REPUBLIC OF SOUTH AFRICA

IN THE SUPREME COURT OF APPEAL OF SOUTH AFRICA

Reportable
Case Number : 440 / 03

In the matter between

SOUTHERNPORT DEVELOPMENTS (PTY) LTD **APPELLANT**

and

TRANSNET LTD **RESPONDENT**

Coram: **HARMS, FARLAM, CAMERON JJA, COMRIE et PONNAN AJJA**

Date of hearing : **16 AUGUST 2004**

Date of delivery : **29 SEPTEMBER 2004**

SUMMARY

Contracts - **lease- essential elements of - restated**
- **an agreement to negotiate in good faith - which is linked to a provision that an arbitrator's award will be final in the event of a dispute between the parties – does not lack certainty - such an agreement to be distinguished from an unenforceable agreement to agree.**

J U D G M E N T

PONNAN AJA

[1] On 7 December 1998, the appellant's predecessor in title Tsogo Sun Ebhayi ('Tsogo Sun') concluded a written agreement ('the first agreement') with the respondent ('Transnet'). The first agreement was subject to a suspensive condition that Tsogo Sun be granted by 31 December 1999 a casino licence as contemplated by the Eastern Cape Gambling Act. It recorded that Tsogo Sun wished to develop a temporary casino, temporary casino parking, a casino, a hotel and certain ancillary entertainment and retail facilities with ancillary parking on portions of erven 1051, 578 and 577 Humewood (collectively referred to in the first agreement as 'the properties'). To that end Tsogo Sun was authorised to procure the rezoning or special consent to utilise the properties for the purpose specified in the agreement. The extent of the erf, the subject in each instance of the agreement, was specified in the first agreement and clearly demarcated on a plan annexed thereto.

[2] On 10 February 2000 the parties concluded a second written agreement ('the second agreement'). The second agreement, described by the parties as a bridging agreement, provided for the conclusion in due

course of a definitive agreement in the event of Tsogo Sun's application for a casino licence succeeding and an alternative agreement should it fail.

[3] Clause 3 of the second agreement, to the extent here relevant, provides:

> '**3.1.2** In the event that the Tsogo Sun Ebhayi casino licence application fails, and all appeals, reviews and other legal challenges initiated by Tsogo Sun Ebhayi that may potentially prohibit the exploitation of the casino licence granted to a competitor of Tsogo Sun Ebhayi in the Port Elizabeth zone, Eastern Cape Province (if any) are finally resolved in favour of that competitor then for three years from that date or from the date of the award of the casino licence to that competitor if no such appeal, review or other legal challenge is made as the case may be, Tsogo Sun Ebhayi (or its nominee) shall have the option to lease the properties (or the agreed portions thereof) on the terms and conditions of an agreement ("the alternative agreement") negotiated between the parties in good faith and approved by each of the party's board of directors.'
>
> '3.4 Should the parties be unable to agree on any of the terms and conditions of either the definitive agreement or of the alternative agreement within 30 days of the date of any notice given by either of such parties to the other of them requiring such agreement, then the dispute shall be referred for decision to an arbitrator agreed on

by the parties. The arbitrator's decision shall be final and binding on the parties. If Tsogo Sun Ebhayi and Transnet are not able to agree on that arbitrator within five days of either of them calling on the other to do so, then that arbitrator shall be selected for that purpose by the Arbitration Foundation of South Africa, and the arbitration shall be finalised in accordance with the Foundation's expedited arbitration rules.'

[4] Premised on the factual foundation that Tsogo Sun's licence application was unsuccessful and that Transnet had failed pursuant to the second agreement to enter into good faith negotiations with its predecessor, the appellant instituted action against Transnet claiming the following relief:-

'1. The defendant be required forthwith, to enter into good faith negotiations with the plaintiff regarding the terms and conditions of an agreement of lease in respect of the properties described in clause 1 of annexure "PC 1".

2. That any dispute between the parties be referred for decision by an agreed or selected arbitrator, as the case may be, in accordance with clause 3.4 of the second agreement, annexure "PC 2" hereto, if the parties are unable to reach agreement on the terms of the alternative agreement, within 30 days from the date of this order.'

[5] The appellant's particulars of claim were met with an exception, which was upheld by Blieden J in the High Court (Johannesburg). With leave of the learned trial judge the matter is now before this Court on appeal. The judgment of the court *a quo* is reported as *Southernport Developments (Pty) Ltd (previously known as Tsogo Sun Ebhayi (Pty) Ltd) v Transnet* 2003 (5) SA 665 (W). The principal thrust of the argument advanced on behalf of Transnet, is: first, there was no agreement between the parties regarding the essential terms of a lease, and, secondly, the second agreement was an unenforceable preliminary agreement. Each of those contentions will be considered in turn.

(i) *Was there agreement between the parties as to the essential terms of a lease agreement?*

[6] The essentials of a contract of lease are that there must be an ascertained thing and a fixed rental at which the lessee is to have use and enjoyment of that thing (*Kessler v Krogmann* 1908 TS 290 at 297; Cooper, *Landlord and Tenant* 2 ed p3). The parties had not agreed upon the use and enjoyment of the property, which according to Blieden J was 'a requirement in any lease agreement such as the one relevant in the present case'. Whilst it is always open to parties to a contract of lease to agree on the intended use of the leased property (and if they do that would

constitute a material term of the agreement (see *Oatorian Properties (Pty) Ltd v Maroun* 1973 (3) SA 779 (A) at 785G) as also, the period of the lease, failure so to do would not invalidate the agreement. For those are not, in each instance one of the essentialia of an agreement of lease (Pothier's *Treatise on the Contract of Letting and Hiring* para 28). It is worth noting, I may add, that the nature of the use and the enjoyment of the property usually flows from the nature of the property itself. In the case of land, that is usually dictated by external factors such as the nature or zoning of the property.

[7] It is indeed so that Clause 3.1.2 of the second agreement contained no agreement on the rental to be paid. Our law has, however, long accepted that principal parties to a contract may delegate to a third party the responsibility of fixing certain terms. Thus parties may validly agree that the price of an article sold may be fixed by a named third party (Grotius 3.14.23) and they may leave the determination of the rental in a lease agreement to a particular arbitrator (Voet 19.2.7). (See also *Genac Properties Jhb (Pty) Ltd v NBC Administrators CC (previously NBC Administrators (Pty) Ltd)* 1992 (1) SA 566 (A); *Benlou Properties (Pty) Ltd v Vector Graphics (Pty) Ltd* 1993 (1) SA 179 (A); *NBS Boland Bank Ltd v One Berg River Drive CC and Others, Deeb and Another v ABSA Bank Ltd,*

Friedman v Standard Bank of SA Ltd 1999 (4) SA 928 (SCA); *Engen Petroleum Ltd v Kommandonek (Pty) Ltd* 2001 (2) SA 170 (W).)

[8] In *Letaba Sawmills (Edms) Bpk v Majovi (Edms) Bp*k 1993 (1) SA 768 (A), an option to renew a lease on the basis that the rental was to be determined by arbitrators ' … within the limits of market-related prices for the timber on the leased property and rental payable in respect thereof … ' was held not to be vague. Even though the concepts 'market-related prices' and 'market price' were not defined, this Court held (per Botha JA) that it was not necessary for the parties to formulate a precise, mathematical criterion for the determination of the rental. In the view of Botha JA the rent remained determinable even though the valuers might so differ over the actual amount as to embroil the court in a protracted hearing.[1] I can conceive of no reason why the principle that *Letaba Sawmills* so firmly establishes should be circumscribed to the determination solely of the rental in a contract of lease. The flexibility that *Letaba Sawmills* introduces must logically extend to other terms as well the formulation of which the parties to a contract may have chosen to delegate to a third party.

[1] Martin Brassey: 'The Law of Lease' (1993) *Annual Survey* p188.

[9] What distinguished *Letaba Sawmills* from the present case, according to Blieden J, is that in the former

> ' ...each party … nominated its own ***"arbitrator"*** to state its case. In the event of these two ***"arbitrators"*** not coming to an agreement a third ***"arbitrator"*** would be jointly appointed and he would determine the matter on the basis of the one or other of the two agreements presented to him… [I]n the present case the ***"arbitrator"*** has been appointed with one purpose, and one purpose only, and that is to determine disputes between the parties'.

For the reasons that follow, in my view, the distinction sought to be drawn by the court *a quo* between *Letaba Sawmills* and the instant case is more illusory than real.

[10] The option granted to Tsogo Sun was one to lease all of the properties, which as I already stated were clearly identified in the first agreement. Well, what if Tsogo Sun wanted to exercise the option in respect of a portion only of the agreed properties, asked the court *a quo*, and no agreement could be reached between the parties as to the properties (or portions thereof) to be leased? The ready answer to that query, it is seems to me, is to be found in the agreement itself. Applying the principle enunciated in *Letaba Sawmills*, that 'dispute' could be determined by the arbitrator. But that did not constitute a 'dispute' within

the meaning of that expression, the court *a quo* postulated. In that, in my view, the learned judge was wrong. The word ‘dispute’ must be interpreted in its contextual setting (*Coopers and Lybrand and Others v Bryant* 1995 (3) SA 761 (A)). The parties undertook to enter into good faith negotiations to agree upon terms and conditions of a lease agreement. In default of consensus between the parties the agreement provided for arbitration. Failure by the parties to agree would constitute a dispute within the meaning of that expression thus justifying a referral to arbitration.

(ii) *Is the second agreement an unenforceable preliminary agreement?*

[11] In upholding the exception Blieden J stated: '[T]here simply is no agreement between them. The fact that the words "*good faith*" have been used to describe the negotiation process, takes the matter no further'. Support for his conclusion, he believed, could be found in the dictum of Schutz JA in *Premier, Free State, and Others v Firechem Free State (Pty) Ltd* 2000 (4) SA 413 (SCA) para 35 ('*Firechem*') that '[A]n agreement that parties will negotiate to conclude another agreement is not enforceable, because of the absolute discretion vested in the parties to agree or disagree’. That principle, it must be stated, falls far short of resolving the issue that arises in the present case. The reliance by Blieden J on *Firechem* is, in my view, misplaced. The contract under consideration in

Firechem contained no deadlock-breaking mechanism. In the present case, the agreement prescribes what further steps should be followed in the event of a deadlock between the parties. The engagement between the parties can therefore be analysed as requiring not merely an attempt at good faith negotiations to achieve resolution of any dispute but also the participation of the parties in a dispute resolution process that they have specifically agreed upon.

[12] The duty to negotiate in good faith is known to our law in the field of labour relations. There, as well, because of the public interest in ensuring harmony in the workplace, deadlock-breaking mechanisms exist to ensure that the negotiating process is legally meaningful. The analogy between ordinary contract negotiations and collective bargaining in our labour law regime is, to be sure, less than perfect. In ordinary contract negotiations there is usually no public interest in a successful outcome or in the process of good faith negotiations itself that is comparable to the interest in preventing labour strife.[2] In *National Union of Mineworkers v East Rand Gold and Uranium Co Ltd* 1992 (1) SA 700 (A), this court held at 733I

[2] Nevertheless, helpful comparisons can be made and useful analogies have been drawn by the U S courts in the application of their Labor Relations Act. cf Prof Allan Farnsworth: 'Pre-contractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations' (1987) 87 *Columbia Law Review* p217 at 271

> '[T]he fundamental philosophy of the Act[3] is that collective bargaining is the means preferred by the Legislature for the maintenance of good labour relations and for the resolution of labour disputes'

and later at 734 D:

> '… the very stuff of collective bargaining is the duty to bargain in good faith'.[4]

The principle of fairness has come to be the overriding consideration in labour relations and the labour courts eventually held that in general terms a failure to negotiate in good faith may amount to an unfair labour practice with the consequences that attach to such a practice.[5]

[13] '[U]nlike some systems of law,[6] English law refuses to recognise a pre-contractual duty to negotiate in good faith, and will neither enforce such

---

[3] The Labour Relations Act 28 of 1956.

[4] See also A. Basson: 'Collective Bargaining and the Appellate Division' (1992) 4 *SA Merc LJ* p97; and SR van Jaarsveld and BPS van Eck: Principles of Labour Law (2000) p149.

[5] Although the duty to bargain in good faith has not been expressly incorporated into the current Act, its provisions patently seek to promote collective bargaining. Employers are obliged to consult and reach consensus with workplace forums before implementing a wide range of decisions. See John Grogan: Workplace Law 7ed (2003) p 309.

[6] European courts have been more receptive than American ones to scholarly proposals for pre-contractual liability based on a general obligation of good faith. German law has developed rules regarding good faith negotiations. The doctrine of good faith plays a most important role in the emerging field of secondary or auxiliary contract obligations in Germany. [The primary obligation of the parties is to perform in terms of the contract. The secondary obligation specifies how the parties have to perform.] Within that category courts have recognised an obligation on contracting parties to bargain in good faith and to deal fairly with each other particularly where the parties have reached agreement on that question. [Werner F. Ebke and Bettina M. Steinhauer: 'The Doctrine of Good Faith in German Contract Law' Jack Beatson and Daniel Friedman: Good Faith and Fault in Contract Law (1995) p171.] Italian scholars have mostly looked for inspiration to German doctrines on good faith. In France principles of good faith extend to both the negotiation and performance of contracts despite the limited terms of the *Code Civil*. Although the French *Code Civil* has been influential in Belgium, Belgian courts have relied more extensively than their French counterparts on the principle of good faith in the performance of contracts. [Simon Whittaker and Reinhard Zimmermann: 'Good Faith in European contract law: surveying the landscape' R.Zimmermann and S. Whittaker: Good Faith in European Law (2000) p 7.] French and Israeli law gives

a duty when it is expressly agreed nor imply it when it is not'. (Per Millet LJ in *Little v Courage Ltd* (1994) 70 P. & C.R. 469 at 475.) Irish and Scots courts have, by and large, followed the same approach as their English counterparts.

[14] In the United States the enforceability of agreements to negotiate in good faith varies from state to state. Each state has its own separate and relatively self-sufficient body of general contract law. In the 1960s the Uniform Commercial Code (UCC)[7] was introduced and adopted by the American state legislatures. Section 205 of the 'Restatement[8] of Contracts Second'[9] like the UCC limits the duty of good faith to the performance and the enforcement of a contract already made. In general the requirement of good faith in American law does not apply to contract negotiations.[10] Some courts, like the English courts, refuse on the ground of indefiniteness, to enforce explicit agreements to negotiate in good faith. Other courts

---

effect to an express contract to negotiate in good faith. [Nili Cohen:'Pre-contractual Duties: Two Freedoms and the Contract to Negotiate' Beatson and Friedman op cit p25.]

[7] Section 1-203 provides: "Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement".

[8] The American concept of a "Restatement" represents an attempt by the American Law Institute, a private organisation of scholars, judges and practitioners to formulate with some precision the leading rules and principles in major fields of American law.

[9] Section 205 provides: Duty of Good Faith and Fair Dealing – 'Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement'.

[10] Robert S. Summers: 'Good Faith in American Contract Law' Zimmermann and Whittaker: op cit p118.

however have been willing to give effect to the expressed intentions of the parties. The latter view has gained a substantial following.[11]

[15] Certainty, it would appear, is the touchstone of enforceability of agreements to negotiate in good faith in Australia.[12] In *Coal Cliff Collieries (Pty) Ltd v Sijehama (Pty) Ltd* (1991) 24 NSWLR 1, Kirby P stated at 26E - 27B:

> 'From the foregoing it will, I hope, be clear that I do not share the opinion of the English Court of Appeal[13] that no promise to negotiate in good faith would ever be enforced by a court. I reject the notion that such a contract is unknown to the law whatever its term. I agree with Lord Wright's speech in Hillas[14] that, provided there was consideration for the promise, in some circumstances a promise to negotiate in good faith will be enforceable…. Nevertheless, … I believe that the proper approach to be taken in each case depends upon the construction of the particular contract:..'

[16] Kirby P then adverted to three situations. He stated of the first:

---

[11] Prof Allan Farnsworth: op cit p264-9

[12] Ian B Stewart: 'Good Faith in Contractual Performance and in Negotiation' (1998) 72 *The Australian Law Journal* p370.

[13] See *Courtney and Fairbain Ltd v Tolaini Brothers (Hotels) Ltd and Another* [1975] 1 W.L.R. 297 C.A.; and *Walford and Others v Miles and Another* [1992] 2 A.C. 128 at 138.

[14] In *Hillas and Co Ltd v Arcos Ltd* in (1932) 147 L.T. 503 at 515, Lord Wright stated: where the parties agreed only to negotiate, the negotiations may be 'fruitless and end without any contract ensuing; yet even then, in strict clear theory, there is a contract (if there is good consideration) to negotiate …'
In *Courtney and Fairbairn Ltd v Tolaini Brothers (Hotels) Ltd and Another* Lord Denning M.R. rejected the views of Lord Wright in *Hillas*. In agreeing with Lord Denning, Lord Diplock described Lord Wright's dictum as bad law, '…although an attractive theory.' Lord Denning held '[I]t seems to me that a contract to negotiate, like a contract to enter into a contract, is not a contract known to the law.'

> 'In many contracts it will be plain that the promise to negotiate is intended to be a binding legal obligation to which the parties should be held. The clearest illustration of this class will be cases where an identified third party has been given the power to settle ambiguities and uncertainties… But even in such cases, the court may regard the failure to reach agreement on a particular term as such that the agreement should be classed as illusory or unacceptably uncertain:… In that event the court will not enforce the agreement.';

of the second:

> 'In a small number of cases, by reference to a readily ascertainable external standard, the court may be able to add flesh to a provision which is otherwise unacceptably vague or uncertain or apparently illusory…';

and, of the third:

> 'Finally, in many cases, the promise to negotiate in good faith will occur in the context of an "arrangement"(to use a neutral term) which by its nature, purpose, context, other provisions or otherwise makes it clear that the promise is too illusory or too vague and uncertain to be enforceable:…'.

The principles enunciated in *Coal Cliff Collieries* accord with our law. The first and third situations alluded to by Kirby P are covered, respectively, by *Letaba Sawmills* and *Firechem.*

[17] It cannot be said that a third party was making a contract for Tsogo Sun and Transnet which they themselves had not put into words. The

second agreement had settled all of the essential terms between the parties and was immediately binding, although fuller negotiations to settle subsidiary terms were still within the contemplation of the parties in accordance with the continuing relationship between them. Simply put, the arbitrator was entrusted with putting the flesh onto the bones of a contract already concluded by the parties. Accordingly there is no sound basis why Transnet should not be held to the contractual obligation, it undertook. It needs to be emphasised that on the facts here present a court would not be making the contract for the parties thereby going beyond its adjudicative role. In that sense it is the very exercise of the right to contract, which has bound the parties to the negotiation in good faith, which they promised. Thus, to enforce that undertaking is not to interfere in the parties' freedom to contract, but to uphold it (*Coal Cliff Collieries* at 26 C-D). Nor for that matter could it be suggested that the second agreement constituted an agreement to agree, which was dependent on the absolute discretion of the parties. For, what elevates this agreement to a legally enforceable one and distinguishes it from an agreement to agree is the dispute resolution mechanism to which the parties have bound themselves. The express undertaking to negotiate in good faith in this case is not an isolated edifice. It is linked to a provision that the parties, in the event of them failing to

reach agreement, will refer such dispute to an arbitrator, whose decision will be final and binding. The final and binding nature of the arbitrator's decision renders certain and enforceable, what would otherwise have been an unenforceable preliminary agreement. It follows that the appeal must succeed.

[18] In the result:

(a) The appeal is upheld with costs such costs to include those consequent upon the employment of two counsel.

(b) The order of the court a quo is set aside and replaced by the following:

'The exception is dismissed with costs including the costs of two counsel.'

V M PONNAN
ACTING JUDGE OF APPEAL

CONCURRING:

HARMS JA
FARLAM JA
CAMERON JA
COMRIE AJA