

CORPORATE AND COMMERCIAL

SALE OF BUSINESS
AGREEMENTS:
THE IMPLIED RESTRAINT
ON CANVASSING
CUSTOMERS

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A recent decision of the Western Cape High Court has highlighted some critical considerations to be borne in mind when dealing with restraint of trade and non-solicitation clauses contained in, for example, sale of business agreements, if such sales include the goodwill of the business (*Grainco (Pty) Ltd v Van Der Merwe and Another* 2014 (5) SA 444 (WCC) (11 July 2014)).

The decision, which criticises but ultimately follows the position expressed by the Supreme Court of Appeal in the early 1980s, makes it clear that a seller of a business should not be under the impression that the absence, or expiry, of an express contractual restraint of trade clause in the agreement means that he then has *carte blanche* to canvass and solicit the customers of the business as at the time of the sale. Even in the absence of a contractual restraint, there is an obligation (implied by law) on the seller to not deprive the purchaser of the goodwill that was sold to the purchaser.

The facts of the Grainco case resemble a common sale and transfer of business structure/scenario and are worth setting out briefly in order to appreciate the implications of the judgement. Messrs Van der Merwe and Kitshoff formed a company (Old GrainCo) which ran a grain-trading business. Old GrainCo ultimately sold the business and its goodwill to BKB Ltd (BKB). Under the sale agreement Old GrainCo, Van der Merwe and Kitshoff bound themselves for five years to not compete with BKB or to canvass any of its customers. BKB immediately on-sold the business and goodwill to the applicant GrainCo (Pty) Ltd (New GrainCo). The sale agreement included a cession of all of BKB's rights in respect of the business to New GrainCo. New GrainCo subsequently employed Van der Merwe and Kitshoff. Their employment agreements incorporated the restraints in the Old GrainCo-BKB sale agreement. More than five years

later, ie after the restraint lapsed, Van der Merwe resigned and formed Perdigon (Pty) Ltd which also ran a grain-trading business. Thereafter Kitshoff resigned from New GrainCo and Perdigon employed him. A few months on, New GrainCo applied to a high court to interdict Van der Merwe, Kitshoff and Perdigon from canvassing the customers of its business. It relied on a term the law implies into a contract to sell a business with its goodwill: that the seller may not later canvass persons who were customers of the business at the time of the sale ('the implied prohibition').

The court considered the following issues:

Could New GrainCo enforce the implied prohibition?

The court held that indeed, it could: BKB had ceded its right to enforce the prohibition to New GrainCo.

The scope of the implied prohibition

The implied prohibition applied only to the seller of the business and its goodwill. It did not prohibit the canvassing of those persons who had been customers before the sale who –

- did not intend to resume trading with the business;
- were unlikely to resume trading with the business; or
- the purchaser had chosen to stop trading with.

The court also held that the prohibition did not bar the seller from canvassing persons who became customers of the business after the sale. A person was a 'customer' if the business supplied goods or services to it for consideration. Furthermore, and importantly, the prohibition only prevented a seller from canvassing a customer — it did not prevent a seller from dealing with a customer. Thus if a seller had unlawfully canvassed a customer and had commenced

dealing with him, the purchaser's remedy would be to sue for damages for breach of the prohibition, not to interdict the seller from dealing with the customer.

The effect and implications of the express contractual restraint on the applicability of the implied common-law prohibition: are they mutually exclusive?

The court had to accept that there was Appellate Division authority that an express restraint on competition would not exclude the implied prohibition which otherwise existed at law, even where the express restraint included within its scope a prohibition against canvassing customers (*Becker & Co (Pty) Ltd v Becker and Others* 1981 (3) SA 406 (A)). The court in Grainco felt that this rule might warrant reconsideration: where a purchaser and seller agreed to an express restraint of a specified period, geographical area, etc the stronger argument is that they intended to have exhaustively regulated the protection that the purchaser would have regarding the acquired customer base.

However, on the principle of *stare decisis* (ie that courts are bound by precedents), the High Court was bound by the decision in Becker. Therefore the court concluded that the implied prohibition was not excluded from the Old GrainCo-BKB sale agreement, and that BKB ceded the right to enforce it to New GrainCo. But, very importantly, the common-law prohibition bound only the seller of the business with its goodwill, Old GrainCo, and not Van der Merwe or Kitshoff (or the vehicle that they used, Perdigon). And Van der Merwe and Kitshoff only began to compete with New GrainCo after the expiry of the express contractual restraints that bound them.

Grainco serves as a reminder that, insofar as canvassing the customer base is concerned, the seller is not necessarily 'out of the woods' as soon as, and merely because, the contractual restraint/non-solicitation clause in the sale of business agreement has expired. If the seller is desirous of canvassing the customers after the restraint expires, this must be made clear in the agreement, otherwise the common law principles around the protection of goodwill will apply. The drafting of the relevant contractual provisions in this regard becomes absolutely crucial.

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