

Corporate & Commercial ALERT

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INCORPORATING
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IN THIS ISSUE

Disclosure vs due diligence when contracting

Every so often we are presented with case law underlining the importance of the duty to disclose and the obligation to investigate by the respective parties to a contract, and the judgment of the High Court, Gauteng Local Division in the of case *Anioma Property (Pty) v DMFT Developers and Others* 49230/2021 handed down on 7 March 2023 is a recent example.



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Background

The applicant, Anioma Property (Pty) Ltd (the seller), entered into a written sale agreement with the first respondent, DMFT Property Developers (the purchaser), and sold its immovable property for R13 million. While the purchaser paid the full purchase price into the conveyancer's trust account, it refused to pay the transfer costs for the registration as it was obliged to do under the sale agreement.

The purchaser argued that the sale agreement stood to be rescinded since the seller deliberately failed to make disclosures of material facts, notwithstanding an obligation to do so, in that it failed to make disclosure of all conditions and endorsements on the title deed or circumstances that brought them about. The title deed of the property contained a caveat preventing the issuing of a certified copy of the title deed and the subsequent transfer of the property in respect of such copy unless leave was obtained from the High Court.

According to the purchaser, the seller failed to disclose to the purchaser that the immovable property in question was under hijack and that upon learning of the caveat to the title deed and investigating it, it became aware that the immovable property was targeted by hijackers. Those hijackers would have to be warded off in court and this would delay the purchaser's plans to develop the immovable property.

The seller contended that the purchaser's averments were speculation and far-fetched, and that clause 20.1 of the sale agreement did specifically provide that "[t]he seller shall remove all caveats that may be placed on the property and facilitate the transfer process". The seller further contended that it considered the purchaser's unilateral non-compliance with the terms of the sale agreement a repudiation and therefore demanded specific performance.



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Findings

According to the court, three questions arose for determination in the matter:

1. Was the language of clause 20.1 of the sale agreement misleading and were pertinent facts omitted?
2. Was there a legal duty on the seller to disclose the exact nature of the caveat?
3. Were the non-disclosed facts material thereby invalidating the sale agreement?

In its analysis the court cited earlier rulings, summed up as follows:

- Failure to disclose a material fact to the other contracting party when there is a legal duty to do so would constitute misrepresentation.
- Non-disclosure and misrepresentation are treated in the same manner, in that they are both grounds for rescission of the agreement if one party is under a duty to disclose such facts and fails to do so.

- Unless there is a duty to speak or act, the silence or inaction cannot constitute misrepresentation.
- Examples of where a duty to speak arise are:
 - A duty to disclose a material fact arises when the fact in question falls within the exclusive knowledge of the defendant and the plaintiff relies on the frank disclosure thereof in accordance with the legal convictions of the community.
 - If the defendant has knowledge of certain unusual characteristics relating to or circumstances surrounding the transaction in question and policy considerations require that the plaintiff be apprised thereof.
 - There is a duty to make a full disclosure if a previous statement or representation of the defendant constitutes an incomplete or vague disclosure which requires it to be supplemented or elucidated.

On the present facts the court ruled that the only two grounds the purchaser could rely on in establishing that the seller had a duty to disclose the exact nature of the caveat were the *"sole knowledge"* ground and the *"omission of pertinent facts or using misleading language"* ground.

Sole knowledge

Under sole knowledge the court elaborated that a party is expected to speak when (i) the information they have to impart falls within their exclusive knowledge so that in a practical business sense the other party has them as their only source; and (ii) the information is such that the right to have it communicated would be mutually recognised by honest men in the circumstances. If the information desired is readily ascertainable it should not be categorised as exclusive knowledge. Exclusive knowledge is rather knowledge which is inaccessible to the point where its inaccessibility produces an involuntary reliance on the party possessing the information.

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The court held that because the caveat could have easily been uncovered through a simple deeds search and subsequently accessed through the Deeds Office it may not qualify as being knowledge which the seller was in the sole possession of. Furthermore, even if the information qualified as exclusive to the seller the second part of the enquiry was whether the purchaser's right to have the knowledge communicated would be mutually recognised by honest men in the circumstances, and to this end, the court held that in terms of clause 20.1 of the sale agreement the seller was bound to remove all caveats and, therefore, it would appear that disclosing all the facts surrounding the caveat was not considered necessary by the seller. Given that the property was never hijacked and all litigation regarding the alleged fraudulent liquidation of the seller was resolved, it seemed reasonable to assume that an honest man in the circumstances would not deem it necessary to disclose the

entire nature of the caveat. The court reiterated that the information in question was readily accessible had the purchaser performed his due diligence and simply conducted a deed search.

Omission or misleading language

Under the omission or misleading language ground, the court also cited earlier cases the principles of which can be summarised as follows:

- A legal duty to disclose occurs when a party has omitted pertinent facts or has used language that is misleading.
- Certain policy considerations may also necessitate the communication of certain facts or information to the other party.
- Often during the negotiation process a party may use vague, unclear or elusive language in order to secure a sale, or to ensure the conclusion of the contract. Nonetheless, a duty to disclose exists if such previously used equivocal terms require clarification.
- There may be particular circumstances, usually associated with the prior conduct of the party who remained silent, that require such party to speak, for example, where only part of the truth has been told and the omission of the remainder gives a misleading impression.
- The fact that subjectively a particular reader latches onto one meaning in an agreement which the reasonable reader would not take as the clear import of the statement is not relevant at the stage of determining whether a misrepresentation has been made.

The purchaser submitted that the language of clause 20.1 of the sale agreement caused it to draw an inference that there were, in fact, no caveats but rather, the seller simply added the clause for the sake of being thorough. The court found that this explanation did not appear plausible saying that clause 20.1 was, at best, unclear. The seller had intentionally

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penned the clause in at the end and the purchaser, as an interested party, should have questioned why this was so, regardless of the wording. The property was going to cost the purchaser a substantial amount of money and as such, required a certain amount of due diligence from the purchaser. A reasonable person in the position of the purchaser would have sought clarity on the clause to ensure that there were no issues pertaining to the title of the property and to further ensure that there were no caveats on the title. A reasonable person, with as much investment in the matter, would have certainly questioned why the seller had specifically added that particular clause into the sale agreement.

Materiality of the non-disclosed facts

The court emphasised that where there is duty to disclose certain facts, the failure to disclose these facts would still have to qualify as material in order to affect the validity of the agreement. The court gave due consideration to the relevant test, being essentially, whether the statement would have induced a

reasonable person to enter into the agreement (or, in the case of non-disclosure, whether disclosure of the relevant information would have persuaded a reasonable person not to enter into the agreement). The court made mention of the fact that the desirability of applying an objective test where the representor has been dishonest or fraudulent has been questioned, and lately it has been held that the test to be applied in such cases is subjective: namely, whether the representee actually believed the representation.

In applying the test the court concluded that it would appear unlikely that the disclosure would have persuaded a reasonable person to not enter into the sale agreement. The existence of the caveat did not affect the title deed, nor did it prevent transfer. Furthermore, the immovable property was not the subject of an attempted hijacking and was never in fact hijacked, so the consequences of buying a hijacked property would not be suffered by the purchaser. As such, it could be argued that a reasonable person in the position of

the purchaser would have proceeded with the sale. At worst, a reasonable person may have instituted a delictual claim if they believed they suffered a financial loss during the negotiation of the purchase price, however, it would appear unlikely that a reasonable person would attempt to rescind the sale agreement entirely. Accordingly, the court ruled in favour of the seller and the sale agreement was upheld.

Insight

As mentioned at the outset, the judgment certainly highlights the importance of the duty on the part of a seller to disclose and the obligation on the part of a purchaser to investigate. For example, in a sale and purchase agreement, a seller must ensure that representations or statements that are made are clear and do not give a misleading impression, otherwise there would be a duty on the seller to elucidate or supplement any incomplete, elusive or misleading statements that qualify as material, meaning the statements in question would have induced a sale.

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Similarly, a seller must ensure that where certain facts are not disclosed those facts do not qualify as (i) facts which fall within the exclusive knowledge of the seller and the right to have those facts communicated would be mutually recognised by honest men in the circumstances; or (ii) facts which contain certain unusual characteristics relating to or circumstances surrounding the transaction in question and policy considerations require that they be disclosed. If the facts fall under (i) or (ii) and they qualify as material, meaning had they been disclosed they would have induced a retraction of the entering into the sale then there would be a duty on the seller

to disclose those facts. In essence a seller has to maintain a careful balance between neither disclosing more nor less than what is required.

These considerations come alive for a seller during due diligence investigations and disclosures made by the seller during the process, and related warranties and disclosures recorded in the sale agreement itself, and a seller should seek competent advice when assessing what to disclose and what not to disclose.

On the other hand, a purchaser should ensure that the information received from a seller is adequately investigated. If the information is unclear or a purchaser is doubtful as

to the meaning of certain statements then the purchaser is advised to seek further clarity. It would be prudent for a purchaser to satisfy themselves by conducting a reasonable due diligence and verifying the accuracy of the information received with the assistance of trusted advisors, which exercise would also go a long way in assisting the purchaser with evaluating the risk associated with the planned purchase and assessing the reasonableness of the price to be paid.

**Zakiya Shaik and
Tessmerica Moodley**

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2022

1st by M&A Listed Deal Flow.
3rd by M&A Listed Deal Value,
M&A Unlisted Deal Value,
M&A Unlisted Deal Flow
and General Corporate
Finance Deal Value.

2021

1st by M&A Deal Flow.
2nd by General Corporate
Finance Deal Flow.
2nd by BEE Deal Value.
3rd by General Corporate
Finance Deal Flow.
3rd by BEE Deal Flow.
4th by M&A Deal Value.

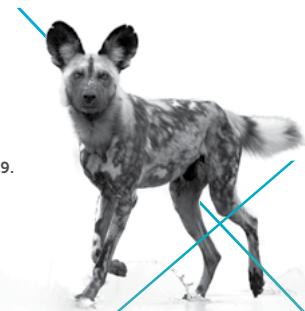
2020

1st by M&A Deal Flow.
1st by BEE Deal Flow.
1st by BEE Deal Value.
2nd by General Corporate Finance Deal Flow.
2nd by General Corporate Finance Deal Value.
3rd by M&A Deal Value.
Catalyst Private Equity Deal of the Year.

DealMakers

2019

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Decade by Deal Flow: 2010-2019.**
1st by BEE M&A Deal Flow.
1st by General Corporate
Finance Deal Flow.
2nd by M&A Deal Value.
2nd by M&A Deal Flow.



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Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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