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# CORPORATE & COMMERCIAL ALERT

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### Fraud unravels all

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## Fraud unravels all

Such clauses ordinarily survive the termination of the contract, but would they do so in the case of fraudulent misrepresentation?

**A fraudulent misrepresentation which induces a party to conclude a contract renders such a contract voidable at the instance of the aggrieved party. The aggrieved party may therefore validly terminate or rescind the contract on the basis of the fraudulent misrepresentation.**

Consider then what would happen where (i) a party concluded a contract based on the fraudulent misrepresentation of the counter-party and (ii) such a contract contained an arbitration clause regulating the settlement of disputes? Such clauses ordinarily survive the termination of the contract, but would they do so in the case of fraudulent misrepresentation?

Put differently, in light of the fraudulent and corrupt conduct of the counter-party, could the aggrieved party be compelled to submit to the arbitration process in accordance with the dispute resolution clause in the contract? This was one of the more interesting questions dealt with in the recent Supreme Court of Appeal (SCA) decision of *Namasthethu Electrical (Pty) Ltd v City of Cape Town and Another* [2020] ZASCA 74 (29 June 2020).

The facts in *Namasthethu* essentially boiled down to an attempt by Namasthethu to compel the City to submit to the arbitration process in accordance with the dispute resolution clause in the contract entered into between the two parties, despite Namasthethu having fraudulently induced the City to award it a tender and subsequently conclude the contract.

The clause regulating disputes was worded as follows:

- i. *'Should any disagreement arise between the employer or his principal agent or agents, and the contractor out of or concerning this agreement or its termination, either party may give [notice] to the other to resolve such disagreement.*
- ii. *Where such disagreement is not resolved within ten working days of receipt of such notice, it shall be deemed to be a dispute and shall be referred by the party giving such notice to either,*
  - a. *Adjudication where adjudication shall be conducted in terms of the JBCC Rules [of] Adjudication current at the time when the dispute was declared.*

Or

*b. Litigation...'*

Upon being satisfied that there had in fact been fraud on the part of Namasthethu during the procurement process, the City exercised its right to terminate the contract with immediate effect. Namasthethu disputed the City's right to termination and insisted that the dispute be adjudicated in accordance with the dispute resolution procedure provided for in the contract and argued that the dispute resolution clause was wide enough to encompass disputes of whatever nature. Namasthethu referred the matter for adjudication. The arbitrator ruled in favour of Namasthethu.

## Fraud unravels all...continued

The SCA found it untenable that an aggrieved party would be expected to give notice to cure fraud and confirmed that where a contract has been rescinded by an aggrieved party, the clause regulating disputes cannot stand, as it was embedded in a fraud-tainted agreement that had been rescinded by election.

On the facts and evidence of the case, the SCA was satisfied that all the requirements of fraudulent misrepresentation had been met. The SCA was required to determine whether the dispute resolution clause survived the termination of the contract by the City on the ground of fraudulent misrepresentations. That is, was the referral of the dispute for adjudication valid and lawful? The SCA rejected Namasthethu's averment that the dispute was required to be referred for adjudication and held that the arbitrator lacked authority to adjudicate the dispute. The SCA affirmed that –

*'No court in this land will allow a person to keep an advantage which he has obtained by fraud. No judgement of court... can be allowed to stand if it has been obtained by fraud. Fraud unravels everything.'*

The SCA found it untenable that an aggrieved party would be expected to give notice to cure fraud and confirmed that where a contract has been rescinded by

an aggrieved party, the clause regulating disputes cannot stand, as it was embedded in a fraud-tainted agreement that had been rescinded by election. The SCA confirmed that an arbitration clause could not survive in the face of allegations of fraud by one party, even where such a contract expressly included the phrase *'any question as to the enforceability of this contract'*. The SCA further confirmed that the clause regulating the settlement of disputes contemplated a dispute arising out of the agreement when it was accepted to be valid from the outset, and that the clause in no way covered fraud.

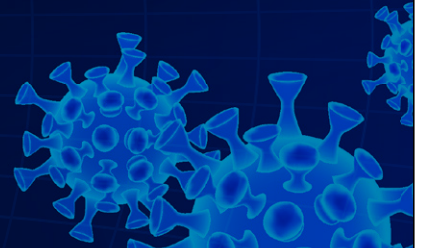
Simply put, disputes regarding the enforceability of contracts induced by fraud were not generally intended to be arbitrable. Therefore, such a clause could not survive such rescission. Any other interpretation, the SCA stated, would be *'offensive to justice'*.

*Boipelo Diale, Michaela Grieve and David Pinnock*



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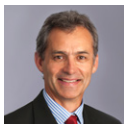
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