

Corporate & Commercial ALERT

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CLIFFE DEKKER HOFMEYR

INCORPORATING
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IN THIS ISSUE

Surfing the waves of contractual interpretation

The case of *Yacht Hardware CC v Zenith International Proprietary Limited* [2022] JDR 3693 (WCC) is a recent appeal heard by the Western Cape High Court involving the interpretation of indemnity clauses in a contract of sale between Yacht Hardware CC t/a Harken South Africa (plaintiff), a manufacturer and distributor of marine products, and Zenith International Proprietary Limited (defendant). For ease of reference the parties in this appeal were referred to as in the court of first instance.



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Surfing the waves of contractual interpretation

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In summary, the High Court reiterated the judicial stance on contractual interpretation: that the inevitable point of departure (in interpreting a contract) is the language of the contract itself. This article highlights the court's approach to contractual interpretation and how parties to contractual negotiations should approach drafting and concluding agreements with this in mind.

Key takeaways

- The wording of the contract is the agreement between the parties. Words must be given their ordinary grammatical meaning, unless to do so would result in absurdity.
- To avoid lengthy and costly (and unnecessary) litigation, the parties' intention must be clarified to ensure that it is reflected in the contract during the negotiation phase. Identifying and resolving

varying interpretations should be dealt with as the contract is drafted and before it is signed. In accordance with the *parol evidence* rule, the courts will not allow extrinsic evidence that contradicts or creates a variation of a term in writing that the parties intended to be completely integrated.

- In interpreting contracts, the courts strive to uphold the principle of *pacta sunt servanda*, which means that agreements must be kept.

Background

The parties entered into a sale agreement in 2019, in terms of which the plaintiff (as seller) sold assets and stock comprising its business to the defendant (as purchaser).



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Surfing the waves of contractual interpretation

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The agreement contained two indemnity clauses:

- Clause 9.1, the **first indemnity clause**, was an indemnity by the plaintiff in favour of the defendant for any liability or obligation of the plaintiff *"which arose prior to the effective date, it being specifically recorded and agreed that the purchaser does not assume any of the seller's liabilities incurred as at or prior to the effective date"*.
- Clause 9.2, the **second indemnity clause**, was an indemnity by the defendant in favour of the plaintiff stating that, *"in light of the fact that the purchaser is not taking on the employees of the seller, the purchaser indemnifies the seller against any claims brought by employees for compensation of whatsoever nature due to the termination"*.

After the contract was signed, but before the *"effective date"* of the contract, two employees of the plaintiff were dismissed. The (former) employees referred the disputes to the Commission for Conciliation, Mediation and Arbitration (CCMA) against the plaintiff. During conciliation at the CCMA, the plaintiff and the disgruntled employees reached a settlement in respect of their claims and the plaintiff, in terms of this settlement, paid these employees R324,010 (in aggregate).

The plaintiff proceeded, under the second indemnity clause, to claim these amounts from the defendant. The defendant denied liability and the plaintiff instituted action in the court *a quo*. The court of first instance dismissed the plaintiff's claim after allowing and considering extensive evidence regarding the intentions of the parties when entering into the agreement. It is against this decision that the plaintiff appealed.

Findings

De Wet AJ (with Erasmus J concurring) penned the court's judgment, which upheld the plaintiff's appeal. The court held that the case hinged upon whether the first indemnity clause or the second indemnity clause was applicable to the plaintiff's claim and confirmed that the correct *"vantage point"* to start interpreting a contract is one located in the text of what the parties in fact agreed.

Using this approach, the court considered the first indemnity clause and second indemnity clause. It held that the first indemnity clause deals with an indemnity by the plaintiff in favour of the defendant for any general claims pertaining to loss, liability, damage, costs or expenses without prejudice to any rights of the plaintiff in terms of the agreement, whilst the second indemnity clause deals with an indemnity by the defendant in favour of the plaintiff against any claims brought by

Surfing the waves of contractual interpretation

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employees due to the termination of the business and “*in light of the purchaser not taking on the employees of the seller*”. The court, in contemplating the language of the first indemnity clause and second indemnity clause, held that it was clear that the employees’ claims fell within the ambit of the second indemnity clause, as the claims were brought by the employees as a result of them losing their employment due to the termination of the business and the fact that the defendant did not want to take over their employment contracts.

The payments made by the plaintiff for the employees’ claims were payments regulated by the (properly interpreted) second indemnity clause,

which payments were covered by the indemnity provided by the defendant in favour of the plaintiff. The court noted that the second indemnity clause contained no ambiguity and if the correct approach was adopted by the court *a quo*, from the outset, the costs and legal resources employed in determining this relatively small claim would not have resulted.

Having regard to the above, the court ordered the defendant to reimburse the plaintiff the amount it paid in settlement of the employee claims.

Conclusion

The contextual approach to contractual interpretation is mostly settled, and the inevitable point of departure is the language of the

provision itself. Wording in contracts must be clear and certain, and, in the event of a dispute, a court will not “*veer down a slippery slide*” of determining what the parties’ opinions were pertaining to the meaning of the clauses: the court will look at the wording itself.

It is therefore imperative that parties and their advisers ensure that the contractual parties’ intentions are reflected in the wording of the contract, and that it is drafted in clear, concise and unambiguous language.

Jaco Meyer and Menachem Gudelsky

CONSISTENTLY SUCCESSFUL

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
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2nd by M&A Deal Value.
2nd by M&A Deal Flow.



OUR TEAM

For more information about our Corporate & Commercial practice and services in South Africa and Kenya, please contact:



Willem Jacobs

Practice Head & Director:
Corporate & Commercial
T +27 (0)11 562 1555
M +27 (0)83 326 8971
E willem.jacobs@cdhlegal.com



David Thompson

Deputy Practice Head & Director:
Corporate & Commercial
T +27 (0)21 481 6335
M +27 (0)82 882 5655
E david.thompson@cdhlegal.com



Sammy Ndolo

Managing Partner | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E sammy.ndolo@cdhlegal.com

Tessa Brewis

Director:
Corporate & Commercial
T +27 (0)21 481 6324
M +27 (0)83 717 9360
E tessa.brewis@cdhlegal.com

Vivien Chaplin

Director:
Corporate & Commercial
T +27 (0)11 562 1556
M +27 (0)82 411 1305
E vivien.chaplin@cdhlegal.com

Clem Daniel

Director:
Corporate & Commercial
T +27 (0)11 562 1073
M +27 (0)82 418 5924
E clem.daniel@cdhlegal.com

Dane Kruger

Director:
Corporate & Commercial
T +27 (0)21 481 6362
M +27 (0)74 914 1402
E dane.kruger@cdhlegal.com

André de Lange

Sector Head: Agriculture, Aquaculture
& Fishing Sector
Director: Corporate & Commercial
T +27 (0)21 405 6165
M +27 (0)82 781 5858
E andre.delange@cdhlegal.com

Andrew Giliam

Director:
Corporate & Commercial
T +27 (0)21 481 6363
M +27 (0)83 359 7069
E andrew.giliam@cdhlegal.com

John Gillmer

Joint Sector Head: Private Equity
Director: Corporate & Commercial
T +27 (0)21 405 6004
M +27 (0)82 330 4902
E john.gillmer@cdhlegal.com

Allan Hannie

Director:
Corporate & Commercial
T +27 (0)21 405 6010
E allan.hannie@cdhlegal.com

Ian Hayes

Director:
Corporate & Commercial
T +27 (0)11 562 1593
M +27 (0)83 326 4826
E ian.hayes@cdhlegal.com

Peter Hesselning

Director:
Corporate & Commercial
T +27 (0)21 405 6009
M +27 (0)82 883 3131
E peter.hesselning@cdhlegal.com

Quintin Honey

Director:
Corporate & Commercial
T +27 (0)11 562 1166
M +27 (0)83 652 0151
E quintin.honey@cdhlegal.com

Brian Jennings

Director:
Corporate & Commercial
T +27 (0)11 562 1866
M +27 (0)82 787 9497
E brian.jennings@cdhlegal.com

Rachel Kelly

Director:
Corporate & Commercial
T +27 (0)11 562 1165
M +27 (0)82 788 0367
E rachel.kelly@cdhlegal.com

Yaniv Kleitman

Director:
Corporate & Commercial
T +27 (0)11 562 1219
M +27 (0)72 279 1260
E yaniv.kleitman@cdhlegal.com

Justine Krige

Director:
Corporate & Commercial
T +27 (0)21 481 6379
M +27 (0)82 479 8552
E justine.krige@cdhlegal.com

Jaco Meyer

Director:
Corporate & Commercial
T +27 (0)11 562 1749
M +27 (0)83 477 8352
E jaco.meyer@cdhlegal.com

OUR TEAM

For more information about our Corporate & Commercial practice and services in South Africa and Kenya, please contact:

William Midgley

Sector Head: Commercial Real Estate
Director: Corporate & Commercial
T +27 (0)11 562 1390
M +27 (0)82 904 1772
E william.midgley@cdhlegal.com

Tessmerica Moodley

Director:
Corporate & Commercial
T +27 (0)21 481 6397
M +27 (0)73 401 2488
E tessmerica.moodley@cdhlegal.com

Anita Moolman

Director:
Corporate & Commercial
T +27 (0)11 562 1376
M +27 (0)72 252 1079
E anita.moolman@cdhlegal.com

Wayne Murray

Director:
Corporate & Commercial
T +27 (0)21 405 6018
M +27 (0)79 691 0137
E wayne.murray@cdhlegal.com

Francis Newham

Executive Consultant:
Corporate & Commercial
T +27 (0)21 481 6326
M +27 (0)82 458 7728
E francis.newham@cdhlegal.com

David Pinnock

Joint Sector Head: Private Equity
Director: Corporate & Commercial
T +27 (0)11 562 1400
M +27 (0)83 675 2110
E david.pinnock@cdhlegal.com

Allan Reid

Joint Sector Head: Mining & Minerals
Director: Corporate & Commercial
T +27 (0)11 562 1222
M +27 (0)82 854 9687
E allan.reid@cdhlegal.com

Jess Reid

Director:
Corporate & Commercial
T +27 (0)11 562 1128
M +27 (0)83 571 6987
E jess.reid@cdhlegal.com

Megan Rodgers

Sector Head: Oil & Gas
Director: Corporate & Commercial
T +27 (0)21 481 6429
M +27 (0)79 877 8870
E megan.rodgers@cdhlegal.com

Ludwig Smith

Director:
Corporate & Commercial
T +27 (0)11 562 1500
M +27 (0)79 877 2891
E ludwig.smith@cdhlegal.com

Tamarin Tosen

Director:
Corporate & Commercial
T +27 (0)11 562 1310
M +27 (0)72 026 3806
E tamarin.tosen@cdhlegal.com

Roxanna Valayathum

Director:
Corporate & Commercial
T +27 (0)11 562 1122
M +27 (0)72 464 0515
E roxanna.valayathum@cdhlegal.com

Roux van der Merwe

Director:
Corporate & Commercial
T +27 (0)11 562 1199
M +27 (0)82 559 6406
E roux.vandermerwe@cdhlegal.com

Andrew van Niekerk

Head: Projects & Infrastructure
Director: Corporate & Commercial
T +27 (0)21 481 6491
M +27 (0)76 371 3462
E andrew.vanniekerk@cdhlegal.com

Charl Williams

Director:
Corporate & Commercial
T +27 (0)21 405 6037
M +27 (0)82 829 4175
E charl.williams@cdhlegal.com

Njeri Wagacha

Partner | Kenya
T +254 731 086 649
+254 204 409 918
+254 710 560 114
E njeri.wagacha@cdhlegal.com

Christelle Wood

Director:
Corporate & Commercial
T +27 (0)11 562 1372
M +27 (0)83 498 2850
E christelle.wood@cdhlegal.com

Emma Hewitt

Practice Development Director:
Corporate & Commercial
T +27 (0)11 562 1635
E emma.hewitt@cdhlegal.com



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JOHANNESBURG

1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa.
Dx 154 Randburg and Dx 42 Johannesburg.
T +27 (0)11 562 1000 F +27 (0)11 562 1111 E jhb@cdhlegal.com

CAPE TOWN

11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.
T +27 (0)21 481 6300 F +27 (0)21 481 6388 E ctn@cdhlegal.com

NAIROBI

Merchant Square, 3rd floor, Block D, Riverside Drive, Nairobi, Kenya. P.O. Box 22602-00505, Nairobi, Kenya.
T +254 731 086 649 | +254 204 409 918 | +254 710 560 114
E cdhkenya@cdhlegal.com

STELLENBOSCH

14 Louw Street, Stellenbosch Central, Stellenbosch, 7600.
T +27 (0)21 481 6400 E cdhstellenbosch@cdhlegal.com

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