obligation comprises the supply of services or property, so that the intention of the parties is not to conclude a sale. This means that the contract rather amounts to an exchange despite the consideration comprising a considerable amount of money, as the sentimental value that the grantor attaches to the services or property is worth even more to her. The holder is not prejudiced as he can only reasonably expect to be preferred above third parties in respect of sales. Perhaps it can even be argued that he can only reasonably expect to be preferred above third parties who would provide the same consideration as him in respect of the type of contract foreseen by the preference contract. A counter-argument that the

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<sup>115</sup> Cf the unreported decision by Swart J of the Transvaal Provincial Division in *Golden Lions Rugby Union v Venter & Others* TPD 2000-02-11 case no 2007/2000, in which the court held that the holder club (Golden Lions Rugby Union) could not match the terms offered by the third party (Natal Rugby Union) in respect of the living, training and working environment of the player. *Inter alia*, the court held that an exercise programme which includes training on the beach and swimming in the sea could not be matched by the Golden Lions Rugby Union. This case is discussed by Prinsloo "Enkele opmerkings oor spelerskontrakte in professionele spansport" 2000 *TSAR* 229 242-243 and Loubser "Sport and competition law" in Basson & Loubser *Sport and the Law in South Africa* Service Issue 2 (August 2001) Ch 8-39 *et seq.*

grantor created a reasonable reliance that only a higher monetary consideration would let him prefer a third party above the holder, is also worthy of consideration. On the other hand, if that argument should disallow the grantor to rely on personal obligations in the third party contract, consistency requires that all exchange contracts should also be regarded as a breach of the preference contract. As there is something to be said for the contrary view, there is no good reason to depart from the existing rule that the grantor is free to conclude an exchange contract with a third party.

In the case of the sportsman, one should first ask whether the preference agreement is an unreasonable limitation on the sportsman's freedom to trade that is unenforceable on the ground of public policy. Loubser has suggested that such an agreement should normally be regarded as an unreasonable and unenforceable restraint of trade which unduly restricts an employee's freedom to work where he pleases.<sup>116</sup> If he is correct, that settles the question.<sup>117</sup> If not, one should probably not allow a non-material

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<sup>116</sup> Loubser "Sport and competition law" in Basson & Loubser *Sport and the Law in South Africa* Service Issue 2 (August 2001) Ch 8-39, Ch 8-40, Ch 8-45. Cf Prinsloo "Enkele opmerkings oor spelerskontrakte in professionele spansport" 2000 *TSAR* 229 242-243.

<sup>117</sup> Loubser argues that the right of first refusal in *Venter's* case is a restraint of trade "that arguably operates while the player is still under contract with a club or union" (Ch 8-40). This is a restraint of trade designed to limit the player's capacity to be employed by another after termination of the employment contract. Loubser is therefore correct in stating that the general principles applicable to the enforceability of restraints of trade should be considered. He argues that the employer's interest in retaining the services of the player or preventing the player from playing for a competing sports body, is not, in itself, a proprietary interest worthy of protection (Ch 8-45). "Contract clauses purporting to restrict the player from freely offering his services in the employment market after termination of an employment contract are therefore regarded as unreasonable, contrary to public interest and unenforceable." (Ch 8-39). He leaves the question open "whether the Supreme Court of Appeal and the Constitutional Court would enforce such a right of renewal or right of first refusal, if it is worded to relate specifically to the financial terms offered by a third party, given that the effect is to prevent a sport professional from freely offering his services in the employment market after termination of the initial term of the employment contract." (Ch 8-40). On the other hand, the grantor of a right of first refusal is or should be free to sound out the market and to negotiate with other prospective employers and need only contract with the holder if the holder can match any offer he can find in the open market. As such, the right of first refusal does not "prevent a sport professional from freely offering his services." As long as he does not contract with another club before the holder had a chance to match that other club's offer, he is free to negotiate with other clubs. It is true that other clubs' interest in

personal obligation undertaken by the third party, which the grantor could never have equalled, to destroy the holder's right. Otherwise the preference contract would be a dead letter. For example, to allow an argument that the holder, an inland rugby club, cannot exercise its right as it cannot offer a lifestyle close to the beach as the rival third party club can do, would mean that the preference contract is a dead letter. The sportsman created a reasonable reliance that the better financial content of the third party offer and other terms integral to his working conditions were all that would sway him not to contract with the holder. Certainly he created a reasonable reliance that the mere fact that another club is situated in a different area would not have an effect on his decision whether to contract with the holder or the third party. As each club is situated in a different area with unique advantages of living there, the preferential right would never otherwise bind the sportsman, as he could always point to some unique advantage of relocating to escape the preferential right which has nothing to do with the advantages integral to the employment contract itself, such as the monetary compensation, housing offered and undertakings on the prominence to be given to the player (for example, that he would play at least 3 out of every 4 matches or would be the first choice player in his position).<sup>118</sup> Countless opportunities to evade the right would therefore be opened if such aspects are considered.<sup>119</sup> Such a result could not have been intended, as the parties clearly foresaw a binding contract. Similar non-material extraneous benefits of contracting with another club should rather play a role when the reasonableness and enforceability of the right of first

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negotiating with the player may be dampened by the right of first refusal, which might not make it worthwhile to invest time and money in negotiations. This would prejudice the player's freedom to trade. However, in the case of a valued or talented player, this is unlikely to be an obstacle to a third party club's interest, as is clear from the *Venter* case. The employer's interest is not the only factor to be considered in evaluating a restraint of trade. The effect on the player's freedom is also crucial. In this regard, a right of first refusal is markedly less onerous than a normal restraint of trade which prohibits an employee from working for a competitor. On the other hand, the non-financial benefits of working for another club could sometimes be relevant to the question whether the holder club did match the conditions offered.

<sup>118</sup> For example, the undertaking by Natal Rugby Union that Venter would be the first choice no 8 player for Natal (p 13 of the judgment) is an integral and material part of the third party's offer relating to the working conditions themselves which should be matched by Golden Lions to exercise its right of first refusal.

<sup>119</sup> Cf *Erman* (Grunewald) § 504 RdNr 8 (now § 463).

refusal as a restraint of trade is considered, or if it passes that test, when the court exercises its discretion to award specific performance or damages.<sup>120</sup> The unreported judgment of Swart J of the Transvaal Provincial Division in *Golden Lions Rugby Union v Venter & Others* cannot therefore be supported insofar as it found that the holder of the right of first refusal, Golden Lions Rugby Union, could not exercise its right as it did not match the third party club's offer which included an exercise programme on the beach and as it could not supply coaching by the same coaches employed by the third party club.<sup>121</sup>

A similar argument could be raised against an author who argues that the atmosphere at a rival publisher's office is superior to that in the grantor firm and that therefore the holder cannot equal the rival's offer. If this matter was important to the author, it should have been stipulated as an exception to the holder's right on granting the preferential right. The grantor should therefore not easily be entitled to rely on such unique, intangible advantages of contracting with a third party to escape, when the contract with the third party remains of the type foreseen in the preference contract and when it is not regarded as contrary to public interest to enforce such a right. Such non-tangible advantages of contracting with a third party should rather be taken into account when the court considers the legality of the right of first refusal or exercises its discretion on the choice between specific performance and damages. It has already been suggested that the close working relationship which a publishing contract requires and the generally inferior bargaining position of the author within that relationship is an important factor which the court should take into account when exercising its discretion on whether specific performance or damages should be awarded. The same generally holds true for an employer-employee relationship.<sup>122</sup>

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<sup>120</sup> A breakdown in the relationships between the player and the holder club or its other employees should also be taken into account when the effect of the right of first refusal on the player is considered. *Cf Troskie v Van der Walt* 1994 3 SA 545 (O).

<sup>121</sup> *Cf Prinsloo* 243 who questions the correctness of the court's decision that exercise by the sea and the opportunity to work with the coaches employed by Natal are of material importance in contracts with rugby players.

<sup>122</sup> Depending on the degree of control by the employer and the closeness of the relationship called for by the employment contract as well as the circumstances surrounding the breach and the parties' relationship. *Cf* the many South African writers who state that employment contracts would not

In the case of a right of first refusal to lease, the majority in *Souteriou v Retco Poyntons (Pty) Ltd*<sup>123</sup> stated that, to use the *Oryx* mechanism, the holder must be able to “step in the third party’s shoes”, and suggested that this applies even in respect of the use to which the premises may be put.<sup>124</sup> This is apparently consistent with the reference in the *Oryx* case to Glück’s statement that the holder must be willing to perform *all* the terms undertaken by the third party,<sup>125</sup> although this was not relevant to the facts of *Oryx*. The approach of the minority in *Souteriou* on this point is preferable – the holder must declare unequivocally and unqualifiedly that he intended to step into the shoes of the third party on the terms and conditions of that lease, “*in so far as they were not inconsistent with his continued use of the premises as before.*”<sup>126</sup> One should accept that the grantor would not have granted the right of first refusal to lease if he intended to prefer a third party solely on the basis of the use to which the third party intends to put the premises. By granting the right of first refusal, the grantor indicated that he is satisfied with the use of the premises for the current purpose, and that, if he decides to lease again, he would allow the holder to enter into a lease for that same purpose, as long as the holder is prepared to match any other terms offered by a third party. Otherwise the grantor would always be able to evade the right of first refusal, as chances are that interested third parties intend running different business from the premises than the holder. By necessary implication, the parties tacitly agreed that the grantor may not evade the holder’s right

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generally be specifically enforced against an employee, such as *Christie Contract* 613; *Kerr Contract* 602; Rycroft & Jordaan *A Guide to South African Labour Law* 2<sup>nd</sup> edition (1992) 102; Brassey “Specific Performance: Labour’s Lost Love” (1981) 2 *ILJ* 57 69.

<sup>123</sup> 1985 2 SA 922 (A) 935C.

<sup>124</sup> 935B. This statement was not applied by the court, as the terms of the third party contract was unknown, so that the court merely ordered that the lessee may not be ejected as he had undertaken to fulfil the terms of the third party contract (935B-E).

<sup>125</sup> 906H. See also *Floyd* 1986 THRHR 253 266. This aspect of *Oryx* is also what swayed the court in *Golden Lions Rugby Union v Venter supra* to insist upon exact matching of the third party’s offer, even as far as the living conditions of the employee is concerned.

<sup>126</sup> 937H.

on the basis that he cannot use the premises for the same purpose as that undertaken by a third party.<sup>127</sup>

What about cases not covered by these rules? An example would be a sale of the grantor's house, worth around R600 000 to R700 000, to her cousin for R600 000 plus delivery of an antique table and chairs once belonging to their grandmother to which the grantor attaches tremendous sentimental value. The third party states that she would not have sold the table and chairs unless she could buy the house. The grantor, on the other hand, acknowledges that obtaining the table and chairs was an important factor, but not the dominant motivation for her decision to sell. However, she would not have sold for merely R600 000 without the table and chairs. She argues that the contract does not trigger the holder's right, as the holder is unable to fulfil the cousin's obligations. Even on the assumption that the right is triggered, she maintains that she is not prepared to put a price on her house for the benefit of the holder, as she should in that case be prepared to withdraw from the contract with her cousin and first sound out the market.

Does this constitute a breach of the preference contract? If so, should this entitle the holder to buy, or only to restoration of the *status quo ante*, so that the grantor could indeed sound out the market for a better price? If the holder is entitled to buy, what value is to be placed on the non-monetary component?<sup>128</sup>

It is submitted that an acknowledgement that the grantor would have wanted to sell even without the personal obligation, shows that the grantor should have realised that

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<sup>127</sup> The minority's view is consistent with a decision by a California Court, *Arden Group Inc v Burk* 53 Cal Rptr 2d 492 (Cal App 2 Dist 1996). The court distinguished the acceptance of a contract offer and the exercise of a right of first refusal. An acceptance must meet exactly the terms of an offer contract. But no such matching is required for the exercise of a first refusal right. Because the party exercising the first refusal right is "stepping into a contract made by a third party," the court must consider commercial realities and allow modifications consistent with the intent of the parties whose contract created the right of first refusal. For a discussion of the case, see "Leases: Right of first refusal properly exercised" January 1998 *Real Estate Law Report* 5.

<sup>128</sup> American case law is not unanimous on these issues. See especially Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-79 *et seq.*

she was concluding a sale, a type of transaction in respect of which the holder had a preference. She should therefore have realised that she was expected to invite the holder to match any third party offer, and to indicate what compensation she would have accepted in lieu of the personal obligation. As this personal obligation was not fundamentally important to her, she should have been able to place a money value on the property as a whole. Contracting with a third party without doing so should therefore be regarded as breach.

Logically, the normal remedies for breach should apply with the court being able to decide the price that the grantor would have accepted for the non-monetary obligation. The grantor's *ipse dixit* should be accorded due weight herein, and if there is no reason to disbelieve her due to an approximation between her stated price and the market value, that should be the price which the holder should be allowed to match.

Alternatively, the grantor could be allowed to withdraw from the third party contract once it is established that it constitutes breach so that the *status quo ante* is restored. The grantor then has a chance to sound out the market again and decide on a monetary value that she is willing to accept for the property. However, as the grantor should have known that she should have given the holder a chance to submit an offer, she should probably be held to have had her chance of sounding out the market. Therefore the holder should not be deprived of a remedy allowing him to enforce performance. Allowing the grantor to gather evidence on the true monetary value of the property in the course of the dispute or litigation with the holder protects the grantor's interest to obtain the best possible price to some extent.

A related issue is whether a contract to sell only a part of the object or to sell it together with other properties amounts to breach. Clearly, where the grantor sells only part of the object, the holder should be allowed the opportunity to buy that portion and failure to give the holder a chance to match a third party offer is breach.<sup>129</sup>

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<sup>129</sup> This is also the position in the United States of America according to Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-75.

It is unfair to force the grantor to sell the whole object to the holder.<sup>130</sup> The rest of the object should remain subject to the holder's right.

The position is more complex when the object is sold as part of a package deal.

In this instance the grantor could argue that the third party is the only person prepared to buy all the properties involved and that the third party is not interested in the other properties without inclusion of the object of the right. Therefore the grantor has a legitimate interest in selling the object as part of the deal to enable her to sell her other properties at a fair price.

As was stated above, controversy rages over this issue in the US.<sup>131</sup>

On the one hand, many US courts hold that the grantor cannot be compelled to sell one of the lots of land if she desires to sell the land as a whole. Therefore the holder is not entitled to an order for specific performance to the effect that the object of the right of first refusal be conveyed to the holder.<sup>132</sup>

Some courts do not regard a "package deal" with a third party as a breach at all.<sup>133</sup> They argue that the grantor is only prohibited from selling that piece of land alone.<sup>134</sup>

Others see the package deal as a violation of the right of first refusal as opposed to a triggering event and therefore hold that the holder is only entitled to an injunction, reconveyance to the grantor where the third party knew of the right, or damages.<sup>135</sup> These decisions place the interest of the grantor to remain as free as possible above

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<sup>130</sup> Cf Tewel 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-76.

<sup>131</sup> Par 4 3 *supra*.

<sup>132</sup> For details see par 4 3 *supra*.

<sup>133</sup> For example, *Sautkulis v Conklin* (1956 2d Dept) 1 App Div 2d 962.

<sup>134</sup> For all details, see Daskal 1995 *Fordham Urban Law Journal* 461; Flannigan March-June 1997 *Canadian Bar Review* 1, Stutzman & Day 1983 *Idaho Law Review* 277; Tewel 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-69 *et seq* and decisions there cited.

<sup>135</sup> *Ibid*.

the interest of the holder to obtain the property, but still recognise the need to protect the holder's interest.

One policy argument in favour of this approach is that there is no way to establish the price at which the holder would be entitled to purchase the property.

The opponents of this approach equate the holder's purpose to obtain the property as the purpose of the contract as a whole. They argue also that remedies aimed at preventing the owner from making a sale to someone else are "worthless and illusory" as they give no "immediate, positive benefit" to the holder, so that the holder is unlikely to enter into litigation to obtain this "pyrrhic result."<sup>136</sup> The possibility of a deliberate circumvention of the holder's right is a major consideration for these writers. Less persuasive is the argument that transactions like a package deal, dissolution of the grantor company, or a sale for considerations which is partly in cash should entitle the holder to buy at market value because "this price standard is implicit in the nature of a right of first refusal."<sup>137</sup>

The *BGB* also provides for package deals. It provides that the holder of a *Vorkaufsrecht* may exercise his right on payment of a proportionate part of the total price.<sup>138</sup> The grantor may require that the pre-emption apply to all the property that cannot be divided without prejudice to him.<sup>139</sup> The grantor may not require this if the holder is prepared to compensate for the prejudice by payment of a sum of money.<sup>140</sup>

In my opinion, the package deal should be regarded as breach of the holder's right. The grantor must have known that the transaction conflicts with his prior undertaking to allow the holder to buy the property should he ever sell. Owners should not lightly conclude preference contracts and then be allowed to escape these contracts. However, the grantor should not be limited to the market value only. The court

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<sup>136</sup> Flannigan March-June 1997 *Canadian Bar Review* 1 34.

<sup>137</sup> Flannigan 31-32.

<sup>138</sup> § 508 *BGB*.

<sup>139</sup> *Ibid.*

<sup>140</sup> *Erman* (Grunewald) § 508 RdNr 3.

should establish the price that the grantor would have accepted for the object separate from the package. The grantor's *ipse dixit*, the structure of the package deal and the market value are all factors that the court should consider in this endeavour. The equitable discretion to award or refuse specific performance will enable courts to arrive at an equitable solution for each case. The holder should, however, not be entitled to insist on the benefit of the entire package deal.

The German writer Schurig has proposed a general principle to deal with all the aforesaid problematic cases where it is disputable whether a trigger event has occurred. He argues that the category of contracts or dispositions that trigger the *Vorkaufsrecht* should be determined by the grantor's interest or purpose in concluding that contract.<sup>141</sup> If the grantor can also achieve his immediate purpose with a specific disposition through contracting with the holder, that type of disposition should trigger the holder's right of pre-emption, even if it does not amount to a "sale". If, however, the grantor's immediate purpose can only be fulfilled through contracting with a third party, the holder's right should not be triggered by the third party contract.

The upshot is that even an exchange could trigger the holder's right as long as the holder can supply the same object agreed to by the third party, or if the grantor is actually only interested in the monetary value of the object to be delivered by the third party.<sup>142</sup> Similarly, transfer of the object in lieu of payment of a debt (a *datio in solutum*) should also trigger the holder's right, even though this is not strictly speaking a sale.<sup>143</sup> Where the third party contract cannot be classified as a sale, Schurig would have the holder bear the onus to establish that the grantor's purpose could be satisfied by a contract with the holder.<sup>144</sup>

On the other hand, a sale to a family member for sentimental reasons, or a transfer to a daughter company due to a company restructuring would not breach the holder's right, as the grantor would not be able to achieve his immediate purpose by

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<sup>141</sup> *Supra* 130 *et seq.*

<sup>142</sup> 134-135.

<sup>143</sup> 136.

<sup>144</sup> 136.

contracting with the holder.<sup>145</sup> As the third party contract can be classified as a sale, Schurig would have the grantor prove that the supposed sale is actually a mixed donation which should not trigger the holder's right.<sup>146</sup> This analysis also allows for a differentiated approach to cases where the grantor causes the object to become part of a partnership's assets upon entering into a partnership. If his purpose is merely to add value to the assets of the partnership whereas the precise nature of the asset to be added is not important, the grantor's purpose is accomplished if the holder pays for the object insofar as the value payable to the partnership is precisely determinable.<sup>147</sup>

Schurig's differentiated approach has been criticised. In a doctoral thesis on this issue, Hees has argued that Schurig's approach flouts the clear provision of the *BGB*, which states that only a sale could trigger the holder's right.<sup>148</sup> In cases where the juristic act in question could (also) be regarded as another type of contract than sale, he argues that this contract should not trigger the holder's right unless the elements of sale could also be identified in that transaction. Therefore, transfer in fulfilment of a money debt would trigger the right, but not a mixed donation or exchange, not even where the holder is able to perform in terms of the exchange contract. However, if the holder can show that the grantor actually intends to conclude a sale whereas he merely seeks to evade the *Vorkaufsrecht* by agreeing upon non-monetary consideration, the holder should be able to exercise his right on the basis of a separate provision of the *BGB*,<sup>149</sup> which essentially provides for fictional fulfilment of conditions in the same instances as this would be allowed under South African law. This approach probably makes it more difficult for the holder to exercise his right than Schurig's approach, as Hees would require the holder to prove an unconscionable effort to evade the right of pre-emption.

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<sup>145</sup> 137.

<sup>146</sup> *Ibid.*

<sup>147</sup> 136.

<sup>148</sup> Hees S *Die vertragstypologische Bestimmung des Vorkaufsfalls und die Wirkungen einzelner Vereinbarungen und Störungen des Drittvertrages für das Vorkaufsverhältnis* (1991). For a summary of his views, see 210 *et seq.*

<sup>149</sup> § 162 *BGB*.

The early South African case of *Fane v Armstrong*<sup>150</sup> supports Schurig's differentiated approach as far as filtering out certain sales are concerned. A sale to the grantor's uncle providing for a right of repurchase in certain contingencies was held not to breach the holder's right of pre-emption. It appeared that the uncle had informed the grantor that the transfer was virtually a trust deed, entered into merely for the benefit of the grantor, who was a prodigal and spendthrift. For this reason, the court held that, though nominally referring to a sale, the documents must be taken to constitute a trust and therefore placed the holder in no worse position than he might have been. In Schurig's terminology, the grantor's purpose in "selling" to his uncle, could not be achieved through a sale to the holder.

*Bellairs v Hodnett*,<sup>151</sup> also lends some support to this approach. The court was not persuaded that a sale at cost value to a company that the grantor considered to be his *alter ego*, breached the right of pre-emption. The court assumed without deciding that this was the case, but still dismissed the holder's claim for damages,<sup>152</sup> as the holder was definitely not entitled to buy at cost price, but rather at the true value of the shares.<sup>153</sup> The court emphasised that rights of pre-emption normally envisage only arm's length transactions in which the grantor is desirous of selling the object at its true value, or at least at a rate bearing some relation to the true value.<sup>154</sup>

On the other hand, the court in *Dithaba Platinum v Erconovaal*<sup>155</sup> refused to allow evidence that the parties' purpose in granting mutual rights of pre-emption was simply to prevent the rights from falling into the hands of a specific competitor, which was not the effect of the transaction complained of.<sup>156</sup> It is submitted that courts should not refuse such evidence on the true purpose of the parties. In such a case, neither party's interest justifies a finding of breach.

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<sup>150</sup> 1899 (XVI) *CLJ* 120.

<sup>151</sup> *Supra*.

<sup>152</sup> 1137H.

<sup>153</sup> 1140A-G.

<sup>154</sup> 1140G-H. The court suggested that, on the assumption that the contract breached the holder's right, remedies aimed at restoring the *status quo ante* would be more appropriate (1140H-1141A).

<sup>155</sup> *Supra*.

<sup>156</sup> 621C *et seq.*

To summarise, at least two broad approaches are possible to determine whether a specific third party contract breaches or triggers the holder's right. The traditional approach is to consider only whether the contract in question displays the characteristics of the main contract foreseen by the preference contract, for example, a sales contract in the case of a right of pre-emption. Only such contracts and all such contracts would therefore breach the holder's right. The parties' actual purpose should, as always, play a role in the classification of the contract. Therefore a sale disguised as an exchange or donation would also breach the holder's right.

The second approach is a more differentiated one. The holder need not necessarily prove that the third party contract constitutes a sale, but only that the grantor could have achieved her immediate purpose by contracting with the holder. This would firstly allow contracts and juristic acts that do not really amount to sales to trigger the holder's right. It also allows the grantor to escape the right of pre-emption where she can prove that the sale to the third party serves some special interest which performance by the holder could not accomplish. The second approach, especially its first-mentioned consequence, could be criticised for ignoring the reference to "sale" in pre-emption contracts. On the other hand, it allows for a more differentiated and therefore just approach, without undue impairment of legal certainty, as it involves one coherent principle to be applied in all cases. Although widening the ambit of the right of pre-emption on this basis may unfairly surprise the grantor, and should therefore not be accepted in our law, the narrowing of the net which this approach achieves in some cases is clearly in accordance with the true purpose of the parties, and achieves a fair balance of their interests.

The first approach has overtones of the conceptual approach criticised by proponents of the *Typenlehre*, whereas the second is indeed a typological, purposive approach.<sup>157</sup>

## 7 2 2 2 2      Exercise of the holder's right upon breach

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<sup>157</sup> Cf the title of Hees's thesis on this topic (n 148 *supra*) that refers to the "typological" determination of the trigger event.

Upon breach, the holder must elect whether to cancel the preference contract and claim damages only or whether to enforce performance. The normal rules on election between remedies for breach apply. This election can be equated with “exercise” of the right of first refusal, a term often used in this context.<sup>158</sup> It is fair to require that the holder must, on request by the grantor, prove that she is willing and able to perform the terms agreed with the third party and comply with any applicable formalities in her declaration of willingness to perform.<sup>159</sup> The juridical explanation for preference contracts should reflect the need to have the holder bound to the decision to exercise her right. This requirement protects the grantor against losing the benefit of the third party contract in favour of a holder who is not bound or able to perform.<sup>160</sup> Good faith requires that the onus be on the grantor who disputes compliance with these prerequisites to point this out to the holder, and to give the holder a chance to prove the contrary or to comply with any formalities. It would be bad faith for the grantor to simply ignore the holder’s indication of willingness to contract, and to argue later that the holder has lost the right to enforce performance due to non-satisfaction of these requirements.

Where the terms agreed with the third party are unknown, the holder should be entitled to an order that the grantor disclose the terms of the third party contract, to enable the holder to decide whether to exercise her right.<sup>161</sup> It would be dangerous for a holder ignorant of the terms of that contract to exercise the right. Whether this would mean that the holder is entitled to an order that the grantor “make an offer to the holder” will be considered more fully hereunder when the juridical explanation of preference contracts will be considered. Even if exercise of the right is explained rather as acceptance of an offer already embedded in the preference contract or as

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<sup>158</sup> See, for example, Floyd 1986 THRHR 253 255; Reinecke & Otto 1986 *TSAR* 18 29.

<sup>159</sup> *Cf Hartsrivier Boerderye v Van Niekerk supra* 706H. The juridical nature of the holder’s declaration of will be considered later when a juridical explanation of the normal preference contract is proposed. Whether it is regarded, for example, as an acceptance of an offer embedded in the preference contract, or as a contractual power to create a contract, policy considerations require that it should bind the holder.

<sup>160</sup> *Cf Hartsrivier Boerderye v Van Niekerk supra* 706H.

<sup>161</sup> *Cf* Tew 1989 *Eastern Mineral Law Institute Procedures* 7-1 7-64.

exercise of a contractual power to create a contract by unilateral declaration upon breach, the holder should be entitled to an order that the grantor supply information on the third party contract which has been concluded in breach of her right.<sup>162</sup> The holder needs this information to decide what remedy to elect.

#### 7 2 2 2 3 Termination of the holder's right

The general rule should be that before the grantor is free to contract with a third party on certain terms, these terms must be disclosed to the holder and the holder must be invited to make an offer at those terms within a reasonable time. The preference contract only terminates upon the grantor subsequently contracting with and performing to a third party on terms that the holder has failed to match within a reasonable time thereafter.<sup>163</sup> Otherwise, the preferential right continues to exist and the grantor would once more have to invite the holder to match terms on which the grantor is prepared to contract at a later stage, even if these terms are exactly the same as the ones originally offered to the holder.

Where the holder of a right of pre-emption submits an offer of R5000 in response to the grantor's invitation without knowing of a competing third party offer of R6000, the grantor would therefore not be free to contract with the third party at R6000 unless the holder has been given a chance to match that offer. Furthermore, when the grantor has disclosed the offer of R6000, a failure to match that offer does not *ipso facto* release the grantor. Only if the grantor indeed contracts with and performs to a third party on those terms within a reasonable time, does the preferential right terminate. Therefore, if the holder has failed to offer R6000, the grantor may not after a year contract with a third party at R6000 or more without again inviting the holder to match the offer. This rule discounts the effects of inflation and prevents the grantor from ridding himself of the holder through a fake offer by the third party.

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<sup>162</sup> Therefore I disagree with Floyd 1986 THRHR 253 268 who argues that situations where the terms of the third party contract is unknown to the holder shows the need for a "normal order" for specific performance to force the making of an offer. A mere order that the grantor disclose such terms may suffice, depending on the juridical explanation of the holder's remedy.

<sup>163</sup> It is conceded that the "reasonable time" requirement may lead to uncertainties.

Where the interested third party's identity was enquired about or disclosed to the holder, the grantor would moreover only be released by contracting with a third party whose identity and offer has been disclosed. This protects the holder's interest in warding off unwanted third parties, which is often an important consideration in the conclusion of preference contracts. If the holder did not request this information, the grantor may assume that the identity of the third party is not important to the holder. However, where the holder requested this or where the grantor voluntarily disclosed the third party's identity, the grantor may not lawfully contract with anybody else upon the holder's failure to make or accept an offer, unless the holder has been informed of the new third party's identity.<sup>164</sup>

Any other conduct that evidences a waiver of the right should, of course, also terminate the right. For example, where the grantor simply invited the holder to make an offer without any additional information, the holder's outright failure or refusal to respond would normally amount to a waiver of the right. This conduct normally indicates that the holder is not at all interested in contracting with the grantor, and that the grantor is free to contract with any third party on any terms.

These rules do not imply an enforceable duty to inform the holder of each and every offer received. Neither can a holder force a grantor who has simply invited an offer by the holder to disclose the terms of third party offers received. The holder may request that information upon the invitation to make an offer and may remind the grantor that without such disclosure the grantor may not lawfully contract with a third party. The holder may not, however, force the grantor to make such disclosure.<sup>165</sup> The rule argued for is that failure to disclose such a third party offer prevents the grantor from lawfully contracting on those terms with a third party. It does not

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<sup>164</sup> Austrian law requires the grantor to inform the holder of the third party's identity before the time limit within which the *Vorkaufsrecht* must be exercised begins to run. See 1957 *Evidenzblatt* 547 (Nr 349) 548. However, where the holder comes to know of the third party's identity during the course of negotiations with the grantor, the failure to include these particulars in the grantor's notice is irrelevant (SZ 22/34 (16.3.1949)).

<sup>165</sup> In any event, such a remedy would be rather toothless against a recalcitrant grantor.

express the grantor's duty, but merely amounts to a qualification of the method by which the grantor may be released from the preference contract.

An inflexible rule that only rejection of the grantor's *offer* would release the grantor is also unnecessary. A rejected invitation to match a sufficiently disclosed third party offer shows that the holder has waived the right to contract with the grantor on those terms. In other words, even if an offer is formally required, this will not make much difference in practice as a failure to respond to the grantor's invitation may nevertheless amount to a waiver of the holder's right. This means that the grantor would be released without an offer being made. The rule argued for also protects the grantor's ability to sound out the market to gain the highest possible price. If only a rejected offer could release the grantor, this would constitute a risk for the grantor, as in the meantime a better third party offer may materialise before the grantor is able to withdraw the offer to the holder.<sup>166</sup>

If the holder does make an offer, the grantor is not obliged to accept it. However, a valid offer matching any disclosed third party offer ensures the continuation of the preferential right.

All of these rules fairly balance the grantor's interest in obtaining as high a price as possible, with the need to protect the holder against losing the opportunity to contract to a third party.<sup>167</sup>

### *7 2 2 3 Juridical explanation or construction of the default type*

The rules proposed above could of course simply be lumped together as the default rules of true preference contracts. However, I will now consider whether there is not perhaps a coherent juridical explanation of these rules consistent with the conceptual

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<sup>166</sup> Under Roman-Dutch law, only a notice to the holder, and not an offer, was required to force the holder to make a decision. See Voet 18 1 2; Sande *DF* 3 4 4. See also Floyd 1986 THRHR 253 256, 257 *in fine et seq.*

<sup>167</sup> The policy considerations at stake have been extensively canvassed in chapter 5. See especially paras 5 2 1 1 and 5 1 2 1 2 *supra*.

structure of South African contract law, which might facilitate their understanding and application.

I will critically consider four possible explanations of the default type just proposed. They are all consistent with the point of departure that the holder should ultimately be able to enforce performance of the main contract, but only when the first refusal contract is breached by a contract with or offer to a third party. I will consider whether they also sufficiently explain the other default rules proposed here. I will also consider the different practical implications of each of these explanations.

The first, rather contrived, explanation is that a preference contract amounts to an *obligatio non contrahendo cum tertii* coupled with an option, conditional upon breach of the right of first refusal. In the absence of breach, the preference contract terminates when the grantor contracts with and performs to a third party within a reasonable time after the holder's failure to match that third party offer, provided there was sufficient disclosure to the holder (par 7 2 2 3 1 below).

The second, perhaps also contrived, but simpler explanation is that the grantor has an enforceable duty to make an offer the moment before the grantor contracts with a third party. Once again, in the absence of breach, the holder's right terminates when the grantor contracts with a third party within a reasonable time after the holder's failure to match that third party offer (par 7 2 2 3 2 below).

The third explanation is a variation on the second and will be discussed under the same rubric. It is that the duty to make an offer the moment before the grantor contracts with a third party is not (only) enforceable by a court order that an offer be made, but that the holder has a contractual power to create the main contract by unilateral, extra-judicial declaration upon breach of this duty. This can be understood as "self-help" specific performance.

The fourth explanation is that the grantor's obligation is simply an *obligatio non contrahendo cum tertii* which terminates when the grantor contracts with a third party within a reasonable time after the holder's failure to offer the same terms. Upon breach of this negative obligation, the holder has a contractual power to create a

contract with the grantor by unilateral declaration on the same terms as agreed with or offered to the third party (par 7 2 2 3 3 below).

#### 7 2 2 3 1 Option conditional upon breach

The default true preference contract can be described as an option conditional upon breach. The condition triggering the option must be equated with breach in order to accommodate two features of the default type. The first is that only breach in the form of a contract with or offer to a third party should trigger the holder's right to enforce performance. The second is the *obligatio non contrahendo cum tertii*, which prevents a contract with a third party being labelled as a neutral trigger event. The conditional option construction was fully discussed in par 5 1 2 1 1 above.

This juristic construction precludes the need for an order that the grantor make an offer. Regarding the preference contract as an option contract explains the extra-judicial creation of the main contract, by the holder's unilateral declaration. This results in an efficient and cost-effective remedy for the holder, in line with the leading case of *Associated South African Bakeries (Pty) Ltd v Oryx & Vereinigte Bäckereien (Pty) Ltd*.<sup>168</sup>

The conditional option construction has the further advantage that exercise of the holder's right is regarded as an acceptance, so that the holder is bound to perform his side of the main contract. This protects the grantor against the risk of losing the interest of the third party due to the holder's exercise of the right, without the holder herself being bound to perform.<sup>169</sup>

Moreover, an *obligatio non contrahendo cum tertii* is in any event an implicit component of options.

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<sup>168</sup> *Supra*. Cf Van der Merwe *et al Contract* 68.

<sup>169</sup> This would be the case if a non-binding indication that the holder wishes to contract is regarded as sufficient exercise of the right. This would leave the holder free to change his mind, after the third party had probably also lost interest due to exercise of the right of first refusal.

If the conditional option explanation is followed, the formalities prescribed in the Alienation of Land Act 68 of 1981 would apply to a pre-emption contract in respect of land. As this explanation regards the grant of a right of pre-emption as an offer to alienate, such grant must be in writing and signed by the grantor. As exercise by the holder amounts to an acceptance of the offer, the formalities requirements apply equally to the holder's declaration.

A problematic aspect of this juridical explanation is that it is rather contrived and strained, and arguably amounts to a fiction. Parties are unlikely to agree on an option that only becomes operative on breach.<sup>170</sup> On the other hand, this objection could be countered by the reminder that many parties do in fact provide for remedies for breach, and it is very conceivable that parties could agree that the holder would have a power to unilaterally create the main contract should the grantor breach his obligation, similar to an option. In any event, the default rules of a contract are not determined merely by the likely *consensus* of parties to such contracts, but also by policy considerations. Moreover, there is support for this explanation in South Africa and other jurisdictions. It has been championed by South African writers such as Reinecke & Otto.<sup>171</sup> It is also effectively the explanation accepted in the USA, where

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<sup>170</sup> It is not as strained to regard a preference contract which creates no *obligatio non contrahendo cum tertii*, such as the *BGB Vorkaufsrecht*, as a conditional option. What makes the option construction unusual in the present context is that one must accept that the parties prohibit fulfilment of the condition as it would in fact breach their contract. This is not the case under the *BGB Vorkaufsrecht*, where contracting with a third party is allowed and in fact required to force a decision on the exercise of the right by the holder. On the other hand, an option usually implies that the grantor may not contract with anybody else. Therefore the *Vorkaufsrecht* is also an unusual type of option.

<sup>171</sup> "Voorkope en ander voorkeurkontrakte" 1986 *TSAR* 18 especially at 24 *in fine et seq.* See also Flack "The pre-emption agreement: is it a viable option?" 2001 *SALJ* 831 who first appear to argue that pre-emption agreements amount to options (see, for example, at 832) but later argues that courts should compel the grantor to make an offer (843). Lubbe 1985 *Annual Survey* 137-138 has also stated that "Grants specifying the pre-emptive price or, expressly or tacitly, incorporating the price at which the grantor is prepared to sell to a third party, will have to be recognized as more akin to option contracts than previously thought." See also Van der Merwe *et al Contract* 67. The view that all preference contracts may be regarded as conditional options was implicitly rejected by the Supreme Court of Appeal in *Hirschowitz v Moolman supra* 765F-G and *Soteriou v Retco Poyntons supra* 932E.

the right of pre-emption is said to ripen into an option upon breach.<sup>172</sup> There is also support for it in English law.<sup>173</sup> The combined *Vorhand* and *Vorkaufsrecht* clauses suggested by some German model contract handbooks amount to the same construction.<sup>174</sup> The *Vorhand* clause confirms the *obligatio non contrahendo cum tertii*, so that contracting with a third party without granting the holder an opportunity to contract would be breach. The *Vorkaufsrecht* clause provides for the situation where the grantor does breach the contract in that manner, and is indeed regarded as a conditional option by some German commentators.<sup>175</sup>

Another likely criticism of this explanation is that the terms on which the holder may exercise the option are not mentioned in the option contract.<sup>176</sup> However, where nothing is said as to the terms of the main contract, the holder is clearly entitled to contract on the terms agreed with the third party. As the only condition which triggers the option is a contract concluded with or a valid offer to a third party, the terms at which the holder may contract are always certain when the option may be exercised. There is no speculation involved as to the terms to which the grantor *would* be prepared to contract with third parties, as is the case where the trigger event is a lesser manifestation to sell. There is therefore no basis to reject this construction for lack of certainty.

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However, the courts did not specifically consider the conditional option construction when they made these comments. Cf Floyd 1986 THRHR 253 261, who strongly opposes the view that preference contracts amount to options, but largely on the basis of those preference contracts which allows (and forces) the grantor to make an offer upon a lesser manifestation of a desire to sell at a price which is not predetermined in any way.

<sup>172</sup> See par 4 3 *supra*.

<sup>173</sup> Cf *Barnsley's Land Options supra* 178: "At the point where the power to compel a disposal arises, the right of pre-emption mutates into an option". English cases such as *Pritchard v Briggs* [1980] Ch 339 (CA) that also speaks of the right of pre-emption changing into an option on breach, rather fall under the category of conditional options to buy at a specified or predetermined price and do not support the present explanation where no price is specified.

<sup>174</sup> See par 4 1 2 *supra*.

<sup>175</sup> See par 4 1 1 2 *supra*.

<sup>176</sup> Janisch 1990 *Responsa Meridiana* 434 442-443. That is, in the type of preference contract under consideration.

An objection that the condition to which the alleged option is subject is a potestative one and therefore inconsistent with a serious intention to be bound to contract is also unfounded. As was argued above, the condition in question is not an objectionable potestative condition that causes liability to be dependant on the mere *ipse dixit* of a party.<sup>177</sup> In the present case, liability is dependant on an action by the grantor, namely the conclusion of a third party contract or the submission of a valid offer to a third party. A court could enforce the contract against a grantor who insists that she does not want to be bound by simply pointing to the conclusion of a third party contract or offer.

That this construction allows the extra-judicial creation of a contract by the holder also does not mean that the court loses its discretion to refuse specific performance.<sup>178</sup> When the holder seeks specific performance of the main contract created extra-judicially, the court has the power to refuse specific performance. It makes no practical difference whether specific performance is refused only at that stage, or earlier. In both cases, damages would be granted on the basis of what the holder's position would have been had he obtained performance of the main contract.

A problematic aspect of this juridical explanation is that it is difficult to reconcile with the view that the grantor may cure the breach, in other words withdraw from the third party contract, as long as the holder has not exercised her right yet.<sup>179</sup> Reinecke & Otto simply state that the offer may not be revoked after fulfilment of the condition, unless the grantor decides not to contract at all anymore.<sup>180</sup> Other commentators have formulated the suspensive condition qualifying the grantor's offer as a sustained

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<sup>177</sup> See further par 7 1 *supra*, but especially paras 5 1 2 1 and 4 1 1 2 where this aspect was discussed in more detail.

<sup>178</sup> Eiselen 1986 *THRHR* 95 99 has criticised the *Oryx* mechanism for depriving the court of its equitable power to refuse specific performance of the preference contract. *Cf* Floyd 1986 *THRHR* 253 267, 265 and Van der Merwe *et al Contract* 68 who appear to propose that exercise of the right take place by unilateral declaration under supervision of a court.

<sup>179</sup> On which see further par 7 2 2 1 1 *supra*. For criticism against the conditional option construction on this point see Janisch 1990 *Responsa Meridiana* 434 444.

<sup>180</sup> 1986 *TSAR* 18 25.

desire to contract.<sup>181</sup> A more precise, but rather complicated, explanation is that once the suspensive condition has been fulfilled, the option becomes subject to a resolutive condition, namely that the grantor withdraws from the third party contract and no longer wishes to contract at all. The conditional option explanation is also inconsistent with a rule that the grantor may cure the breach after the holder has exercised her right. This is because exercise of the right brings the main contract into existence.<sup>182</sup>

Options are also generally regarded as cedable, whereas this may be regarded as undesirable and unfair in the case of rights of pre-emption.<sup>183</sup> However, both options and rights of pre-emption should not be cedable in any situation where the holder's identity is of material importance.<sup>184</sup> This sufficiently provides for the discomfort commentators have expressed with the general principle of cedability.<sup>185</sup>

The conditional option construction is somewhat problematic when the third party contract creates personal obligations or where it involves a package deal. If the third party contract does in fact breach the preference contract,<sup>186</sup> it has been suggested that the holder should be entitled to buy at the monetary value of the personal obligation. In the case of a package deal, it was suggested that the holder may buy at the price that the grantor would have accepted for the object on its own, taking into account the structure of the entire deal. These cases could, of course, be forced rather uncomfortably into the conditional option mould if courts consider it the best explanation for true preference contracts. The holder should then proceed to exercise his right unilaterally at the monetary value that he considers appropriate. If the

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<sup>181</sup> See, for example, Flack 2001 *SALJ* 831 835.

<sup>182</sup> It would not help to regard the preference contract as simply a conditional offer, as that would not explain why the grantor cannot unilaterally withdraw from the preference contract at any stage.

<sup>183</sup> Cf Flack 2001 *SALJ* 831 837; *Hersch v Nel* 1947 3 SA 365 (O) 373; Mitchell 2001 *University of Chicago Law Review* 985.

<sup>184</sup> Lubbe & Murray *Contract* 76; Flack 2001 *SALJ* 831 837. Mitchell 2001 *University of Chicago Law Review* 985 argues for a residual rule that rights of first refusal are personal and therefore not assignable.

<sup>185</sup> Cf Kerr *Sale and Lease* 50.

<sup>186</sup> As to how this is established see par 7 2 2 2 1 *supra*.

grantor disputes the value placed on the personal obligation, he could simply refuse to perform, forcing the holder to approach the court to obtain an order for specific performance. In the course of those court proceedings, the grantor should raise the issue of the price at which the holder was entitled to contract.

However, in these cases it is probably advantageous to force involvement of a court to ascertain the price at which the holder may contract before the main contract may be created, in any event where the grantor disputes the sum value placed on the performance by the holder. A conditional option, by contrast, allows the holder to create the main contract even where the grantor disputes the terms on which she may do so.

Moreover, the conditional option construction is perhaps not overly helpful as one simple, coherent explanation of all the default rules, as it does not explain the special rules on termination of the default preference contract that I have argued for. One could, however, argue that compliance with those rules indicates the only circumstances under which the holder could be regarded to have waived the option, so that they fit the conditional option explanation. It could be argued that the holder would not be prepared to waive her right if she realised that the grantor invited her to match a third party offer without a serious intention to contract with and perform to the third party. Neither could a failure to match a third party offer be seen as a waiver in the absence of sufficient information on the identity of and terms offered by the third party. An invitation to make an offer or to match the terms of a third party offer is therefore what is expected from a grantor who wishes to contract, although the holder cannot force him to do so at any stage before breach.

However, this remains a rather strained juridical explanation and courts may therefore be unwilling to apply it to true preference contracts.

#### 7 2 2 3 2 Duty to make an offer just before the grantor contracts with a third party

A simpler explanation of the proposed default type is that the grantor has an enforceable duty to make an offer to the holder at a specific point in time. This is

how many courts and writers have understood preference contracts.<sup>187</sup> The proposed default preference contract denies such a duty upon any manifestation of a desire to sell. Can such a duty be identified at any other point whilst adhering to the policy decision that the holder's right is not triggered in the absence of a third party offer or contract? It could be argued that the default construction still affirms the duty to make an offer immediately before the grantor agrees to contract with a third party.<sup>188</sup> Up to that point there is only an *obligatio non faciendi*. However, immediately before the grantor actually contracts with a third party, a duty to make an offer has arisen. The exact time and date upon which the grantor must make an offer is therefore only determinable once the grantor has contracted with a third party or made an offer to contract with the third party. Only at that point can one say at what time the grantor had to make the offer - namely the moment before. Therefore the grantor is only in breach upon contracting with or making an offer to the third party and can only be forced to make an offer at that point.

Conceivably, an objection may be raised that specific performance of the duty to make an offer *before* conclusion of a third party contract becomes impossible upon the grantor contracting with a third party, so that damages or setting aside a transfer to a *mala fide* third party are the only available remedies. This argument relies on the apparent absurdity of an *ex post facto* identification of a duty to make an offer. It amounts to classifying the type of breach as prevention of performance or repudiation where performance is impossible, and not merely as *mora debitoris*.

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<sup>187</sup> See for example, the minority decision by Ogilvie Thompson JA in *Owsianick v African Consolidated Theatres (Pty) Ltd*, the majority decision in *Soteriou v Retco Poyntons supra*, *Rogers v Phillips* 1985 3 SA 183 (E) 187D; Floyd 1986 THRHR 253 267; Flack 2001 SALJ 831 843; Eiselen 1986 THRHR 95 97, 99.

<sup>188</sup> Cf Floyd 1986 THRHR 253 259. (However, Floyd also regards a lesser manifestation of a desire to contract as a trigger event. He specifically mentions advertising the property for sale at 264. He also lays down that where there is no offer by a third party, the terms of the main contract must be established with reference to the terms which the grantor would require if he would have made an offer to the third party (260).)

However, the grantor can still make an offer to or contract with the holder even though he has contracted with a third party.<sup>189</sup> Performance of the duty would merely be late. The prerequisites for *mora debitoris* exist.<sup>190</sup> There is an *obligatio faciendi* and late performance still serves the contractual purpose. To say that breach of the obligation to make the offer in time renders the obligation impossible to enforce would mean that the stipulation of any date for performance would make performance after that date impossible, which is of course absurd and unacceptable. If the breach does amount to repudiation (which it most likely does)<sup>191</sup> it is of the kind where the innocent party can still obtain specific performance. If it can in fact be described as prevention of performance, then it is of the kind where substantial performance is still possible.<sup>192</sup>

Although an enforceable duty to make an offer the moment before the grantor agrees to contract with a third party may appear to be a strained construction, it is submitted that it is a logically sound construction and should be regarded as one of the possible juridical explanations of the default true preference contract.

Specific performance of this duty may be structured in various ways. Firstly, two separate actions could be required to enforce performance of the main contract. In terms of this construction, the court must first order the grantor to make an offer. Once this is obtained and accepted, the holder would have to approach the court in a separate action for specific performance of the main contract. This was the approach of the minority in *Owsianick v African Consolidated Theatres (Pty) Ltd.*<sup>193</sup>

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<sup>189</sup> Cf 1964 *Evidenzblatt* 239 240 where Austria's highest court followed Klang's and Ehrenzweig's opinion that the offer to the holder can be made before or after conclusion of the contract with the third party. (The court's statement is actually based on the view that making the offer after conclusion of the third party contract is not breach).

<sup>190</sup> Floyd 1986 THRHR 253 264 regards the breach as *mora ex re*.

<sup>191</sup> Floyd 1986 THRHR 253 264.

<sup>192</sup> Cf *Wireohms SA (Pty) Ltd v Greenblatt* 1959 6 SA 909 (C) 912; Lubbe & Murray *Contract supra* 483.

<sup>193</sup> *Supra*.

Alternatively, the court may be prepared to immediately order specific performance of the main contract and bypass or short-circuit an order that an offer be made. Alternatively, it may give such an order simultaneously with the order for specific performance of the main contract. In the latter case, the judgment is deemed equivalent to the action required of the grantor.<sup>194</sup>

As was noted in par 2 4 above, the decisions in *Dithaba Platinum v Erconovaal*<sup>195</sup> and *Malan v Schalkwyk & Odendaal*<sup>196</sup> support the possibility of such a short-circuited form of specific performance of the duty to make an offer. Both courts granted specific performance of the main contract. Both also confirmed the grantor's duty to make an offer.<sup>197</sup> An order that the grantor be ordered to do what he had agreed to do, namely to make an offer, was therefore bypassed or short-circuited.

However, as was noted before, the *Malan* case cited no authority in favour of such a remedy.<sup>198</sup> The decision in *Dithaba* was based on an apparently mistaken understanding of the *Oryx* mechanism as amounting to specific performance of the duty to make an offer, whereas the court in *Oryx* did not clearly regard it as such.<sup>199</sup> On the other hand, Van Heerden JA in *Oryx* did give some indication that he might possibly consider the *Oryx* mechanism to be "specific performance in the wide sense" when he stated that

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<sup>194</sup> Authority for such an approach can be found in Pothier *Treatise on the Contract of Sale* 6 1 1-6 1 3. He states that the act which is the fulfilment of an obligation to conclude a contract of sale may be supplied by a judgment decreeing that, in default of the debtor's being willing to pass a contract of sale, the judgment itself shall be equivalent to one. His comment relates not to preference contracts specifically, but rather to bilaterally binding agreements to conclude a contract in future. However, the principle is the same in both contexts.

<sup>195</sup> *Supra*.

<sup>196</sup> 1 S 225 (decided in 1852). The clause provided that should the grantor (the buyer) incline to part with the land, he would "give" same to the holder (the seller) for the original purchase price plus the value of the improvements.

<sup>197</sup> *Dithaba Platinum* case at 623E-F.

<sup>198</sup> For details, see par 2 4 *supra*.

<sup>199</sup> *Cf* 627D.

“indien ek ‘n wye diskresie sou hê om nie ‘n bevel gemik op spesifieke nakoming, in die breë sin, te verleen nie, ek...dit nie ten gunste van die respondente sou uitoefen nie.”<sup>200</sup>

In any event, it is practically expedient to recognise such a short-circuited remedy, not only in this context, but in all cases where a party is required to make a declaration of will before the other party is entitled to further relief. It is submitted that South African civil procedure should, like some overseas jurisdictions, recognise a rule that if a court considers a party bound to make a certain declaration of will, that declaration of will should be deemed to be made on the court’s decision to that effect. This should enable the court to order the party to give effect to that declaration of will in the same action or application. The advantages hereof are obvious.

For example, in Germany, article 894 *Zivilprozessordnung (ZPO)* creates a fiction that a declaration of will prayed for (such as an offer) is regarded as made upon the judgment granting the prayer. This procedural provision enables the holder of an *Angebotsvorhand* to sue in one action for both an order that an offer be made and an order that the contract created by acceptance of that offer, be performed.<sup>201</sup>

Whereas the High Court has the power to recognise such a rule by reason of its inherent power to regulate its own procedure,<sup>202</sup> the Magistrate’s Court Act or rules would probably need to be amended in this respect.<sup>203</sup> Amendment of the High Court Act or rules would be desirable in any event to remind courts of this power.

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<sup>200</sup> 919A (my emphasis). However, at 913F-G Van Heerden JA stated rather vaguely that: “Daar is nog ander oorwegings wat my laat twyfel of die regsposisie met betrekking to ‘n diskresie wat in sake soos die *Haynes*-saak supra geformuleer is, wel in ‘n geval soos die onderhawige toepassing vind. Vanweë die gevolgtrekking waartoe ek hieronder kom, veronderstel ek egter ten gunste van die respondente dat sodanige wye diskresie wel in casu uitgeoefen kan word.”

<sup>201</sup> See further par 4 1 3 1 2 *supra*.

<sup>202</sup> See, for example, the *Dithaba Platinum* case *supra*.

<sup>203</sup> The Magistrate’s Court has no jurisdiction to grant specific performance in the form of an order that an offer be made, unless damages is claimed as an alternative. If the order prayed for is for delivery or transfer of property up to R100 000, specific performance may be ordered (section 46(2)(b) of the Magistrate’s Court Act 32 of 1944). Suppose damages is claimed as an alternative, then the Magistrate’s Court would have no procedural power to short-circuit the order to make an offer, as its enabling legislation does not authorize this. Pothier *Treatise on the Contract of Sale* 6 1 1-6 1 3 states

Involving a court in the decision whether the holder is entitled to exercise his right and, if so, at what price, is advantageous where the offending third party contract contains some personal obligations, which the holder is prepared to compensate for by payment of a monetary sum. The court could then determine the terms of the “offer” to be made to the holder and grant an order that the grantor perform the ensuing contract in one action. The same advantage applies where the third party contract is a “package deal”.

Floyd also argues that exercise of the right of first refusal by unilateral declaration should be regarded as a “shortened form of specific performance” and should only be countenanced if it occurs by involvement of a court.<sup>204</sup> What this involvement entails and how it should be structured is not spelt out.

Another explanation of the holder’s entitlement to approach the court for specific performance of the main contract, is that contract law recognises a form of self-help specific performance in this context. This means that breach of the duty to make an offer before contracting with a third party entitles the holder to create the main contract extra-judicially upon the occurrence of breach. In a sense, the holder may perform on behalf of the grantor. The power to unilaterally create the contract derives from an *ex lege* (contract law) rule that specific performance is available in this form.<sup>205</sup> As such no special procedural power is required to enable the court to

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that the act which is the fulfilment of an obligation to conclude a contract of sale may be supplied by a judgment decreeing that, in default of the debtor’s being willing to pass a contract of sale, the judgment itself shall be equivalent to one. However, it is likely that this power of the court will be regarded as a procedural one which therefore requires a procedural mandate in the Magistrate’s Court Act.

<sup>204</sup> Especially at 267 *et seq.* (He calls this the “verkorte vorm van spesifieke nakoming”).

<sup>205</sup> *Cf* Van der Merwe *et al Contract* 68 who argue that the *Oryx* mechanism could be understood as a power or capacity to create the main contract by unilateral declaration, and then state that “The rules regarding specific performance would, of course, have to be developed to accommodate such situations.” Although they then proceed to compare the holder’s power with the power of an option holder to create the legal bond without agreement and the irrevocable authority given as security, both of which are not generally regarded as instances of extra-judicial specific performance, their reference to a development of the rules on specific performance suggest that they may regard the holder’s power

directly order performance of the main contract. The extra-judicial nature of this remedy is comparable to the *exceptio non adimpleti contractus*. Both are self-help extra-judicial contractual remedies aimed at enforcing specific performance. Of course, the remedy that I describe goes beyond the *exceptio non adimpleti contractus* as it does not simply allow withholding of performance to persuade the grantor to make an offer as promised, but amounts to the holder making the offer on the grantor's behalf. In this respect it is comparable to a remedy available to a lessee aggrieved by the lessor's failure to adequately maintain the leased premises. The lessee may effect the necessary repairs herself and claim these costs directly from the lessor.<sup>206</sup> This is not merely an application of the *exceptio non adimpleti contractus*, as the lessee is not only entitled to withhold the rental until the grantor repairs the defect, or indeed to withhold the rental to cover her repair costs. She may directly claim the costs from the lessor even if they exceed the outstanding rental. In a sense, the lessee is allowed to perform on the lessor's behalf. Similarly, the holder of the preference contract may be allowed to perform on the grantor's behalf.

Both remedies make economic and practical sense in the specific context, as orders that the breaching party should perform would often be ineffective and appear unnecessary and wasteful.<sup>207</sup> Continued refusal to perform is likely, and would require further, costly interventions by the court to persuade the breaching party to perform, such as a charge of contempt of court. The introduction of a rule that a penalty is payable for each day in which a party refuses to perform a court order<sup>208</sup> is probably valuable to deal with such cases, but has its own administrative demands. It

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to create the contract as a special form of specific performance. This is also how their view was interpreted (and endorsed) by Du Plessis *Spesifieke nakoming* 58.

<sup>206</sup> Cooper *Landlord and Tenant* 90; De Wet & Van Wyk 359; *Poynton v Cran* 1910 AD 205 217, 226; *Bowen v Daverin* 1914 AD 632; *Lester Investments v Narshi* 1951 2 SA 464 (C) 468; *Harlin Properties v Los Angeles Hotel* 1962 3 SA 143 (A) 150H. De Wet's comment on this remedy suggests the link with specific performance: "Volgens ons howe kan die huurder die verhuurder nie dwing om in forma specifica herstelwerk te doen...nie. Die huurder kan egter onregstreeks dieselfde resultaat bereik en wel deur self die herstelwerk te doen en die koste daarvan op die verhuurder te verhaal...."

<sup>207</sup> Cf Van der Merwe *et al Contract* 68; Schurig *Das Vorkaufsrecht* 53.

<sup>208</sup> Such a rule is recognised in Germany and the Netherlands. See par 5 2 2 1 1 (II) for details.

is more expedient that the innocent party be allowed to sort the problem out extra-judicially, without any court intervention being required.

In both contexts, the interests of the breaching party are sufficiently protected, so that intervention of the court is not required at the time of exercise of the power, or performance on the breaching party's behalf. The lessor must first be given a chance to effect the repairs herself, and could dispute the reasonableness of the repairs in court when the lessee claims these. In the vast majority of cases, breach of preference contracts would be cynical and the contents of the offer to be made would also almost always be absolutely clear.<sup>209</sup> If the grantor denies that breach had occurred or disputes the terms to which the holder is entitled to contract, he is still protected. He could simply withhold performance of the alleged main contract, forcing the holder to approach a court and to prove the lawful exercise of her right. The court would therefore still have the opportunity to hold that there was in fact no breach, that the breach was cured, that equities demand that the holder should only be entitled to damages or that the value placed by the holder on the subsidiary personal obligations undertaken by the third party was too low.

It therefore appears that our law recognises the need for a remedy of extra-judicial specific performance which goes beyond the *exceptio non adimpleti contractus* in specific contexts where policy considerations make this expedient, where the nature of the performance allows this and where the breaching party's interests are sufficiently protected.

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<sup>209</sup> It will be the terms agreed with or offered to the third party. Uncertainty on the terms on which the holder may contract may be caused where the third party has undertaken subsidiary personal obligations or when the object of a right of pre-emption has been sold as part of a package deal. There would also be uncertainty where the parties depart from the proposed default position by clearly providing for a lesser manifestation of a desire to contract as a trigger event to the holder's right to an offer or to contract. If the holder seeks to enforce this right before a contract with or offer to a third party, her right must necessarily relate to fair, reasonable or *bona fide* terms (if there is no usual price or other price determination). Perhaps holders should in such cases only be entitled to specific performance in the ordinary or short-circuited sense, so that a court determines the terms on which the offer is to be made. On the other hand, even in such a case, unilateral extra-judicial creation of the main contract would not really prejudice the grantor as his refusal to perform would force the holder to seek specific performance, and therefore, to prove that the power was exercised legitimately.

To object to such a remedy on the basis that it deviates from the normal scheme of contractual remedies, is not persuasive.<sup>210</sup> Legal concepts do not have a life of their own. An objection based on a present scheme of legal concepts should not be afforded too much persuasive force, especially not when the objection is based on the view that the default rules of specific contracts should be in absolute harmony with the principles (or default rules) of general contract law. As noted before, differentiation in the default rules or *naturalia* of specific contract types should be recognised in our law as a vehicle for mediating a fair balancing of the unique typical interests of parties to such contracts and the special policy considerations arising in that sphere. Recognition of a special remedy in the context of only one or two specific types of contracts is therefore not dogmatically suspect in itself.

If courts are uncomfortable with this extra-judicial version of specific performance, the shortened form of specific performance argued for above, with the necessary amendments to the Magistrate's Court Act, should be accepted as a suitable alternative. There is not much practical difference between these two conceptions of the holder's remedy. In both instances, the holder would have to approach the court once anyway when faced with an unrelentingly stubborn grantor, whereas under both systems the holder does not have to approach a court at all if the grantor could be persuaded that the holder is entitled to performance.

The default rules on termination that I have argued for also fit the present explanation of default true preference contracts. A failure to match terms offered by a third party amounts to waiver of the holder's right, as long as the grantor does in fact contract with and performs to the third party within a reasonable time. This latter qualification is consistent with the principles on waiver. It could be argued that the holder would not be prepared to waive his right if he realised that the grantor is making the offer without a serious intention to contract with and perform to the third party. Neither

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<sup>210</sup> Although writers like De Wet 358-359 argue that breach of the lessor's duty to maintain the premises should give rise to the normal remedies for breach, they do not criticise the availability of the special remedy referred to above.

could a failure to make an offer be seen as a waiver in the absence of sufficient information on the identity and terms offered by the competing third party.

The present juridical explanation also presents no logical obstacle to a cure of the breach after exercise of the holder's right. Insofar as the holder must approach a court before the main contract comes into existence, or may make the offer on the grantor's behalf, the grantor is not prevented from curing his breach before that point. If the holder's unilateral declaration of exercise is, by contrast, seen as acceptance of an offer embedded in the preference contract, resulting in a binding contract, it appears illogical to allow a cure that could destroy that contract. Therefore the present explanation leaves conceptual room for a policy decision that the holder is sufficiently protected by restoration of the *status quo ante* through a cure of the grantor's breach, even after the holder has indicated that he wishes to exercise the right.<sup>211</sup>

One conceivable objection against typifying the holder's right as an entitlement to an offer is that it does not logically force the holder to submit a binding undertaking that he would perform his side of the main contract upon exercising the right. The logical implication of the duty to make an offer is that the holder is only bound to perform once he accepts an offer by the grantor, and not already on his indication that he insists on such an offer. The grantor may therefore ultimately be left without anybody to contract with, having lost the interest of the third party on the holder's exercise of his right.<sup>212</sup>

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<sup>211</sup> The counter-argument against such an approach is the possibility of a further cynical breach by the grantor, which gives the holder a real interest in protecting his interest through enforcing performance of the main contract despite an avowal to cure.

<sup>212</sup> This danger is possibly what led the minority in *Soteriou v Retco Poyntons (Pty) Ltd* 935C to require that the holder should at least have declared "unequivocally and unqualifiedly" that he wishes to step into the shoes of the third party to avail himself of the *Oryx* remedy (937E-938D; cf *Kerr Sale and Lease* 298 n 31). This, the court said, should be done even where the holder is unsure of the contents of the third party contract, whereas he may then add to his unequivocal and unqualified declaration of intent that he would step into the third party's shoes insofar as they were not inconsistent with his continued use of the premises as before.

However, in the majority of cases this is not a well-founded objection against the present construction. If the grantor wants to know whether the holder is in fact serious about contracting, he should simply comply with the preference contract by making a voluntary offer to the holder to match the third party terms. A failure by the holder to accept this offer within a reasonable time, amounts to an election not to exercise the right, so that the grantor is free to continue with the third party contract. The same reasoning applies if the grantor can prove that the holder is unable to perform the contract. On the other hand, it may be argued that such a voluntary offer does not provide a solution for the grantor's predicament when he disputes an alleged breach on his part on the basis that the contract concluded with a third party entails personal obligations not susceptible to monetary valuation. Ultimately a court may find that there is breach and that he must make an offer, by which stage the third party may have lost interest, whereas the holder is not bound to accept the offer. In such a case, recognition that the holder might get extra-judicial, self-help specific performance would solve the problem.<sup>213</sup> The holder should not wait for an offer, but must bring the contract into being extra-judicially by a proper acceptance. Alternatively, if our courts should be unwilling to recognise extra-judicial specific performance as a remedy, one should accept that the juridical explanation considered here does not account for each and every implied term of preference contract. What needs to be added is a specific rule that the exercise of the holder's right should be unqualified and unequivocal and bind the holder even if it does not amount to acceptance of an offer still to be made.

What are the implications of the present construction for formalities requirements, most importantly, those of the Alienation of Land Act, 68 of 1981? As the preference contract does not itself contain an offer to sell the land, and as indication by the holder that she wishes to exercise her right does not amount to acceptance of such an offer, it is arguable that these declarations of will need not comply with the formalities requirements. That *Rogers v Philips*,<sup>214</sup> in conflict with the *Oryx* case, held that a right of pre-emption does not entail an offer, but merely gives the holder a personal right to

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<sup>213</sup> However, if such self-help specific performance is regarded as merely an alternative to normal specific performance of the default true preference contract, the problem remains.

<sup>214</sup> 1985 3 SA 183 (E).

an offer, explains why the court considered the formalities requirements inapplicable to the preference contract itself. The contrary decision in *Hirschowitz v Moolman*<sup>215</sup> is, however, also defensible on the basis that the purpose of the legislation would be thwarted if an oral preference contract could entitle the holder to a court order which effectively forces the grantor to transfer to the holder.<sup>216</sup> If that is the real reason why the formalities legislation should also apply to preference contracts, applicability of these requirements is not affected by the juridical explanation of the holder's remedy.

To regard a preference contract as creating an enforceable duty to make an offer the moment before the grantor makes an offer to or contracts with a third party, is on the whole a helpful and coherent way of understanding and explaining the default rules proposed. However, as there is still a possibility that courts may consider it too strained and contrived an explanation, I will consider one further possible explanation.

#### 7 2 2 3 3 Contractual power to create the main contract upon breach

This juridical explanation views the grantor's obligation as a negative one only, namely a duty not to contract with a third party unless the holder has failed to match the third party offer. Upon breach of this obligation, the law grants the holder a power to create the main contract.<sup>217</sup> In German legal terminology, the holder has a *Gestaltungsrecht*.<sup>218</sup> Added to this basic construction are the further default rules set out above. This construction therefore regards a preference contract as a *sui generis* contract with a set of default rules that aims to achieve a fair balance of the different

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<sup>215</sup> 1985 3 SA 729 (A) 767.

<sup>216</sup> The "anomalous situation" which would otherwise ensue, namely that the grantee could become a purchaser on the strength of a verbal contract, was an important reason for the court's decision. This view is approved by Lotz 386 and Van Rensburg "Formaliteitsvoorskrifte, Voorkoopregte en Opsies" 1986 *THRHR* 208 215.

<sup>217</sup> Breach logically only occurs once the grantor has concluded a contract with or made a valid offer to a third party.

<sup>218</sup> See par 4 1 1 2 *supra*.

interests and policy considerations involved. It refuses to provide a grand scheme explanation of all the default rules involved.

The implied power of the holder is justified by the policy considerations favouring a remedy by which the main contract can be enforced upon breach, and the inefficiency of an order that the grantor must contract with the holder. That the main contract is created by the holder's unilateral declaration is not unfair to the grantor as she has clearly promised this at the conclusion of the preference contract. Therefore the requirements for contractual liability are satisfied. Of course, no continuing *consensus* is required for contractual liability. An objection that the main contract as a separate agreement requires a new meeting of the minds or new grounds for reasonable reliance,<sup>219</sup> is overly dogmatic. If policy considerations do in fact command that the holder should be entitled to performance of the main contract upon breach, it makes no real difference to the grantor whether she is induced to conclude that contract by court order or whether the holder need not even approach a court to bring the main contract into being. The court's discretion to refuse specific performance where equity demands this still comes into play when the holder seeks enforcement of the main contract, regardless of whether the latter came into existence by court order or extra-judicially.

Various German writers and courts are content with explaining the *Vorkaufsrecht* as a contract granting the holder a *Gestaltungsrecht* or power to create the main contract by unilateral declaration upon conclusion of a third party contract.<sup>220</sup> Many others, however, insist on an explanation of the origin of the *Gestaltungsrecht*, for example, that there is an offer embedded in the preference contract, which, like all offers, grants

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<sup>219</sup> Cf Du Plessis *Spesifieke nakoming* 46-47.

<sup>220</sup> See par 4 1 1 2. Schurig *Das Vorkaufsrecht* 60 points out that, as the *Vorkaufsrecht* is based on the Germanic *ius retractus*, it remains difficult to fit this institution into an essentially Romanistic system of obligations. This is why even the first commission tasked with drafting the *BGB* merely listed a number of possible juridical explanations for this figure, and why many writers are content with the *Gestaltungsrecht* explanation which simply refers to the nature of the holder's remedy without explaining the origin of that right.

the addressee a power to create a contract by unilateral declaration in the form of an acceptance.<sup>221</sup>

As indicated above,<sup>222</sup> South African law knows the concept of contractual powers to unilaterally terminate or amend the contents of a contract or to bring a new contract into existence, which equates with the *Gestaltungsrecht* in German law. The power to cancel a contract for breach and the power to accept an offer are two examples.<sup>223</sup> No additional explanation of the origin of the power to cancel for breach is required. The law has simply decided, in view of the policy considerations and reasonable party expectations involved, that a party should in some circumstances have the power to unilaterally terminate the contract. Moreover, the power to withhold performance under the *exceptio non adimpleti contractus* could also be described as an *ex lege* contractual power which is used to induce specific performance of a contract, even though it possibly does not fall under the *Gestaltungsrecht* concept of German law, as it does not entitle the repository of the power to create, amend or terminate an existing contract. As there is no need to explain the origins of these *ex lege* powers in terms of the *consensus* between the parties, this should also not be necessary in the case of the power to unilaterally create the main contract upon breach of the preference contract. It is a power recognised on the basis of policy considerations, which is consistent with the parties' typical intentions. It does not prejudice the grantor in any way. If he disputes the occurrence of breach, the terms on which the holder is entitled to create the contract or the equity of enforcing performance to the holder, he should simply refrain from performing the contract allegedly created by the holder's declaration. This forces the holder to seek a court order for specific performance, which gives the grantor an opportunity to lay his concerns before a court. The court therefore retains

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<sup>221</sup> See par 4 1 1 2.

<sup>222</sup> See par 4 1 1 2.

<sup>223</sup> See Cockrell "Second-guessing the exercise of contractual power on rationality grounds" 1997 *Acta Juridica* 26. The Supreme Court of Appeal has also recognised that parties may agree on a power to unilaterally amend the contents of the contract in *NBS Boland Bank v One Berg River Drive CC* 1999 4 SA 928 (SCA). See also Lubbe "Kontraktuele diskresies, potestatiëwe voorwaardes en die bepaaldheidsvereiste" 1989 *TSAR* 159 and *Engen Petroleum Ltd v Kommandonek (Pty) Ltd* 2001 3 1013 (W). Cockrell 33 *et seq* gives examples of contractual powers created by express agreement.

the power to decide whether the holder has exercised the power in a legitimate way<sup>224</sup> and also retains its power to order damages instead of performance of the main contract to the holder. It could be pointed out again that refusal of specific performance of the preference contract itself has exactly the same effect as and would be based on exactly the same factors as refusal of specific performance of the main contract. The holder is granted damages to place him in the position he would have been in had the main contract been concluded. Objection to the holder's power to create the main contract on the basis that it strips the court of its equitable discretion to refuse specific performance is therefore unfounded.

Van der Merwe *et al* has supported the view that breach immediately vests the holder with a power or capacity to create a substantive contract by unilateral conduct.<sup>225</sup> Like the court in *Oryx*, they refer to the German concept of *Gestaltungsrechte* in support of their view.<sup>226</sup>

As was indicated before, another explanation of the holder's power is that it is not only an *ex lege* contractual power, classed along with any contractual power whether *ex lege* or consensual, but also a particular form of specific performance which our law of contract needs to recognise, at least in certain contexts.

In my opinion the best juridical explanation of the default true preference contract is that the grantor has a duty to make an offer to the holder immediately before contracting with a third party, which is enforceable upon breach by a contractual power to create the main contract by unilateral declaration and extra-judicially. This power can be understood as a form of self-help specific performance which is sanctioned in this context as the other party (the grantor) remains sufficiently protected by the court's discretion to refuse specific performance of the main contract created in this manner, and as an ordinary order for specific performance is superfluous, wasteful and likely to be disobeyed.

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<sup>224</sup> Cf Cockrell "Second-guessing the exercise of contractual power on rationality grounds" 28.

<sup>225</sup> 68.

<sup>226</sup> 68.

### 7 3 Exclusion of default rules

Under what circumstances would the proposed default rules be excluded?

This is obviously a matter of interpretation. In this process, courts should keep in mind the variety of preference contracts identified in previous chapters, and not just assume that there is only one logical and economically sensible construction. I have already argued that courts should generally not exclude evidence on prior negotiations by the parties, as the typical, brief formulations used by South African drafters are inherently ambiguous and wide enough to cover a whole spectrum of very different types of preference contracts.<sup>227</sup> Owing to this ambiguity, the admission of “parol evidence” would not generally result in the “amendment” of their contract, but rather only shed light on its proper interpretation.<sup>228</sup> In those rare cases where there is evidence that the parties have actually discussed the purpose, ambit or meaning of the preference agreement,<sup>229</sup> courts should carefully consider this evidence in an attempt to reflect the true agreement.

If the parties provide for a right to contract at a specified price should the grantor desire to contract, unless the grantor has obtained a better offer from a third party, the question arises whether the first or second default type should apply. It would be a matter of interpretation whether the parties intend that any manifestation of a desire to contract would allow the holder to enforce his right to contract, on condition that no

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<sup>227</sup> See further chapters 5 and 6 *supra*.

<sup>228</sup> On the admissibility of evidence to establish the proper interpretation of express provisions, see *Delmas Milling Co Ltd v Du Plessis* 1955 3 SA 447 (A) 454H-455B; *Richter v Bloemfontein Town Council* 1922 AD 57 70; *Consolidated Diamond Mines of South Africa Ltd v Administrator, SWA* 1958 4 SA 572 (A) 609E-F, 632 G-H; *Pritchard Properties (Pty) Ltd v Koulis* 1986 2 SA 1 (A) 10C-D; Kerr 328, 383; Vorster *Implied Terms* 13. Cf *List v Jungers* 1979 3 SA 106 (A).

<sup>229</sup> See, for example, *Dithaba Platinum v Erconovaal supra* 621C-D where the court was not prepared to hear evidence that the right of pre-emption was intended to prevent a specific competitor from obtaining the mineral rights in question, and not to prevent an internal restructuring of the grantor company, which resulted in the mineral rights being transferred from an external company to its wholly-owned subsidiary at a nominal price.

better offer exists. It is submitted, however, that a preference contract providing for the possibility of a price offered by a third party, reflects an interest on the part of the grantor to negotiate with third parties, so that the holder should not easily be allowed to force him to contract with her upon a mere manifestation of a desire to sell. The presumption should be in favour of the second default type. Parties with a contrary intention should clearly provide that any manifestation of a desire to contract should entitle the holder to contract on the predetermined terms, unless the grantor can point to a better third party offer when the holder exercises the right, in which case the holder only has a right to buy at the terms offered by the third party.

The effect of formulations typically employed by South African drafters should also be considered. The question arises whether they are in themselves sufficient to exclude the main default rules that I have proposed for true preference contracts.

The following formulations have been considered in our case law:

1. The grantor shall not have the right to sell the said property, until she has first offered it for sale to the holder.<sup>230</sup>
2. The grantor shall be obliged not to sell the thing except to the holder.<sup>231</sup>
3. The grantor shall not be entitled to sell the thing to others, but shall be obliged to give the holder the exclusive preference to buy.<sup>232</sup>
4. The holder shall have the first refusal to purchase the thing.<sup>233</sup>

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<sup>230</sup> As in *Wissekerke v Wissekerke supra* and the *Oryx* case *supra*. Cf *Crous NO v Utilitas Belville* 1994 3 SA 720 (C). Cf *Transvaal Silver Mines v Jacobs, Le Grange & Fox* 1891 4 SAR 116: in case the land came to be sold, it had first to be offered to the holder at the same price (presumably referring to the same price at which the remainder of the farm was sold to the holder).

<sup>231</sup> As in *Meyer, Smuts' Executrix v Meyer* 3 S 75.

<sup>232</sup> As in *Van Pletzen v Henning* 1913 AD 82.

<sup>233</sup> As in *Cohen v Behr* 1946 CPD 942 (coupled with a description of the period in which the holder will have such right). Cf *Aronson v Sternberg (Pty) Ltd* 1985 1 SA 597 (A) and *Soteriou v Retco Poyntons* 1985 2 SA 922 (A). In *Skinner v Goldberg* 1943 WLD 42 the court simply states that the holder's "request... for the right of pre-emption... was granted....". Cf *Hartsvrивier Boerderye (Edms) Bpk v Van Niekerk* 1964 3 SA 702 (T): if the grantor would decide to sell the thing, the holder shall have the first right of refusal to buy. Cf *Dithaba Platinum v Erconovaal supra*.

5. If the grantor desires to sell, he shall, before the conclusion of a sale, offer the object to the holder on the same price as he is prepared to sell to a *bona fide* purchaser.<sup>234</sup>
6. If the grantor desires to sell the object, he shall first offer it to the holder.<sup>235</sup>
7. The grantor agrees to (or shall) give the holder the first option to purchase the thing, should he desire to sell the thing.<sup>236</sup>
8. The grantor hereby gives the holder the first right and option to purchase the thing, should she decide to sell the thing.<sup>237</sup>
9. Any shareholder desirous of transferring his shares, shall give a notice to the directors (or secretary) of the company, stating the number of shares that he wishes to transfer and the price which he is willing to accept. The directors shall thereupon send to each of the other members of the company a circular containing these particulars and naming a day on or before which offers to purchase the shares will be received. If such offers are received at the price mentioned, the directors shall cause a contract to be concluded as the agent of the parties.... If the selling shareholder should not have received notice that his offer to sell has been accepted, he may within ... months sell or dispose of them at a price not less than that named in the notice of sale.<sup>238</sup>
10. Should the grantor desire to sell the object, he shall offer it to the holder.<sup>239</sup>

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<sup>234</sup> *Owsianick v African Consolidated Theatres (Pty) Ltd supra.*

<sup>235</sup> *Le Roux v Odendaal & Os* 1954 4 SA 432 (N). The clause added "at the highest price offered to him" to this formulation.

<sup>236</sup> *Sher v Allen* 1929 OPD 137; *Hirschowitz v Moolman* 1985 3 SA 729 (A)

<sup>237</sup> As in *Hattingh v Van Rensburg* 1964 1 SA 578 (T) and *Krauze v Van Wyk* 1986 1 SA 158 (A).

<sup>238</sup> *Cf Bellairs v Hodnett* 1978 1 SA 1109 (C); *Smuts v Booyens; Markplaas (Edms) Bpk en 'n Ander v Booyens* 2001 4 SA 15 (SCA). The similar clause in the statutes of the first respondent in *Associated South African Bakeries (Pty) Ltd v Oryx & Vereingte Bäckereien (Pty) Ltd supra* was not the right of pre-emption in issue. The dispute involved a later agreement worded like the one at n 230 *infra*.

<sup>239</sup> As in *Smith & Os v Momberg & Os* 1895 SC 295, where the contract specified a price. A similar clause is found in *Joseph's Executor v Peacock* 1868 Buch 247, where the price was specified as the original selling price plus the value of further improvements, which would be determined by agreement, or failing agreement, by arbitration. See also *Ah Ling v Community Development Board & Os* 1972 4 SA 35 (E) where the statute provided that an owner who desires to dispose of the property, shall offer to the Board and the Board shall thereupon have a preferential right to purchase at a price to be agreed, or failing agreement, to be fixed by arbitration.

11. The grantor agrees to (or shall) give the holder the option to purchase the thing, should he desire to sell the thing.<sup>240</sup>

The first three formulations are clearly not inconsistent with the proposed default construction. They do not contain any suggestion whatsoever that the grantor has an enforceable duty to make an offer upon a mere manifestation of a desire to sell. The negative formulation in these clauses is consistent with the default construction that the only enforceable obligation which exists prior to a contract with or offer to a third party, is a negative one, an *obligatio non contrahendo cum tertii*. I have already shown that there are indeed strong policy considerations why the holder should perhaps be limited to damages and remedies aimed at restoring the *status quo ante* upon breach of this negative obligation. It is possible that a court may wish to follow this route, especially in cases like these where the grantor's duty is merely expressed as a negative one. However, it is my submission that, on balance of the relevant policy considerations, courts should follow the default rule which I have proposed, namely that the holder should be entitled to performance of the main contract upon breach of the negative obligation.

The fourth clause is also not sufficient to exclude the default construction. I have already argued that the words "first refusal" do not logically force the conclusion that the grantor has an enforceable duty to make an offer upon a lesser manifestation of a desire to sell.<sup>241</sup> It can merely indicate that the grantor is supposed to give the holder the first chance to match (or refuse to match) any third party offer which the grantor considers accepting, whereas this is not an enforceable duty, and breach only occurs upon an offer to or contract with a third party.

The fifth formulation also makes it clear that as long as the grantor makes the offer *before* conclusion of a sale, he is not in breach of his contract, so that the holder

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<sup>240</sup> *McGregor v Jordaan* 1921 CPD 301, where the price was stated to be "at a price not exceeding £500". Cf *Crossroads Properties (Priv) Ltd v AI Taxi Service Co (Priv) Ltd* 1954 4 SA 514 (SR): in the event of the grantor desiring to dispose the thing, he shall give the right to the holder to purchase the thing at such terms and conditions as the grantor shall, *bona fide*, obtain from any other person.

<sup>241</sup> See par 2 1 1 *supra*, especially with reference to the minority judgment of Botha JA in *Soteriou v Retco Poyntons supra* at 936B-C on this point, approved of by Radesich 408-410.

cannot insist that she may “exercise” her right until he has actually concluded a sale. This is consistent with the default rules argued for here.

Neither do the sixth and seventh clauses exclude the default consequences proposed. They indicate that as long as the grantor makes the *first* offer or grants the *first* option to the holder and not to a third party, there is no breach or “trigger event”. This cannot therefore by itself import that the grantor has an enforceable duty to make an offer upon the manifestation of a desire to sell. As long as he does not first offer to contract with a third party, he is not in breach.

Similarly, the word “first” in the eighth formulation prevents an interpretation that the holder has already been granted an option to buy, which comes into operation the moment that the grantor desires to sell. It indicates that the holder must merely be preferred above third parties.

Provisions like the ninth clause, common in private company statutes, do not by themselves mean that the grantor could be forced to comply with the prescribed procedure when he informally expresses some desire to sell. Therefore this wording does not exclude the default construction that only a voluntary compliance with the procedure, or a sale in breach thereof, would entitle the holder to the remedies provided for.

The last two formulations are, in my view, the only ones open to an interpretation that the grantor has an enforceable duty to make an offer upon a lesser manifestation of a desire to sell, and not just on a sale in breach of the holder’s right. They do not qualify the duty to make an offer by the word “first”. It is not surprising that most such clauses considered in our case law, predetermined the price at which “the offer” was to be made. This was done either by reference to a fixed price or by a mechanism for fixing the price, for example by a third party. As I have indicated, if the price is predetermined in this manner, the parties do not intend a true preference contract but rather an option conditional upon the manifestation of a desire to contract.<sup>242</sup> In such cases, the holder should indeed have a right to contract upon any manifestation of a

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<sup>242</sup> This type of contract was discussed in par 7 2 1.

desire to sell. This should definitely be the case in those instances where the price determination is so clear that the holder has no interest in sounding out the market to establish the highest price obtainable.

What about the cases where the pre-emption clause accords with the last two clauses, but does not fall under the category just mentioned, as it does not predetermine the price, or refers only to “a price which the grantor would be prepared to accept from a third party.” In *Crossroads Properties (Priv) Ltd v AI Taxi Service Co (Priv) Ltd*,<sup>243</sup> for example, the lease provided that if the lessor *desires* to dispose of the property, he shall give the lessee the right to purchase it on the price and conditions that the lessor “shall, *bona fide*, obtain from any other person.” Should the lessee not buy the property within one month of such offer, the lessor would have the right to sell the property to anybody else. Does such a clause also mean that any manifestation of a desire to sell should “trigger” the holder’s right to buy at a *bona fide* price? It is submitted that the preference contract remains ambiguous, and could also mean that the grantor is expected, but cannot be forced, to submit any third party offers to the holder upon a manifestation of a desire to sell. The wording could mean that the making of the offer is the only method by which the grantor could be released from the duty to prefer the holder, whereas he cannot be forced to make such an offer, not even where he did obtain an offer from another person. In any event, the grantor cannot be said to have a “sustained and unqualified” desire to sell until he actually makes a voluntary offer to the holder or a third party.<sup>244</sup> The policy considerations in favour of a strict interpretation of preference contracts support such an interpretation, which remains in line with the proposed default type.<sup>245</sup> Therefore any lesser manifestation of a desire to contract should not entitle the holder to a *bona fide* offer.

However, once the grantor has made a voluntary offer, does a preference clause that refers to a *bona fide* offer entitle the holder to insist upon better terms if the holder can prove that the offer is not *bona fide*? As I have indicated before, this will be difficult to prove in the absence of a more advantageous offer to or contract with a

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<sup>243</sup> 1954 4 SA 514 (SR).

<sup>244</sup> See *Ah Ling v Community Development Board & Others supra* 39G.

<sup>245</sup> See also par 6 5 2 *supra*.

third party. An outrageously high offer by the grantor is not necessarily *mala fide*. Setting a very high price may simply be due to optimism or stupidity on the part of the grantor and not to a devious attempt to circumvent the holder's right.

It is therefore my submission that courts should not lightly hold that the holder is entitled to contract with the grantor upon a manifestation of a desire to sell in the absence of an offer to or contract with a third party. The first characteristic element of the default type should therefore not lightly be excluded.

What should justify a departure from the second basic characteristic of the proposed default type, namely the availability of a remedy by which the holder could enforce performance of the main contract? In other words, under which circumstances should the court hold that, apart from damages, only remedies aimed at restoring the *status quo ante* were intended by the parties?

Would evidence suffice that the holder's main contractual objective was the power to ward off unwanted third parties, whereas the holder had no desire to obtain the property for herself for any other reason? Could one argue that the parties therefore implicitly agreed that the holder should be content with remedies aimed at restoring the *status quo ante* the offending contract, especially where the grantor indicates that he is prepared to withdraw from the third party contract, even after exercise of the right? This differentiation between parties with different contractual purposes is certainly worthy of consideration. As indicated before,<sup>246</sup> the primary problem would be the difficulty of proving that the holder indeed had only a prohibitive purpose in concluding the contract, especially since the holder is likely to deny this during the trial. If it can be proved on a balance of probabilities, there is much to be said for allowing a cure of the breach even after "exercise" of the right by the holder. The argument by some German writers that this would be unfair to a holder who later developed a desire to obtain the object,<sup>247</sup> is not very convincing. If this change in contractual purpose was not communicated to the grantor, it should not also play a

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<sup>246</sup> This issue, including the views of German, Swiss and Austrian commentators, was discussed in par 6 4 2 *supra*.

<sup>247</sup> *Soergel & Siebert* (Huber) Vor § 504 RdNr 5.

role in the interpretation of the contract. Perhaps if this changed contractual purpose was communicated to the grantor who saw no reason to object thereto, the grantor was arguably not set against allowing the holder the benefit of the main contract upon breach. This would imply that he could not insist on cure after exercise of the right. A more weighty argument against exclusion of the proposed default rule is that even holders with a mere prohibitive purpose would wish to be protected against the possibility of further cynical breaches by enforcing performance. This issue will benefit from further debate by commentators and courts.

#### **7 4 The relationship between options and preference contracts**

The term “preference contracts” refers to those contracts where the grantor is unsure whether to contract at all or of the contract price that she would accept, but nevertheless promises to prefer the holder above third parties should she decide to contract or negotiate.

Option contracts, on the other hand, are contracts to keep an offer open. Therefore the decision to contract on the part of the grantor is already made. They can be conditional or unconditional.

Preference contracts and options are *pacta de contrahendo*, that is, “contracts aimed at the conclusion of another contract.”<sup>248</sup> Preference contracts and options overlap in respect of those preference contracts which predetermine the main contract price and those which allow the grantor to contract with a third party first, but grants the holder the preferential right to contract on the terms agreed with the third party. These preference contracts can be understood as conditional options. All such preference contracts are conditional upon the grantor manifesting a desire to conclude the main contract. This condition is what simultaneously places them in the “preference contract” category.

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<sup>248</sup> In the words of Van der Merwe *et al Contract* 56.

Ordinary preference contracts that do not predetermine the price and contain an *obligatio de non contrahendo cum tertii*, differ from unconditional options, firstly, in that a similar condition is added to the holder's right, namely that it only becomes enforceable upon a manifestation of a desire to sell. I have argued that the default rule should be that only a contract with or offer to a third party should be sufficient to trigger the holder's right to performance of the main contract. They could be described as options conditional upon breach of the *obligatio de non contrahendo cum tertii*, but that juridical explanation is somewhat forced in the case of ordinary preference contracts, as it is strained to say that a right is contingent upon conduct which is prohibited by the contract creating the right.

The abovementioned overlap between options and preference contracts shows that these categories of *pacta de contrahendo* are types that are part of a *Typenreihe* (row of types) with fluid borders. The one end of the spectrum consists of unconditional options comprising an offer granting an immediate power of acceptance to the holder. In a sense, these options also grant the option holder the "preferential" right to conclude the main contract, and they are therefore related to preference contracts. They are not, however, preference contracts. Preference contracts refer to those contracts where the grantor has not yet made an operative offer to the holder, but has promised to prefer the holder above anyone else when concluding, negotiating or performing the main contract. The other end of the spectrum consists of "first negotiation rights", which merely grant the holder the right to negotiate with the grantor first should the latter decide to contract. They are not options as they do not comprise an offer to contract, whether conditional or unconditional. Conditional options linked to some other condition than the desire to contract, for example, the grantor's son's marriage to the holder, are not preference contracts either, but remain options even though they do not comprise an immediately operative offer. The borders start to blur in respect of preference contracts with a predetermined price and preference contracts with no *obligatio non contrahendo cum tertii*.

## **7 5 Conclusion**

Three default types of preference contract should be recognised, each with a clearly delineated field of application.

Where the parties to a preference contract would allow the grantor to contract with a third party first, the holder has an option to contract at the terms agreed with the third party. The preference contract can therefore be regarded as an option conditional upon conclusion of a contract with a third party. Although commonly used in some European countries, such contracts are rare in South Africa.

In other cases, the default rule should be that the grantor must first give the holder a chance to contract before he contracts with a third party.

The default construction of these types of preference contracts depends on whether the preference contract itself predetermines the main contract price. If this is the case, the holder has a right or option to contract at that price upon any manifestation of a desire to conclude the relevant type of contract. Once again this type of preference contract can be understood as an option conditional upon the grantor manifesting a desire to sell. However, a reference to a price that the grantor would be prepared to accept from third parties or to a *bona fide* price, is not sufficient to place the preference contract in this category.

Where the preference contract does not predetermine the price, or refers to a price that the grantor would accept from third parties, any manifestation of a desire to sell should not be sufficient to trigger the holder's right. The grantor and society has a legitimate interest in having her freedom to negotiate with third parties to obtain the best possible price curtailed as little as possible. In such cases, the default rule should be that only a contract with or offer to a third party in breach of the holder's right constitutes breach, and the holder should only be entitled to the benefit of the main contract upon such breach. To distinguish this default type of preference contract from the previous one, I refer to it as the default ordinary preference contract, as it is the type most often encountered in modern South African practice. Such contracts only oblige the grantor to "prefer" the holder above interested third parties if the holder matches the terms offered by them, whereas the previous type actually gives the holder a right to contract at a specified price despite a better offer by a third party.

The default rule should be that ordinary preference contracts only terminate (in principle) upon the grantor actually contracting with and performing to a third party within a reasonable time after the holder declined the opportunity to match those terms, and provided the identity of the third party was disclosed to the holder on request. The holder therefore cannot lose his preferential right by rejection of an outrageously high offer by the grantor.

The holder's remedy upon breach of a true preference contract could be understood in a number of ways. Regardless of such juridical explanation, it is practically expedient that the holder faced with a recalcitrant grantor, should only be required to approach a court once after breach to obtain an order for specific performance of the main contract. This means that the holder's remedy should not merely be an order that the grantor make an offer. Such an order is difficult to enforce and, even where it is ultimately obeyed, may require the holder to approach the court again to enforce the main contract. The court's equitable discretion to refuse specific performance to the holder need only be exercised once, and refusal to enforce the main contract has exactly the same practical effect as refusal to make an order that an offer be made, or an order that the holder may not create the main contract by unilateral declaration. Concern for retention of the court's equitable discretion is therefore not a valid ground for insisting on a separate order that an offer be made.

One juridical explanation of the default ordinary preference contract is that the holder is entitled to an offer the moment before the grantor contracts with a third party, or offers to do so. This moment can therefore only be established once breach has in fact occurred, which therefore leaves the grantor free to negotiate without fear of action by the holder upon a lesser manifestation of a desire to contract. This explanation links up with the traditional understanding of preference contracts and allows for the fairest balancing of the typical party interests and policy considerations involved. In the interests of efficiency, breach should entitle the holder to obtain both an order that an offer be made and an order that the grantor perform the main contract in one action. The efficiency of the holder's remedy therefore depends on a rule of civil procedure that such a combined order may be made. Such a combined order is sanctioned by the procedural law of a number of overseas jurisdictions in cases where a party seeks both a declaration of will by another, and an order that this declaration

be enforced. Although the High Court has an inherent power to grant such an order, amendment to the Magistrate's Court Act is called for to allow such orders. Moreover, the South African High Court has been willing, on at least two occasions, to skip or short-circuit an order that an offer be made by directly ordering the grantor to perform the main contract upon breach, even though the court identified the obligation of the grantor as a duty to make an offer. If the holder's remedy is indeed regarded as specific performance of the duty to make an offer, the Magistrate's Court Act may need to be amended to recognise the possibility of such a short-circuited order, as it involves a procedural power.

There are also three alternative juridical explanations of the holder's ability to claim directly for specific performance of the main contract, which do not involve exercise of a special procedural power by the court. These explanations accept that the preference contract itself entitles the holder to unilaterally create the main contract upon breach.

The first is merely a variation on the explanation that the grantor has an enforceable duty to make an offer the moment before breach occurs. Instead of requiring an approach to court to obtain a short-circuited order for performance of the duty to make an offer against a recalcitrant grantor, our law can be said to recognise a self-help remedy of specific performance in this context, which allows the holder to create the main contract extra-judicially. As an extra-judicial remedy aimed at obtaining specific performance, this remedy is comparable to the *exceptio non adimpleti contractus*. However, it goes beyond the latter remedy as it effectively allows the holder to perform on the grantor's behalf. In this respect it is comparable to a remedy available to a lessee aggrieved by the lessor's failure to adequately maintain the leased premises. The lessee may effect the necessary repairs herself and claim these costs directly from the lessor if they exceed the outstanding rental. This remedy also goes beyond the *exceptio non adimpleti contractus*, as the lessee is allowed to perform on the lessor's behalf. Both remedies make economic and practical sense in the specific context, as orders that the breaching party should perform would often be ineffective and wasteful. In both contexts, the interests of the breaching party are sufficiently protected.

The second view is that the default true preference contract is an option conditional upon breach, which entitles the holder to contract on the terms agreed with or offered to the third party. Although there cannot be any objections to this juridical explanation on the basis of the supposed potestative nature of the condition or uncertainty of the price, it remains a rather strained and contrived construction, as it is not very likely that parties would agree that an option should only arise upon conduct that is actually prohibited. If the grantor is allowed to cure the breach when he no longer wants to contract at all, this construction is also not helpful.

The third view is that the preference contract creates an *obligatio non contrahendo cum tertii* and that breach thereof vests the holder with an *ex lege* contractual power or capacity to create the main contract by unilateral declaration. This power is recognised on the basis of policy considerations and the reasonable reliance created by the grantor that the holder would be entitled to contract upon breach. Our law knows the concept of contractual powers to unilaterally amend, terminate or create a new contract, such as the power to cancel upon breach or the power of an optionee to create the contract even against the wishes of the offeror. All these powers to unilaterally create, amend or terminate contracts are grouped together in German law under the concept of *Gestaltungsrechte*. The power of the holder of a *Vorkaufsrecht* to unilaterally create the main contract is also regarded as a *Gestaltungsrecht* by a number of German commentators and courts, and this explanation was also referred to in the *Oryx* case.

However, opponents of this juridical explanation of the *Vorkaufsrecht* argue that a mere description or classification of the holder's power is not a sufficient explanation thereof, and that the origin of the power must also be explained, for example, by labeling the preference contract as a conditional option contract.

Ultimately, the choice between these different juridical explanations does not make much practical difference. Courts should consider whether they deem such dogmatic explanations necessary to facilitate understanding and consistent and coherent application of the proposed body of default rules. In my opinion, such constructions would indeed be helpful for these reasons. The current uncertainty surrounding preference contracts is caused, to a large extent, by the absence of a coherent legal

explanation of the default rules on preference contracts, especially of the holder's ability to unilaterally conjure up the main contract by way of the *Oryx* mechanism. I prefer the explanation that the grantor has a duty to make an offer to the holder the moment before he contracts with a third party, which is enforceable upon breach by a contractual power to create the main contract by unilateral declaration and extra-judicially. This is consistent with the widespread view that the grantor has a duty to make an offer at some point as well as with the *Oryx* mechanism which provides a more efficient remedy than an order to make an offer. It could be explained as self-help specific performance analogous to the power of a lessee to perform the maintenance duties of a lessor on the latter's behalf and then claim compensation. The grantor remains sufficiently protected by the court's discretion to refuse specific performance of the main contract that the holder has created and by the court's scrutiny of the holder's right to have created the main contract when it is asked to enforce such contract. Where a voluntary offer or invitation to make an offer was rejected by the holder, the preference contract should only terminate once the grantor has contracted with and performed to a third party within a reasonable time after the holder was invited and failed to match her offer. This prevents circumvention of the holder's right through conclusion of a fake agreement with a third party. Where breach has occurred, the holder may request the court to order disclosure of the terms agreed with the third party to enable her to exercise her right.

It is a matter of interpretation whether the parties' agreement is sufficiently clear to exclude the proposed default rules. In interpreting the contract, courts should keep in mind the variety of preference contracts identified in previous chapters, as well as the policy considerations supporting the proposed default rules. Evidence on prior negotiations by the parties should not lightly be excluded as the typical, brief formulations used by South African drafters are frequently ambiguous. Often they are wide enough to cover very different types of preference contracts. Evidence on the purpose of a specific preference contract and the effect on that purpose of the transaction objected to is also relevant to establish whether the transaction indeed breaches the preference contract, and perhaps also, what the holder's remedies should be if it does.

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## Abbreviations

&	and
§	section / paragraph
2d	Second Series (USA)
3d	Third Series (USA)
A	Appellate Division
A	Atlantic Reporter (USA)
ABGB	Allgemeines Bürgerliche Gesetzbuch (Austria)
AC	Appeal Court (England)
AD	South African Supreme Court Appellate Division Reports
AG	Aktiengesellschaft (Germany)
All ER	All England Law Reports (England)
ALR	American Law Reports Annotated
ALR 2d	American Law Reports Annotated Second Series
ALR 3d	American Law Reports Annotated Third Series
ALR 4th	American Law Reports Annotated Fourth Series
App	Appeal Court (USA)
App Div	Appellate Division (USA)
art	article
BB	Betriebs-Berater (Germany)
BFH	Bundesfinanzhof (Germany)
BGB	Bundesgesetzbuch (Germany)
BGH	Bundesgerichtshof (Germany)
BGHZ	Entscheidungen des Bundesgerichtshofs in Zivilsachen (Germany)
Buch	Buchanan's Law Reports
C	Cape Provincial Division
C	Codex (of Justinian)
CA	Court of Appeal (England)
Cal App	California Appeal Court (USA)
Cal Rptr	California Reporter (USA)
<i>cf</i>	compare

<i>CF</i>	Censura Forensis
Ch App	Chancery Appeal Court
Ch D	Chancery Division (England)
Ch	Chancery Division (England)
Cir	Circuit (USA)
CLJ	Cape Law Journal
CLJ	The Cape Law Journal
Co	Company
CPD	South African Supreme Court Law Reports, Cape Provincial Division
<i>D</i>	Digesta (Digest of Justinian)
D&C	Durban and Coast Local Division
DLR	Dominion Law Reports
DNotI-Report	Deutsche Notarial Report (Germany)
DNotZ	Deutsche Notar-Zeitschrift (Germany)
E	Eastern Cape Provincial Division
ed	editor
eds	editors
EFG	Entscheidungen des Finanzgerichts (Germany)
EG	Estates Gazette (England)
EGLR	Estates Gazette Law Reports (England)
et seq	et sequitur (and following)
EWiR	Entscheidungen zum Wirtschaftsrecht
F	Federal Reporter (USA)
Gr	Grotius
GRUR	Gewerblicher Rechtsschutz und Urheberrecht (Germany)
HHA	Hoogste Hof van Appèl
HRR	Höchstrichterliche Rechtsprechung (Germany)
ILJ	Industrial Law Journal
Ill	Illinois (USA)
<i>Inl</i>	Inleidinge tot de Hollandsche Rechtsgeleerdheid
JW	Juristische Wochenschrift (Germany)
K	Kaapse Provinsiale Afdeling
LG	Landesgericht (Germany)
Ltd	Limited

Md	Maryland (USA)
Mich	Michigan (USA)
Mo	Missouri (USA)
N	Natal Provincial Division
n	note / footnote
NC	Northern Cape Provincial Division
NE	Northeastern Reporter (USA)
Neb	Nebraska (USA)
NH	New Hampshire Supreme Court Reports (USA)
NJ Super	New Jersey Superior Court Reports (USA)
NJB	Nederlands Juristenblad (Netherlands)
NJW	Neue Juristische Wochenschrift (Germany)
NK	Noord-Kaapse Provinsiale Afdeling
NLR	Natal Law Reports
Nr	Number
NYS	New York Supreme Court (USA)
O	Orange Free State Provincial Division
OGH	Oberste Gerichtshof (Austria)
Or App	Oregon Appeal Court (USA)
OH	Outer House (Scotland)
OLG	Oberlandesgericht (Germany)
OLGR	Oberlandesgericht Report (Germany)
OLGR	Oberlandesgericht Report (Germany)
Ont Ct	Ontario Court (USA)
OPD	South African Supreme Court Law Reports, Orange Free State Provincial Division
OVG	Oberverwaltungsgericht (Germany)
Pa	Pennsylvania (USA)
par	paragraph
paras	paragraphs
PCR	Planning and Compensation Reports (England)
P&CR	Property and Compensation Reports (previously Planning and Compensation Reports) (England)
Pty	Proprietary

RdNr	Rand Nummer (German)
RG SeuffA	Reichsgericht Seuff Archiv (Germany)
RGZ	Entscheidungen des Reichgerichtshofs in Zivilsachen (Germany)
<i>RHR</i>	Het Rooms-Hollands Regt
S	Searle's Cases in the Supreme Court
SA	Juta's South African Law Reports
SAJHR	South African Journal of Human Rights
SALJ	South African Law Journal
SAR	South African Law Reports
SC	Supreme Court Law Reports
SCA	Supreme Court of Appeal
SE	Southeastern Reporter (USA)
SEC	South Eastern Cape Local Division
SLT	Scots Law Times (Scotland)
Sol Jo	Solicitor's Journal and Reporter (England)
SR	Southern Rhodesia
Stell LR	Stellenbosch Law Review
SW	Southwestern Reporter (USA)
SWA	Reports of the High Court of South West Africa
SZ	Sammlung der Entscheidungen des Obersten Gerichtshofs in Zivil- und Justizverwaltungsachen (Austria)
T	Transvaal Provincial Division
Tenn Ct App	Tennessee Court of Appeal (USA)
Tex App	Texas Appeal Court (USA)
<i>Th</i>	Theses Selectae
THRHR	Tydskrif vir Hedendaagse Romeins-Hollandse Reg (Journal of Contemporary Roman-Dutch Law)
TPD	Transvaal Provincial Division Law Reports
TS	Transvaal Supreme Court Reports
TSAR	Tydskrif vir die Suid-Afrikaanse Reg
Vol	Volume
Vor	Vorbemerkung (German)
Vorbem	Vorbemerkung (German)
W	Witwatersrand Local Division

WD Tenn	Weekly Digest Tennessee (USA)
WL	Westlaw (USA)
WLD	South African Supreme Court Law Reports, Witwatersrand Local Division
WLR	Weekly Law Reports (England)
WM	Wertpapier Mitteilungen (Germany)
ZPO	Zivilprozessordnung (Germany)
ZSC	Zimbabwe Supreme Court