The *pactum de non cedendo*: A re-evaluation

By

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A thesis submitted in partial fulfilment of the requirements for the degree of Magister Legum in the Department of Private Law, University of the Western Cape.

September 2009

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KEYWORDS

Contract

Cession

Pactum de non cedendo

Prohibition on transfer

Non-assignment

Anti-assignment

Validity

Effect

Commercial transactions

Factoring

ABSTRACT

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Plenty has been written on this topic, but with changing times, much of what has been written is outdated. Not necessarily outdated in the sense that recent case law or legislation has not been considered, but outdated in that some of the ideas expressed do not foster commercial growth and development, nor consider international trends.

Since the *pactum de non cedendo* is prohibitory by its nature and operation, our law should have proceeded with caution when determining its effect. This, unfortunately, is not what transpired in the *locus classicus* decision. Nor did subsequent cases correct this fatal *ratio*.

The distressing truth is that the old authorities, upon whom the *locus classicus* judgment is based, were in all probability not writing about *pacta de non cedendo*. Strangely enough, when this was suggested by an academic in the field, it elicited no response.

The lack of response evidences a lack of interest in the topic in general, partly due to the uncertain state of affairs in which the *pactum de non cedendo* operates, and partly due to the courts' unwillingness to rectify the situation.

Despite the waning interest, the *pactum de non cedendo* is prevalent and appears in many types of contracts, most recently in the powerhouse factoring industry, and cannot simply be swept under the rug.

This dissertation breathes new life into the *pactum de non cedendo* and discusses its validity and effect from a fresh perspective: A commercial perspective with a strong influence from American law.

Hopefully this re-evaluation of the *pactum de non cedendo* will re-capture the attention of academics and judges alike, so that those in the position to do so, will re-consider its validity and effect.

September 2009

OPSOMMING

The *pactum de non cedendo*: A re-evaluation

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Die onderwerp het in die verlede menige artikels ontlok, maar met die veranderende tye is baie wat geskryf is, verouderd: nie noodwendig verouderd in die opsig dat onlangse gewysdes of wetgewing nie oorweeg is nie, maar verouderd in dié opsig dat sommige van die idees wat uigespreek is nie alleen nalaat om kommersiële groei te kweek nie, maar ook nie daarin slaag om internasionale neigings na behore in ag neem nie.

Aangesien die *pactum de non cedendo* vanweë sy aard en werking verbiedend is, behoort ons reg die gevolge daarvan met omsigtigheid te benader. Ongelukkig is dit nie wat gebeur het in die *locus classicus* uitspraak nie en die daaropvolgende sake het ook nie juis daarin geslaag om hierdie gebrekkige *ratio* reg te stel nie.

Die hinderlike waarheid is dat die ou gesag waarop die *locus classicus* uispraak gegrond is, bes moontlik nie oor *pacta de non cedendo* gehandel het nie. Dit is dus vreemd dat toe hierdie toedrag van sake deur ‘n vooraanstaande skrywer op dié gebied aan die lig gebring was, dit geen reaksie uitgelok het nie.

Die gebrek aan reaksie slaan duidelik op ‘n gebrek aan belangstelling in die onderwerp in die algemeen. Hierdie stand van sake is deels toe te skryf aan die onsekerhede waaronder die *pactum de non cedendo* aanwending vind en deels aan die howe se onwilligheid om die situasie te beredder.

Ten spyte van die kwynende belangstelling kom die *pactum de non cedendo* dikwels voor in ‘n verskeidenheid van ooreenkomste, meer onlangs in die groeiende faktoreringsindustrie, en kan gevolglik nie sonder meer ignoreer word nie.

Hierdie verhandeling dien as ‘n vernuwingskuur vir die *pactum de non cedendo* en kyk na die geldigheid en uitwerking daarvan vanuit ‘n vars oogpunt: ‘n kommersiële perspektief met ‘n sterk Amerikaanse inslag.

Hopelik sal dié herbeoordeling van die *pactum de non cedendo* dien om die aandag van beide akademiese skrywers en regters te trek om sodoende die geldigheid en uitwerking daarvan van voor af onder die soeklig te plaas.

September 2009

DECLARATION

I declare that *The* pactum de non cedendo*: A re-evaluation* is my own work, that it has not been submitted for any degree or examination in any other university, and that all the sources I have used or quoted have been indicated and acknowledged by complete references.

Signed: ……..

Kelly Dawn Sunkel

September 2009

ACKNOWLEDGEMENTS

I would like to extend my sincere appreciation to my supervisor, Professor Catherine Maxwell, for her many hours spent meticulously critiquing my thesis.

To my co-supervisor, Advocate Fourie Kotze, my profuse thanks must be noted for all his encouragement and for his constant challenging of my ideas throughout the research and writing process. Thank you also, for labouriously helping me with Afrikaans translations. I will be forever grateful.

My final thank you is to Professor Solly Leeman for proofreading my thesis.

CONTENTS

INTRODUCTION

In order to fully appreciate the discussions of *pacta de non cedendo* which are to follow, the need for a thorough understanding of the law of cession as a whole cannot be over-emphasised.

Different kinds of rights are transferred in different ways. Real rights, for example, where the object of the right is corporeal property, are transferred by delivery if the corporeal property is movable, or registration if the corporeal property is immovable. With personal rights, where the object is the right to claim performance,[1] transfer takes place by way of cession.[2]

Cession can thus be defined as:

> …[A] bilateral juristic act whereby a right is transferred by mere agreement between the transferor, termed a cedent and the transferee, termed a cessionary.[3]

After a cession has taken place, the cedent becomes the 'old' creditor and the cessionary becomes the 'new' creditor in his stead. Where the debtor had to perform to the cedent before the cession, he now has to perform to the cessionary after the cession.[4]

Cession fulfils a very useful and convenient commercial function:

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[1] This performance is claimed from a party called the debtor and it is owed to a party called the creditor. The performance may be positive or negative. See PM Nienaber 'Cession' in *LAWSA* 2ed vol 2 (2003) para 4.

[2] Nienaber op cit para 2-4.

[3] Nienaber op cit para 1.

[4] S Scott *The Law of Cession* 2ed (1991) 12; Nienaber op cit para 4; S Van der Merwe Van Huyssteen, MFB Reinecke and GF Lubbe *Contract General Principles* 2ed (2003) 420.

> It facilitates commerce by enabling a creditor to turn his rights to account by selling them instead of enforcing them himself, it avoids circuity of actions and it has a number of other practical uses. [5]

It must be pointed out at the outset that cession is a method of transfer and, although it is brought about by agreement, it is not itself a contract.[6]

The agreement which brings about a cession is called an 'obligationary agreement'. It obliges the cedent to transfer the right, or put differently, it is the agreement whereby the cedent undertakes to cede the right, and constitutes the underlying *causa* or reason for the cession.[7] The obligationary agreement can manifest itself in a number of ways, it may be, for example, a contract of sale, donation, lease or security.[8]

The agreement which constitutes the actual transfer of the personal right is the cession itself and is known as the 'real agreement' or the 'transfer agreement'.[9] Although they are two separate acts with different functions, the obligationary agreement and the transfer agreement often occur simultaneously in one transaction.[10] This is probably why a cession is often mistaken for a contract.

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[5] RH Christie *The Law of Contract in South Africa* 5ed (2006) 464.

[6] Scott op cit 7-8; Van der Merwe et al op cit 422.

[7] *Botha v Fick* 1995 (2) SA 750 (A); Scott op cit 8-9, 60, 79 *et seq*; Nienaber op cit para 8-9 and para 28; Van der Merwe et al op cit 423. Were it not for the obligationary agreement, cession would take place in a vacuum. The obligationary agreement, however, does not effect an actual transfer.

[8] The obligationary contract may even arise *ex lege*. Nienaber op cit para 28; Van der Merwe et al op cit 423-424.

[9] *Botha v Fick* supra; Scott op cit 9, note Scott's reservation when using the term 'real agreement' in connection with personal rights; Nienaber op cit para 8; Van der Merwe et al op cit 428.

[10] *Botha v Fick* supra; Scott op cit 61; Nienaber op cit para 8; Van der Merwe et al op cit 423.

The only substantive requirement for a valid cession is a duly constituted agreement either orally and informally or in writing, but in a manner that indicates that the parties are *ad idem*.[11]

The consequences of a cession are broadly twofold:

First, because cession is a mode of transfer, the personal right will consequently vest in the estate of the cessionary. Unless the cession is one *in securitatem debiti*, it brings about complete transfer of the right and the cedent will be wholly divested thereof.[12] This necessarily means that the cessionary is the only person who may administer the right or enforce it.[13]

Secondly, in accordance with the *nemo plus iuris* rule,[14] the cessionary only steps into the shoes of the cedent and cannot be in a better or weaker position than that in which the cedent was.[15] Consequently, the right is transferred with all its attributes, be they benefits and privileges or defects and disadvantages.[16]

The free transferability of personal rights may be subjected to certain prohibitions. Cession may be prohibited by statute; for instance s37A of the Pension Funds Act[17] prohibits the cession of a pensioner's right to his or her pension.[18]

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[11] Nienaber op cit para 25: '…a mere loose understanding will not do'. Van der Merwe et al op cit 430.

[12] Nienaber op cit para 45; Van der Merwe et al op cit 459.

[13] *Paiges v Van Ryn Gold Mine Estates Ltd* 1920 AD 600 608; Nienaber op cit para 45-46; Van der Merwe et al op cit 459-460.

[14] *Nemo plus iuris ad alium transferre potest quam ipse haberet.*

[15] *Paiges* supra 616; Scott op cit 221; Nienaber op cit para 44; Van der Merwe et al op cit 460-461.

[16] Scott op cit 221-224; Nienaber op cit para 49-50.

[17] Act 24 of 1956 as amended as well as s2(1) of the Statutory Pensions Protection Act 21 of 1962.

[18] Nienaber op cit para 35.

Prohibitions may also stem from the common law, either generally where a cession is against public policy, or specifically, for example, where ceding the right to maintenance is prohibited.[19]

Cession may also be prohibited through agreement by the parties themselves, the so-called *pactum de non cedendo*. Such a prohibition on cession is the focus of this dissertation.

It is usually the debtor who would insist on a *pactum de non cedendo*. One is hard pressed to think of an instance where a creditor would suggest or insist that the parties should agree to place a restriction on the disposal of his rights.

There are various reasons why a debtor may insist on a *pactum de non cedendo*:

a) he fears double payment of the debt (if notice is missed);
b) he may be prevented from using set-off against the creditor;
c) he is familiar with the creditor;
d) he is of the belief that the creditor may be more willing to grant time extensions;
e) he is of the belief that the creditor may be more willing to overlook some indebtedness;
f) a change in creditor may be generally inconvenient.

The current approach in South African law, based on the leading case, *Paiges v Van Ryn Gold Mine Estates Ltd*,[20] is that the debtor has to show that he has an interest in the prohibition. If he can do this, then the *pactum de non cedendo* is valid and binding. The personal right is accordingly rendered non-transferable and a cession in contravention of

[19] Nienaber op cit para 36.

[20] Supra.

the *pactum de non cedendo* is void.[21] If the debtor cannot show that he has an interest in the *pactum de non cedendo*, then the cedent may validly cede the personal right.

A *pactum de non cedendo*, although only a brick in the vast wall called the law of cession, may present itself more often than one may realise.[22] It appears not only in general contracts, but in specific areas of application, for example, in the law of insolvency, company law, law of negotiable instruments, law of insurance and book debts (factoring).

It has been aptly said that cession 'straddles the law of property and the law of obligations'.[23] The legal relationship between the creditor and the debtor in terms of which the debtor has a legal obligation to render performance and the creditor has a right to receive performance falls under the law of obligations.[24] The right to receive performance, on the other hand, is also an asset in the creditor's estate which he can transfer should he wish to do so. The transferring of assets thus also falls under the law of things or the law of property.[25]

This dual nature has unfortunately caused numerous uncertainties in many areas of the law of cession and the *pactum de non cedendo* is no exception.

At times when the application of the *pacta de non cedendo* principles causes difficulties or problems, the proposed theoretical solution can have either a law of property or a law of obligations jurisprudential basis. In a

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[21] Scott op cit 206; Nienaber op cit para 37; Van der Merwe et al op cit 443-444. The purported cessionary would probably have an action for damages against the 'cedent' for breach of contract.

[22] It seems that contractants or their legal representatives include clauses prohibiting cession as a matter of standard practice and as a 'catch-all' net, without fully understanding their purpose and function.

[23] Nienaber op cit para 9.

[24] Scott op cit 4-5.

[25] Scott op cit 5.

particular instance a law of property solution may be preferred, in another instance a law of obligations solution may be preferred. The outcome is that *pacta de non cedendo* are not governed by a single approach, but are instead governed by a kind of mixed approach.[26]

The dual nature of *pacta de non cedendo* is the root of other problems, *viz*, academics' blatant dissatisfaction with the *locus classicus*, *Paiges v Van Ryn Gold Mine Estates Ltd*,[27] which, as mentioned above, laid down the rules regarding the validity and effect of *pacta de non cedendo*.

The feud between academics and our courts regarding how one should deal with a *pactum de non cedendo* has been rather fiery. The leading case has set a precedent that has been passionately criticised by academics, yet subsequent cases pay little or no attention to the academic outcry, except for one case: *Trust Bank of Africa Ltd v Standard Bank of South Africa Ltd*.[28] This case, however, itself attracts debate as to whether it has actually departed from the *dictum* in *Paiges* or not.

The reason why no court has clearly adopted a different approach is probably because the criticisms by academics are so varied in nature.

The most striking criticism is that the foundation upon which the approach in *Paiges* was developed is based on a misunderstanding of the texts of the old authorities who wrote on the issue, Sande and Voet. If this submission is indeed correct, it raises the question whether everything that has developed from the incorrect interpretation adopted in *Paiges* is also incorrect?

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[26] This mixed approach is a recipe for confusion and uncertainty. Either a law of property approach or a law of obligations approach should be preferred and applied consistently. Each will have its own advantages and disadvantages – the ultimate question being which is the lessor evil.

[27] Supra. See Scott op cit 205 *et seq*; Nienaber op cit para 37; Van der Merwe et al op cit 443 *et seq*. See Chapter 4 for a further discussion.

[28] 1968 (3) SA 166 (A).

If so, which academic's submissions should be followed? Perhaps none of them.

The practical result is that commercial transactions are hindered and can result in litigation, with each party having sufficient literature on the issue to substantiate his case, as so many contradictory opinions exist. Consequently, the courts usually cannot (or refuse to) decide which academic to follow and fall back on the approach of the Appellate Division in *Paiges*.

This happens despite the fact that the case was decided in 1920 and might be in need of modernisation; despite the fact that the academics vehemently disagree with this decision; and despite the fact that there is a persuasive suggestion that the leading case was based on an incorrect interpretation of Sande and Voet.

The law governing *pacta de non cedendo* is convoluted and out of touch with modern trends, and this research is well overdue. In an endeavour to clarify the specific uncertainties that arise surrounding the *pactum de non cedendo*, inspiration will be sought from American law to give *pacta de non cedendo*, as a whole, a fresh perspective.

CHAPTER ONE

HISTORICAL DEVELOPMENT

The Appellate Division in the *locus classicus* on *pacta de non cedendo*, *Paiges v Van Ryn Gold Mine Estates Ltd*,[29] relies on the writings of Sande and Voet as authority for the *ratio* as laid down in that case. This *ratio* has ever since been dutifully followed in numerous other cases, as well as confirmed by academics.[30]

What follows is a brief history and discussion of the specific texts relied on by the court in *Paiges*. It must, however, be understood from the outset that in their writings Johannes à Sande and Johannes Voet were in all likelihood not referring to *pacta de non cedendo*, but rather *pacta de non aliendo*.[31] The following discussion nevertheless proceeds on the presumption that the Appellate Division's reliance on these texts was correct and critique on the issue has been reserved for Chapter 4.[32]

1.1 Roman Law

The modern concept of cession was not known in Roman law and consequently the *pactum de non cedendo* was nowhere to be found during this time in history.

The transfer of a personal right was not recognised as Roman lawyers considered an obligation as something highly personal.[33] In fact, Roman lawyers adhered to the maxim '*nomina ossibus inhaerent*':

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[29] 1920 AD 600.

[30] Except for one academic, but see Chapter 4 for a detailed discussion.

[31] That is, not the prohibition on transfer of ownership in incorporeal property, like personal rights, but rather the prohibition on transfer of ownership in corporeal property, like land.

[32] Although the issue is also touched on in Chapter 3.

[33] R Zimmermann *The Law of Obligations: Roman Foundation of the Civilian Tradition* 2ed (1995) 58.

> [T]he action arising from an obligation hinges on the bones and entrails of the creditor and can be no more separated from his person than the soul from the body.[34]

There was, however, a practical need for cession, so Roman lawyers achieved a similar result by using two other legal institutions: *novatio* and *procuratio in rem suam*.

The transfer of a personal right by way of *novatio* is quite different from a transfer by way of cession. *Novatio* brought about a cancellation of the existing obligation between the debtor and the original creditor and replaced it with a fresh contract between the debtor and a new creditor (the 'cessionary') having exactly the same content.[35]

The 'cessionary' was not in a secure position as the substituted agreement required the consent and co-operation of the debtor for the transfer to function in favour of the 'cessionary'.[36]

The transfer of a personal right by way of *procuratio in rem suam* was more complex and even riskier. In reality the original creditor would take on the role of principal and commission (through mandate) the new creditor to sue the debtor on his behalf as his agent. Agency, however, was not recognised in Roman law so, although in reality the personal right was being transferred by agency, the façade of *procurator in rem suam* (agent in his own name) allowed the *procurator* or new creditor to sue the debtor in his own name and to retain whatever he recovered from the debtor.[37]

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[34] Ibid.

[35] PC Anders *Commentary on Cession of Actions by Johannes à Sande* (1906) 1 (hereinafter referred to as '*Cession of Actions'*); Zimmermann op cit 60.

[36] Ibid.

[37] Anders op cit 2.

Although the consent and co-operation of the debtor was not required, the 'cessionary' was therefore in no better a position than a transfer through *novatio* as he was merely a procedural representative of the original creditor in the suit against the debtor and the personal right still belonged to the original creditor.[38] As a result, the original creditor could frustrate the arrangement by suing the debtor himself or accepting his performance, or alternatively by releasing the debtor from the obligation.[39] The situation could also be upset by the death of the original creditor, or by his revoking his commission (*mandatum*).[40]

These two legal institutions clearly had their own shortcomings as the 'cessionary' and sometimes the debtor were very often left in precarious and unsatisfactory positions.[41]

In response to this, Roman law developed an action, the *actio utilis*, to provide the *procurator in rem suam* with some relief. This relief came in the form of the *procurator* no longer suing in his own name, but in his own right and this right could no longer be frustrated by revocation or death.[42] Effectively, the object of a transfer by way of *procurator in rem suam* was not a personal right, but an action, the *actio utilis*.

Unfortunately the *actio utilis* was not nearly a solution to the plight of the *procurator* as it did not actually transfer the original creditor's claim. The original creditor still retained the *actio directa* as this action was too personal to transfer. As a result, the creditor could still frustrate the situation, for example, by accepting performance from the debtor.[43]

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[38] Zimmermann op cit 61; Anders op cit 3.

[39] Zimmermann op cit 61.

[40] Anders op cit 3.

[41] Zimmermann op cit 60-62.

[42] Zimmermann op cit 62.

[43] Zimmermann op cit 62; S Scott *The Law of Cession* 2ed (1991) 12.

1.2 Roman-Dutch law

Due to the unsatisfactory state of affairs in Roman law, the position changed dramatically in Roman-Dutch law, as jurists began to view personal rights more from the law of property perspective and less from the perspective of the law of obligations.[44]

This shift in perspective allowed the Roman-Dutch jurists to move away from the idea that personal rights are too personal to transfer, and to consider a personal right as an incorporeal asset in the estate of the owner[45] of the right, who may transfer it should he wish to do so.[46]
The change was prompted by jurists like Vinnius[47] who accepted that a cession was the transfer of a right of action by agreement and if the 'cessionary' was appointed *procurator in rem suam*, the agreement transferred the *actio utilis* in such a way that he (the 'cessionary') was also entitled to use the *actio directa*, an action formally reserved for the 'cedent'.[48]

Vinnius, however, cannot be regarded as the 'father' of cession as he was not prepared to acknowledge an immediate and complete transfer by the agreement.[49]

The next step in the development of a complete transfer of a right by agreement was taken by Sande, a well-respected jurist, who published *De Cessione Actionum* in 1623 and *De Prohibita Rerum Alienatione* in 1633, and Voet who published *Commentarius ad Pandectas* in 1698.

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[44] As can be seen from the development of cession. Jurists thus began to see personal rights as a form of property.

[45] I use the word 'owner' as opposed to 'holder' as the holder of a right may not necessarily be the owner thereof.

[46] Scott op cit 3 footnote 9.

[47] *Jurisprudentiae Contractae Sive Partitionum Juris Civilis Libri* (1624).

[48] *LTA Engineering CO Ltd v Seacat Investments (Pty) Ltd* 1974 (2) All SA 6 (A) 10. See also *Johnson v Incorporated General Insurance Ltd* 1983 (1) SA 318 (A) 331C.

[49] *LTA Engineering CO v Seacat Investments* supra 11.

Sande wrote: [50]

> As a rule every action, real as well as personal, is competent to be ceded.[51] (Anders' translation)
>
> Even an action once ceded may again be ceded by the cessionary thereof, for since the ceded action vests in the cessionary, there is no doubt but he can transfer the same in turn to another person. [52] (Anders' translation)

Voet wrote: [53]

> In modern law naked agreements seriously made give rise to actions without qualification. But if these distinctions as to agreements giving or not giving shape to an action were not entirely necessary to a true understanding of Roman law, and to an explanation of enactments which without such prior knowledge are partly obscure and partly savouring of injustice, they could surely have been left wrapped in silence for all the use they have in court practice. I say this because nowadays it is quite trite and universally admitted that an action arises from naked agreements entered into with a grave and determined mind just as much as from contracts. Much more so if they have been annexed to the contracts whether *bonae fidei* or *stricti juris*.[54] (Gane's translation)

From the above it is clear that by the end of the 17th century the use of and distinction between the *actio utilis* and *actio directa* had disappeared[55] and

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[50] *De Cessione* V, 1: '*Regulariter omnes actiones tam reales, quam personales cedi possunt'.*

[51] *Cession of Actions* 58.

[52] *Cession of Actions* 59. *De Cessione* V, 3: *'Actio etiam semel cessa, ab eo, cui cessa est, cedi potest, cum enim cessa actio fiat cessionari, dubium non est, quin eam rursus in alium transferre possit'.*

[53] *Commentarius* 2 14 9: '*Caeterum si non hae circa pacta, actionem formantia aut non formantia, distinctiones necessariae prorsus essent, ad Romani juris genuinum intellectum, legumque sine hoc praecognito to partim obscurarum, partim iniquitatem redolentium, explicationem; potuissent sane quantum ad fori usum attinet silentio involvi; eo quod nunc tralatitium prorsus est, & passim receptum, ex pactis nudis, serio ac deliberato animo interpositis, aeque ac ex contractibus, actionem nasci, multoque magis, si contractibus sive bonae fidei sive stricti juris adjecta sint; sive in continenti, sive ex intervallo id ipsum contigerit'.*

[54] P Gane *The Selective Voet being the Commentary on the Pandects by Johannes Voet and the Supplement to that work by Johannes van der Linden* (1955) 419 (hereinafter referred to as '*Commentary on the Pandects'*).

[55] Scott op cit 14.

it was widely accepted that cession effected a complete transfer of rights.[56]

It is thus only after the recognition of a cession as a complete transfer of rights that the *pactum de non cedendo* was born. It is impossible to establish when exactly in history the *pactum de non cedendo* first appeared.

It is, however, clear from the writings of Sande in *De Prohibita Rerum Alienatione* in 1633 that the *pactum de non cedendo* already existed. Some 65 years later, Voet also wrote about restrictions on cession in *Commentarius* and judging by the detailed recordings in their works, these two common law writers were clearly authorities on the subject.[57] What follows is a discussion of the views of Sande and Voet.

1.2.1 The debate

1.2.1.1 Sande

Sande deals with the validity of a *pactum de non cedendo* in the following manner: [58]

> A pact entered into with the owner, to the effect that he [the owner] shall not alienate his own property, is inoperative. Unless the person who makes the agreement [the *stipulans*] has an interest in the property.[59] (Webber's translation)

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[56] Scott op cit 12.

[57] Once again, it must be remembered that Sande and Voet are the alleged authorities on the on the law of cession and particularly on the law governing *pacta de non cedendo*, because from one of the earliest cases to address the validity and effect of *pacta de non cedendo* (*Paiges v Van Ryn Gold Mine Estates Ltd* 1920 AD 600) to the most recent case dealing with these issues [*Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd* 2008 (4) SA 510 (C)], these two old authorities have been cited as authority. See Chapter 4 for a critique on this issue.

[58] *De Prohibita* 4 1 Summary: '*Pactum initum cum domino, ne is rem suam alienet, est inutile. Nisi paciscentis intersit'.*

[59] W Webber *A Treatise upon Restraints upon the Alienation of Things* (1908) 293. (Hereinafter referred to as '*Restraints upon Alienation*'.)

From the outset Sande distinguishes between two forms of restraints:

> There is a great difference between any one making an agreement with the owner that he [the owner] shall not alienate his own property; and the owner, when he is alienating his own property by gift or sale, imposing this pact on the transfer of the property, that the donee or purchaser shall not alienate the property. [60] (Webber's translation)
>
> In the former case the pact is useless. For there is here no *causa* upon which such a pact can be supported; and utility, which is the mother of all good and of equity, demands that those pacts shall not be valid, which impede all commerce, and take away from us without any consideration the use of our own property. And just as we cannot infringe or take away the free use of their property by our neighbours by imposing a servitude upon it, unless we have some interest upon which to hang this servitude; so also we cannot by a pact take away from an owner the power of alienating his own property, unless we have some interest in it. From such an agreement, therefore, that the owner shall not be allowed to alienate his property, even if the stipulation is a valid one, not even a personal action can arise, for obligations and all actions can be summed up to this effect, that each person acquires to the extent of his own interest.[61] (Webber's translation)

Thus, the first form of *pactum de non cedendo* is invalid or '*inutile*' (useless) as the agreement has no *causa* and is contrary to the principle of utility – even if the stipulation was valid. The *pactum de non cedendo* would only be valid if the *stipulans* (the debtor) has an interest in the restraint.

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[60] *Restraints upon Alienation* 294. *De Prohibita* 4 1 Introduction: *'Interest utrum quis paciscatur cum ipso domino ne rem suam alienet; an vero dominus dum rem suam alienat donando, vel vendendo, tale pactum traditioni rei suae apponat, ne donatarius vel emptor eam rem alienet'.*

[61] *Restraints upon Alienation* 294. *De Prohibita* 4 1 1: '*Priori casu pactum est inutile. Nam nulla hic subset caussa, qua talis pactio sustineri queat; & utilitas, quae mater est boni & aequi, postulat, ne ea pacta valeant, quae rerum commercia omnino & sine caussa impediunt, nostrarumque rerum usum nobis adimunt. Ac quemadmodum fervitute aliqua imposita non possumus infringere ac tollere libertatem praediorum vicinorum, nisi nostra intersit ea nobis servire: Ita quoque pacto domino facultatem rei suae alienandae adimere non possum, nisi mea intersit. Ex hac igitur conventione, ne domino liceat rem suam alienare, quantumvis stipulatione vallata, ne personalis quidem nascitur actio, cum obligationes & actiones omnes ad hoc comparatae sint, ut unusquisque, quod sua interest*'.

Sande goes on to emphasise the interest requirement and uses the following practical example as an illustration:[62]

> If, therefore, the person making the pact or stipulation has any interest in that the owner shall not alienate his own property, a pact to the effect that the property shall not be alienated, is valid.[63] (Webber's translation)

> The agreement is therefore valid, if I make a pact with regard to a thing to which is not mine, but in which I have some right; for instance, that you shall not alienate your land which you have mortgaged to me. For it is to my interest that the land shall not be alienated, for instance, to a litigious man, or to any other troublesome person, against whom, if I bring a hypothecary action, I shall be compelled to adduce more conclusive evidence; for I shall then be required to prove that the property has been mortgaged to me, and also that it was the property of the debtor.[64] (Webber's translation)

Sande also considered the validity of the second form of *pactum de non cedendo*. He wrote:

> Now, in the second case, where a person on the donation, or sale, or transfer, or alienation of his property, adds the condition that it shall not be alienated, such a pact is wholly valid. For every man has free control and administration over his own property and can at the time of alienation place any condition he pleases upon his property; and as Gaius says…it is undoubted law that every pact made by a person transferring his own property is valid. And as Justinian says…an owner would not wish to transfer his right under any condition unless he relied upon such agreement.[65] (Webber's translation)

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[62] See *De Prohibita* 4 1 4 and 4 1 5 for examples not mentioned herein.

[63] *Restraints upon Alienation* 294. *De Prohibita* 4 1 2: '*Quod si igitur paciscentis vel stipulantis intersit, ne dominus rem suam alienet, valet pactum de re aliena non alienanda'.*

[64] *Restraints upon Alienation* 294-295. *De Prohibita* 4 1 3: *'Hinc valet conventio, si pactus sim de re, quae quidem non est mea; sed in qua jus aliquod habeo, veluti ne alienes fundum tuum, qui mihi pignori obligatus est. Quia interest mea, ne fundus alienetur forte in litigiosum, aut alioqui incommodum hominem, contra quem hypothecaria acturus gravioribus probationibus onerabor: cum eo casu & rem mihi obligatam esse, & in bonis debitoris fuisse probare tenebor'.*

[65] *Restraints upon Alienation* 296. *De Prohibita* 4 1 6: '*Posteriori casu: quando quis donationi, venditioni, traditioni vel alienationi rei suae eam legem asscribit, ne alienetur, pactum omnino utile est. Est enim quisque rei suae liber moderator & arbiter, & eam quam vult legem rei suae, tempore alienationis dicere potest in traditionibus rerum*

It thus seems that this form of *pactum de non cedendo* is 'wholly' valid as it stands, without an interest as a prerequisite since no mention is made to the contrary. In the very next paragraph, however, mention is made of an interest and it is unclear whether Sande contradicted himself or whether he merely intended to qualify the preceding paragraph.

> Now, the interest of the person making such a pact should not be too strictly judged; for he has sufficient interest who can in every case say that he would not otherwise have alienated his property.[66] (Webber's translation)

Sande then goes on to deal with the effect of a *pactum de non cedendo* and the distinction between the two forms of *pacta de non cedendo* is still evident. The effect of the first form is as follows:

> A pact concerning the property of another, in which the person who imposes the restriction has no interest, is of no effect or moment, unless a penalty is also imposed which is to become due in case of alienation; for even a person who has no interest in a property can make a pact with regard to it, if a penalty is added… but this should be understood not as referring to any stipulation, but… to a stipulation with a penalty attached; for from such a stipulation an action is given to a person, who would otherwise have no interest in the property.[67] (Webber's translation)

> If the person making the pact or stipulation has some interest in the property of another person, then a pact that such person shall not sell such property is binding, and when added to a *bona fide* contract, or strengthened by a stipulation, gives rise to an action on the contract or stipulation for the amount of such interest against

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suarum, quodcunque pactum sit, id valere manifesissimum esse, Cajus respondit. Nec alia lege dominus jus suum transferre voluit, nisi tali fretus conventione, ut Justinianus loquitur & sub hac conditione minoris vendidit'.

[66] *Restraints upon Alienation* 296. *De Prohibita* 4 1 7: '*Nec hic scrupulose inquirendum est, an paciscentis intersit: quia hoc ipso satis interest, quod omni casu is, qui pactus est, dicere potest, se non alias rem suam fuisse alienaturum'.*

[67] *Restraints upon Alienation* 299. *De Prohibita* 4 2 1: '*Pactum appositum rei alienae, si paciscentis non interest, inessicax & nullius momenti, est nisi forte ei poena adjecta sit, quae in casum alienationis committarur, quia ex stipulatione poenali agit etiam, cujus non interest… non accipiendum est de stipulatione quacunque, sed… de stipulatione poenali, ex qua datur actio ei cujus alioqui nihil interest*'.

> the person who has alienated the property in spite of the agreement.[68] (Webber's translation)

> If an owner promises, upon his oath, to the person with whom he makes the stipulation or pact, that he will not alienate his own property, the Doctors do not agree as to whether dominium will be prevented from passing because of such oath. The more correct view is that it is not so prevented. For an oath does not change the nature of an act on which it is made, but retains all the qualities and conditions which such act has; and, therefore, if a person engages upon his oath that he will not alienate his property, and then he breaks his oath, he is liable for any loss, and if the property be sold, the dominium passes to the purchaser by virtue of such sale….[69] (Webber's translation)

The first form of *pactum de non cedendo*, therefore, has no effect unless a penalty clause is inserted into the agreement, or if the *stipulans* has some other interest in the agreement. Should a penalty clause or other interest exist, the agreement is valid and binding.

Sande emphasises that the effect of such an agreement is not entirely settled because the jurists do not agree as to whether ownership passes to the cessionary despite the *pactum de non cedendo* or whether ownership fails to pass because of the *pactum de non cedendo*. Sande, however, believes that the more correct view is that ownership does pass to the cessionary, although the cedent will be liable for any loss suffered by the debtor (*stipulans*).

The effect on the second form of *pactum de non cedendo* is as follows:

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[68] *Restraints upon Alienation* 299-300. *De Prohibita* 4 2 2: *'Si interest paciscentis vel stipulantis, tunc pactum de non alienando appositum rei alienae utile est, ac adjectum contractui bonae fidei, vel stipulatione vallatum producit actionem ex ipso contractu vel ex stipulatione in id quod interest contra eum, qui insuper habita conventione alienavit'.*

[69] *Restraints upon Alienation* 304. *De Prohibita* 4 2 11*: 'Si dominus stipulanti vel paciscenti juratus promiserit, se rem suam non alienaturum, an vi juramenti impediatur dominii translatio, inter Doctores controvertitur? Non impediri verius est. Quia juramentum non mutat naturam actus, super quo interponitur, sed recipit omnes qualitates & conditiones, quas actus habet, & ideo, qui jurato promisit se non alienaturum, si contravenerit, tenetur ad id quod interest, & dominium rei traditae non potest non per traditionem factam ex titulo habili transire in accipientem…'.*

> If an owner on the transfer of his property, for instance when selling his property at a sale, makes this a condition of the sale that the purchaser shall not alienate or sell to anyone but him; and the purchaser, in spite of such condition, does thereafter sell to someone other than the former owner, he is liable in an action on the sale for the damage which the original vendor has sustained through the property being alienated or sold to another than himself.[70] (Webber's translation)
>
> There has also been considerable controversy on the point whether, if the owner on the sale of his property makes a pact that the purchaser shall not alienate it, such a pact is so far effective as to prevent the dominium from passing if the new owner does alienate the property? The most common view amongst the Doctors is that it will not have such effect….[71] (Webber's translation)
>
> From the different arguments that have been given on both sides, it appears that the more correct view is held by those who say that the passing of the dominium can be prevented by a pact, if only the owner imposes this pact at the time of the transfer of his property, or makes a condition at the time of the alienation of the property, and not subsequently, as by tradition the right has been acquired by another person….[72] (Webber's translation)

The effect of this form of *pactum de non cedendo* is that if the cessionary ceded contrary to the *pactum de non cedendo*, then the cedent would have an action for damages against him.

Like the other form of *pactum de non cedendo*, some debate exists as to whether ownership is transferred to the third party when alienation occurs contrary to the *pactum de non cedendo*. Sande sets out the conflicting

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[70] *Restraints upon Alienation* 304. *De Prohibita* 4 2 12: *'Si dominus in transsatione rei suae, ut venditor in venditione & traditione rei suae legem dixerit, vel pepigerit, ne emptor alienaret, vel ne alii quam sibi venderet, & emptor nihilominus eam alienaverit, vel alii, quam priori domino vediderit, imprimis tenetur actione ex vendito in id quod venditoris interest, eam esse alienatam vel alii, quam sibi venditam'.*

[71] *Restraints upon Alienation* 306. *De Prohibita* 4 2 14: *'At quaestionis est multum controversae, si dominus in traditione rei suae paciscatur, ne liceat accipienti eam alienare, an hoc pactum adeo efficax sit, ut dominii translationem impediat? Negant hoc frequentius Doctores…'.*

[72] *Restraints upon Alienation* 314. *De Prohibita* 4 2 26: *'Ex his utrinque disputatis[72] satis liquet veriorem esse sententiam docentium translationem dominii posse impediri pacto, dummodo illud dominus apponat traditioni rei suae istam legem dicat in ipsa traditione vel alienatione, non postea, cum ex traditione alteri jam jus quaesitum est…'.*

arguments of the jurists and concludes that the more correct view is that ownership does not pass, provided that the condition is made at the time of alienation and not thereafter.

The consequence of this, as Scott notes, is that the cessionary obtains limited ownership as he is unable to make a further transfer. The cessionary thus obtains a limited real right from the cedent as upon transfer the right is rendered non-transferable.[73]

1.2.1.2 Voet

Voet's writings on the *pactum de non cedendo* appear to be very similar to Sande's, except for the fact that Voet makes no distinction between different forms of *pacta de non cedendo* and writes only (according to Sande's distinction) of the first form of *pactum de non cedendo* as if no other form exists.

> Agreements also by which an owner deprives himself of discretion and control as to his own property are without effect whenever no advantage accrues from them to the other party. An agreement does not affect things, but binds a person to keep faith. If he did not stand to his promises, by Roman law no action could be given for damages. And if, as is the case, an action is now given on an agreement, there could be no room at all for it, where no one has an interest. In this sense it is true that no one can by making an agreement bring it about that he shall have no power to consecrate his own place, or to bury a corpse in his own ground, or that he shall not part with his land without the consent of his neighbour.
>
> But if you assume that the person agreeing has an interest, and that such an agreement has been annexed in accord with Roman law to a *bonae fidei* contract such as purchase, the better opinion is that it ought to be kept, though there was of old a doubt upon the matter. This is not because things done contrary to the agreement would be *ipso jure* null, or would affect the thing itself… [i]t is because a personal action for either damages or penalty (if a

[73] S Scott 'Pacta de non cedendo' 1981 *Tydskrif vir Hendendaagse Romeins-Hollandse Reg* 158.

penalty had been annexed to the agreement) would have to be given to the other person agreeing.[74] (Gane's translation)

As to the validity of *pacta de non cedendo*, Voet confirms that an agreement depriving an owner of the management of his own property is without effect, unless the other party has an interest.

As to the effect of *pacta de non cedendo*, Voet further confirms that alienation in contravention of the prohibitory agreement has no effect on the object being alienated, nor would the alienation, in contravention of the prohibitory agreement, be void. This means that ownership is transferred despite the *pactum de non cedendo*. In effect the *pactum de non cedendo* is merely to enforce that a person remains faithful to his promise, with an action for damages arising should he dishonour his promise.

1.3 Conclusion

It is interesting to consider the gaps and incomplete statements of the law in the contributions of Sande and Voet.

Both writers recognised that a transfer of a right of action may be prohibited by agreement if the *stipulans* has an interest in the prohibition, but neither explains the content of this interest requirement.[75]

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[74] *Commentary on the Pandects* 434-435. *Commentarius* 2 14 20: '*Inutilia quoque pacta, quibus dominus sibi de re sua arbitrium ac moderamen adimit, quoties inde nulla ad alterum utilitas pervenit: cum enim pactum res non afficiat, sed personam obstringat ad fidem servandam, eo promissis non stante, nulla jure Romano ad id quod interest actio dari posset, & si maxime ex pacto detur nunc actio, ei locus esse haud poterit, cum nullius intersit. Eoque sensu verum est, neminem paciscendo essicere posse, ne sibi locum suum dedicare liceat; aut, ne sibi in suo mortuum sepelire liceat; aut ne vicino invito praedium alienet. Sed si paciscentis interesse ponas, & pactum tale adjectum ex jure Romano bonae fidei contractui, velut emtioni, servandum esse, verius est, licet de eo olim dubitatum fuerit. [N]on, quod contra pactum gesta ipso jure nulla forent, aut rem ipsam afficerent… sed quod vel ad id, quod interest, vel ad poenam, (si quae conventioni adjecta sit) personalis actio paciscenti danda foret'.*

[75] See Chapter 4 for a more detailed discussion of this issue.

A point to consider regarding the penalty clause is whether the enforceability of the agreement hinges on the inclusion of a penalty when no interest exits, or whether the agreement remains ineffective due to the lack of an interest, becoming effective only if the right is transferred contrary to the penalty.

Perhaps the most interesting consideration is why Voet failed to distinguish between the two forms of *pacta de non cedendo* as Sande clearly did, especially since Voet published *Commentarius* 65 years after *De Prohibita* was published; no academic has attempted to explain this.[76]

A possible explanation for Voet's failure to make the same distinction is that this form of *pactum de non cedendo* was either not used by contractants and/or accepted by other jurists, or the area of its application was too narrow to be mentioned. Since Voet was very thorough in his writings, the more convincing reason would be the former.

Another possible reason may be found in the fact that, although Sande and Voet were both writing on Roman-Dutch law, they had different perspectives on the law. Sande was born and raised in Friesland and it is generally accepted that the old authorities from that part of Holland adhered more closely to Roman law. The Roman-Dutch law which prevailed in Friesland thus leaned toward strict Roman law in comparison to the Roman-Dutch law that was received in the other provinces of Holland where the local law was more prominent.[77]

Voet, on the other hand, was born and raised in Utrecht and was much more focussed on the *usus modernus*. The general idea was to reconcile

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[76] According to Scott 'Pacta de non cedendo' op cit 157 in footnote 86, Sande's second form of *pactum de non cedendo*, where he recognises that a cedent can enter into an agreement with a cessionary to prevent the cessionary from ceding the right further, is not possible in any other legal system.

[77] JW Wessels *History of the Roman-Dutch Law* (1908) 239-240. See also GF Kotze *Die Leerstuk van Onherroeplike Volmag in die Suid-Afrikaanse Verteenwoordigingsreg* (1985) LLM thesis University of Stellenbosch 38.

Roman law with the practice of his time. Thus it may be said that Voet failed to make the same distinction as that of Sande because such a distinction was out-moded by the modern practice of that time.[78]

[78] Wessels op cit 320-330; Kotze op cit 38.

CHAPTER TWO

FOREIGN LAW PERSPECTIVE

This Chapter investigates how the English and American legal systems deal with the validity and effect of the *pactum de non cedendo*.

2.1 English Law

2.1.1 English law of assignment in general

English law uses different terminology in this area of the law to that which is generally used in South Africa. 'Cession' in English law is called 'assignment', the cedent is referred to as the 'assignor' and the cessionary is the 'assignee'. The 'debtor' is also often referred to as the 'obligator'. English law also terms a 'personal right' a 'chose in action'.[79]

Much like Roman law, the English common law originally did not recognise an assignment of a chose in action, as choses in action were considered to be strictly personal. Only the person who had the right could sue on it and it could not be transferred to a person not party to the original obligation.[80]

The rule was initially based on the difficulty to comprehend that an intangible thing could be transferred. Later, the rule was said to be based on the fear that assignment of choses in action might lead to 'maintenance', a term used to describe 'intermeddling' where 'the intermeddler has no concern' in the matter.[81]

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[79] PH Pettit 'Choses in Action' in *Halsbury's Laws of England* 4ed vol 6 (2003) 3.

[80] A Wood Renton and MA Robertson *Encyclopaedia of the Laws of England* vol 3 (1907) 49; J Salmond and J Williams *Principles of the Law of Contracts* 2ed (1945) 456; GH Treitel *The Law of Contract* 9ed (1995) 590; Pettit op cit 11.

[81] Treitel op cit 590.

The rule preventing a transfer of a right was further upheld by the doctrine of privity of contract, whereby a person could not become a party to a contract which he was originally not a party to.[82]

In an attempt to effect a transfer of a right, English law made use of novation, acknowledgment and power of attorney.[83] These alternatives, however, like in Roman law, had their own shortcomings.[84]

Consequently, from a very early period (17th century) the equitable jurisdiction of the Court of Chancery began to view choses in action as property and came to realise the commercial importance of transferability.[85] As a result equitable assignments were freely permitted, although in reality only equitable ownership vested in the assignee, with the assignor still retaining legal ownership. [86]

Enforcement of the assignee's equitable title posed a problem. Although the Courts of Chancery recognised the assignee's equitable title, they did not commonly exercise jurisdiction to enforce claims arising *ex contractu*.[87] The Courts of common law refused to recognise the assignee's equitable title, so neither could he sue for performance in the Courts of common law.[88]

To overcome this problem the Courts of Chancery imposed a duty on the assignor to allow the assignee to sue in his name in the Courts of common

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[82] GF Kotze *Die Leerstuk van Onherroeplike Volmag in die Suid-Afrikaanse Verteenwoordigingsreg* (1985) unpublished LLM thesis University of Stellenbosch 2.

[83] Treitel op cit 590-591; Kotze op cit 2 *et seq*.

[84] Ibid.

[85] Salmond and Williams op cit 456-457.

[86] Wood Renton and Robertson op cit 50; Salmond and Williams op cit 456-457; Treitel op cit 591; Pettit op cit 11.

[87] Salmond and Williams op cit 457.

[88] Ibid.

law – ostensibly on behalf of the assignor as legal owner, but in reality for himself.[89]

Later, the common law somewhat relaxed the rules regarding assignment as the common law was influenced by mercantile custom, which disregarded the common law and allowed negotiable instruments to be freely assigned.[90] Further, statutes were also enacted that allowed certain classes of choses in action to be assigned.[91]

It was only in 1873 that legislation was passed to transform the law in a more drastic manner. This transformation was brought about by the Judicature Act, specifically s25(6), which made choses in action assignable at law.[92] Substantial portions of this Act were later re-enacted by the Law of Property Act in 1925 with s25(6) being replaced by s136.[93]

The English law now provides that an assignment of a chose in action transfers legal ownership and all the rights and remedies attached thereto, to the assignee, who may sue the debtor in his own name.[94]

According to s136 of the Law of Property Act, an assignment amounts to a legal assignment if three requirements are met.[95] The requirements under the Act are first, that the assignor must reduce the assignment agreement to writing. Secondly, the assignment must be absolute and not 'by way of charge only'.[96] An assignment is not absolute if the assignor retains an

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[89] Salmond and Williams op cit 457; Pettit op cit 11.

[90] Wood Renton and Robertson op cit 51-52; Salmond and Williams op cit 457.

[91] Wood Renton and Robertson op cit 52, for example, Bills of Lading Act of 1855, Policies of Assurance Act of 1867 and Marine Insurance Act of 1868.

[92] Salmond and Williams op cit 458; Treitel op cit 593; Pettit op cit 11.

[93] Ibid.

[94] Pettit op cit 12.

[95] Pettit op cit 13.

[96] Pettit op cit 15. It seems that there is no fixed test to determine if an assignment is by way of charge only. Rather, a holistic approach should be adopted taking into account the intentions of the parties and the terms of the agreement. An example of an assignment by way of charge only is where a document assigned only gives the

interest in the subject matter[97] or if the assignment is conditional.[98] Thirdly, express notice in writing must be given to the debtor either by the assignor or the assignee. This is an important requirement as assignment is said to operate as from the date when such notice was received by the debtor.[99] If an assignment fails to comply with these requirements it will not, as a consequence thereof, be considered a legal assignment. It may, however, still amount to an equitable assignment.[100]

The Law of Property Act is still in force in England at present and the law of assignment has not changed significantly since the passing of the Act.

2.1.2 Unassignable contracts through the cases

English law, like South African law, also prohibits the assignment of certain choses in action. Some of these prohibitions[101] include assignments contrary to public policy,[102] rights arising from personal contracts (otherwise known as *delectus personae*), pensions, a wife's right to spousal maintenance, rights to social security benefits and bare rights of action.[103]

English law also recognises *pacta de non cedendo* as possible prohibitions on assignment, although the term '*pactum de non cedendo*' is

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'assignee' a right to payment out of a particular fund or property, and does not absolutely transfer the fund or the property.

[97] Salmond and Williams op cit 468-469; Treitel op cit 593.

[98] Pettit op cit 15. For example, if the assignment was made only for such time as money advanced is repaid, the assignor retains an interest. Or, if an insurance policy is assigned with the condition that the assignee shall be entitled to the insurance money only if the assignor predeceases the assignee, the assignment is a conditional one.

[99] Treitel op cit 596; Pettit op cit 18.

[100] Treitel op cit 596.

[101] Treitel op cit 610-613; Pettit op cit 53-62.

[102] Pettit op cit 53.

[103] As described in Pettit op cit 57, a bare right of action is a right of litigation for damages for defamation or personal injury.

not used. Phrases like an 'unassignable contract' or a 'non-assignment clause' are used instead.

In English law, an unassignable contract is regarded as completely valid and not much dispute has arisen in this regard. The debtor does not have to show that he has an interest in the restriction, nor does public policy place any kind of hindrance on the rights of parties wishing to make a contract unassignable.[104]

On the other hand, the effect of an unassignable contract on a subsequent cession has caused quite a stir. What follows is a discussion of the historical development of the effect of an unassignable contract through the cases.[105]

Brice v Bannister[106] was decided soon after the Judicature Act was passed. In that case Bramwell LJ made the following statement:

> … it does seem to me a strange thing and hard on a man, that he should enter into a contract with another and then find that because the other has entered into some contract with a third, he, the first man, is unable to do that which it is reasonable and just he should do for his own good. But the law seems to be so; and any one who enters into a contract with A must do so with the understanding that B may be the person with whom he will have to reckon. Whether this can be avoided, I know not; may be, if in the contract with A it was expressly stipulated that an assignment to B should give no rights to him, such a stipulation would be binding. I hope it would be.[107]

As to the effect of a contravention of a non-assignment clause, Bramwell LJ seems to favour absolute invalidity of the purported assignment. The

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[104] *Linden Gardens Trust Ltd v Lenestra Sludge Disposals Ltd* [1993] 3 All ER 417.

[105] This discussion focuses solely on cases considering the effect of an unassignable contract that has been assigned in contravention thereof. Other cases which have considered some other aspect of unassignable contracts have thus not been included.

[106] [1878] 3 QBD 569.

[107] Supra 580-581.

result is that the agreement between the assignor and debtor remains completely unscathed, while the assignee obtains nothing under the assignment agreement, barring presumably, an action for damages against the assignor for breach of contract.

The next case that considered the effect of a contravention of an non-assignment clause was *Shaw & Co v Moss Empires Ltd and Bastow*,[108] where Darling J held that the non-assignment clause in the contract between the debtor and assignor:

> …could no more operate to invalidate the assignment [between the assignor and the assignee] than it could to interfere with the laws of gravitation.[109]

As to the effect of a contravention of a non-assignment clause, Darling J seems to favour partial invalidity. The result is that the right of ownership passes to the assignee, while still allowing the debtor to perform as he would have, had no assignment taken place.

Seventy years later, in the case of *Helstan Securities Ltd v Hertfordshire County Council*,[110] the council employed Renhold Road Surfacing Ltd, a firm of contractors, to carry out some road works. One of the clauses in their contract provided that Renhold Road Surfacing Ltd was prohibited from assigning the contract or any benefit thereunder or interest therein, without the written consent of the council.

During the currency of the contract Renhold Road Surfacing Ltd experienced severe financial difficulties and consequently assigned the debts owing to it by the council to Helstan Ltd without first obtaining the council's consent. The council refused to recognise the assignment due

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[108] [1908] 25 TLR 190.

[109] Supra 191.

[110] [1978] 3 All ER 262.

to the existence of the non-assignment clause, and claimed that the assignment was invalid, even as between the assignor and the assignee.

The case was decided by Croom-Johnson J, who reviewed both the earlier cases on the issue (as I have done above) but passed very little comment, if any. Croom-Johnson J did, however, express himself very clearly in response to an argument advanced by Helstan Ltd.

Helstan Ltd argued that a very different rule regarding unassignable contracts applies in the case of leases. According to the argument, when a lessee assigns his lease in contravention of the non-assignment clause, the assignment is valid with the result, in the worst case scenario, being that the lessor may sue the assignor for breach of contract. The assignment, however, is still valid as between assignor and assignee.

Croom-Johnson J refused to recognise any comparison between the two areas of unassignable contracts and stated that 'the law concerning covenants running with the land is not something which is readily adaptable to choses in action'.[111] He failed to give a satisfactory explanation for this refusal and simply stated that:

> There are certain kinds of choses in action which, for one reason or another, are not assignable and there is no reason why the parties to an agreement may not contract to give its subject-matter the quality of unassignability.[112]

Croom-Johnson J was further of the opinion that a debtor should not be forced to deal with an unknown assignee when he has specifically contracted to avoid this occurrence.[113] In concluding that the non-assignment clause rendered the assignment in contravention thereof invalid, the judge also added that there was no injustice in expecting

[111] Supra 265.

[112] Supra 265-266.

[113] Supra 266.

Helstan Ltd to make proper enquires before agreeing to take assignment of the debts.[114]

As to the effect of a contravention of a non-assignment clause, Croom-Johnson J, like Bramwell LJ mentioned above, thus also seems to favour absolute invalidity.

The next case, *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd and others and another appeal*,[115] is to date the most authoritative case on the issue.

In this case Stock Conversion and Investment Trust plc (Stock Conversion) were the owners of a leasehold of certain property. Stock Conversion entered into an agreement with McLaughlin & Harvey plc (the second defendant) for the removal of asbestos from the property. [116] Clause 17 of their contract contained a non-assignment agreement whereby neither party could assign the contract without the other's consent.

After McLaughlin & Harvey plc carried out its work of removing the asbestos, more asbestos, which it should have removed, was discovered. Stock Conversion consequently entered into a contract with Ashwell Construction Co Ltd (the third defendant) for the removal of the said discovered asbestos. This contract also contained a non-assignment clause.

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[114] Ibid.

[115] [1993] 3 All ER 417.

[116] It must be noted, for the sake of completeness and to explain the presence of Lenesta Sludge Disposals Ltd as a party to the action, that the latter company was the nominated sub-contractor for the removal of the asbestos and was of no significance to the legal proceedings.

Some time later Stock Conversion began to institute legal proceedings against Lenestra Sludge Disposal Ltd for breach of contract. In the course of instituting the latter Stock Conversion assigned to Linden Gardens Trust Ltd (Linden Gardens) its interest in the leasehold as well as all its rights under the two asbestos removal contracts (which necessarily included the right to take over and continue the action against Lenesta Sludge Disposal Ltd). At no time, however, was the consent of McLaughlin & Harvey plc and Ashwell Construction Co Ltd ever sought or given.

Subsequently, yet more asbestos was discovered on the premises and Linden Gardens incurred the cost of its removal. Consequently, Linden Gardens as assignee in the present action, sought to sue the defendants for breach of contract.

Lord Browne-Wilkinson, who delivered the majority judgment in the House of Lords, noted that two questions arose from the case:[117] First, whether the assignment to Linden Gardens was effective, considering the non-assignment clauses and secondly, whether Linden Gardens, as assignee, could recover damages (incurred after assignment) for the cost of removing more asbestos.[118]

Lord Browne-Wilkinson thought it wise to consider the opinion of Goode,[119] one of the more prominent English writers on the law of assignment, and pointed out that where a contract prohibits assignment of contractual rights, the effect of such a prohibition depends on the construction of the contract. Goode proposed as early as 1979 that there are four possible constructions.[120]

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[117] Supra 423.

[118] The second issue, however, is not relevant for the purpose of this discussion.

[119] RM Goode 'Inalienable rights?' 1979 *Modern Law Review* (vol 42) 553.

[120] Supra 428. See below for a more detailed discussion.

The judge also considered whether non-assignment clauses were against public policy. The rationale for this enquiry was that usually it is against public policy to render property inalienable.[121] He noted that neither in *Helstan Securities Ltd v Hertfordshire County Council* nor in other cases was public policy advanced as an argument. In fact, the cases accepted the validity of non-assignment clauses.[122] The court was referred to Scottish, American and even South African cases (*Paiges v Van Ryn Gold Mine Estates*) to illustrate that in these legal systems a contract prohibiting assignment is also not against public policy.

In concluding, the judge could see no good reason for declaring such contracts as against public policy and stated the following:

> In the case of real property there is a defined and limited supply of the commodity and it has been held contrary to public policy to restrict the free market. But no such reason can apply to contractual rights: there is no public need for a market in choses in action. A party to a building contract, as I have sought to explain, can have a genuine commercial interest in seeking to ensure that he is in contractual relations only with a person whom he has selected as the other party to the contract. In the circumstances, I can see no policy reason why a contractual prohibition on assignment of contractual rights should be held contrary to public policy.[123]

Lord Browne-Wilkinson thereafter considered the effect of an assignment made contrary to a transfer prohibition. Relying on, *inter alia*, *Shaw & Co v Moss Empires Ltd*, Linden Gardens submitted that even if the assignments constituted a breach of the clause in question, the clause could not prevent a cause of action from vesting in the assignee.[124]

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[121] Supra 430.

[122] Ibid.

[123] Ibid.

[124] Supra 431. This quotation seems to be a reflection on the doctrine of privity of contract.

Even though the judge criticised *Shaw & Co v Moss Empires Ltd* as being inadequately reported and felt that the *ratio* was ambiguous, he held:

> …a prohibition on assignment normally only invalidates the assignment as against the other party to the contract so as to prevent a transfer of the chose in action: in the absence of the clearest words it cannot operate to invalidate the contract as between the assignor and the assignee and even then it may be ineffective on the grounds of public policy.[125]

The judge also considered *Helstan Securities Ltd v Hertfordshire County Council* and noted that:

> Croom-Johnson J did not follow the Shaw case and held that the purported assignment in breach of the contractual provision was ineffective to vest the cause of action in the assignee…. Therefore the existing authorities establish that an attempted assignment of contractual rights in breach of a contractual prohibition is ineffective to transfer such contractual rights. I regard the law as being satisfactorily settled in that sense. If the law were otherwise, it would defeat the legitimate commercial reason for inserting the contractual prohibition, viz, to ensure that the original parties to the contract are not brought into direct contractual relations with third parties.[126]

The action brought by Linden Gardens was accordingly dismissed. The House of Lords, therefore, declared that the contractual relationship as between the assignor and assignee remains intact, but only in the sense that the assignee may have recourse to damages for breach of contract and not for an action of specific performance. Ownership, however, still appears to vest in the assignor.

It seems that no subsequent case has departed from this *ratio*.[127]

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[125] Supra 431.

[126] Supra 431-432.

[127] *Yeandle v Wynn Realisations Ltd (in administration)* [1995] 47 Con LR 1, CA; *Flood v Shand Construction Ltd* [1996] 54 Con LR 125, CA; *Don King Productions Inc v Warren* [1998] 2 All ER 608; *Hendry v Chartsearch Ltd* [1998] CLC 1382, CA; *Quadmost Ltd v*

2.1.3 The English academics' opinions

The English academics started their debate around 1945 when Salmond and Williams were of the opinion that there was no reason why a contract should not be made unassignable.[128] Their view to the effect of such a prohibition was that every assignee was bound by the terms of the contract so assigned to him, and the assignee could, therefore, not attempt to enforce his rights against the debtor, as this was something that the terms of the contract specifically prohibited.[129]

The authors added that if the assignment of a contract was prohibited, and it was assigned in contravention of the agreement, it would be difficult for the assignee to find a legal ground on which to base such a defiance so that he might enforce performance from the debtor.[130]

Salmond and Williams also noted that a contractual prohibition on assignment seems to be strictly construed, requiring express terms to ensure its intended application.[131]

In 1979, one year after *Helstan Securities Ltd v Hertfordshire County Council* was decided, the debate continued when two more articles on non-assignment clauses were published.

In his exploration of the effect of an assignment in contravention of a non-assignment clause, Goode points out that a non-assignment contract can

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Reprotech (Pebsham) Ltd [2001] BPIR 349. *Contra* A Trukhtanov 'Trust of a non-assignable contractual benefit: *Barbados Trust Company v Bank of Zambia*' 2007 *Modern Law Review* (vol 70) 484 although the issue under discussion in this article and the case considered therein is somewhat off the topic.

[128] Salmond and Williams op cit 477.

[129] Ibid.

[130] Ibid.

[131] Ibid.

appear in four different constructions.[132] Each construction will necessarily have a different result on the effect of such a transfer. Further, the application of any one of the possible constructions depends entirely on the words used to form the contract.[133]

The first construction is that the prohibition constitutes a mere personal undertaking or promise not to assign. An assignment in contravention thereof is not rendered ineffective as against the debtor; the assignee *would* acquire rights against the debtor. The debtor's only remedy would be to sue the assignor for breach of contract.[134]

Goode states that this construction is simple enough and needs no comment,[135] but in *Linden Gardens* Lord Browne-Wilkinson remarked that in his opinion this construction is very unlikely to occur.[136]

The second construction is that assignment in contravention of the prohibition is indeed rendered ineffective against the debtor. As a result the debtor is permitted to ignore the notice of assignment, and he may continue to pay the assignor and set up equities (raise defences) against him as if no assignment has occurred. The status of 'ineffectiveness-as-against-the-debtor' does not interfere with the assignor's right to assign the fruits of the contract after he has received it from the debtor.[137]

Goode remarks that this construction is a valid one and that the law would give effect to it. The result, however, would not be a statutory assignment

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[132] RM Goode 'Inalienable rights?' 1979 *Modern Law Review* (vol 42) 553.

[133] Goode op cit 554. Lord Browne-Wilkinson in *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* approved of Goode's submissions.

[134] Goode op cit 554.

[135] Ibid

[136] *Linden Gardens* supra 428. One wonders why the judge thought that this construction would be unlikely**.** No reasons were advanced for this opinion.

[137] Goode op cit 554.

for the purposes of s136 of the Law of Property Act, as the Act allows an assignee to sue in his own name.[138]

Goode asserts that in *Helstan Securities Ltd v Hertfordshire County Council,*[139] the argument advanced by the council went a step further as it was argued there that the prohibition rendered the assignment ineffective even as between the assignor and assignee.[140]

Goode is alarmed at the judge's agreement with this argument.[141] He submits that the difficulty in determining the effect of a prohibited transfer lies, *inter alia*, in the failure to differentiate between the concept of ineffectiveness against the debtor and the concept of invalidity between the assignor and assignee.[142] A debtor may stipulate that he will accept counter-performance only from the assignor and that he will make payment only to the assignor. The interest in the monies handed over to the assignor, however, vests in the assignor. Whether and to whom the assignor transfers such monies, is of no concern to the debtor. It cannot affect him in any way and terms of this nature (that is, bringing about such invalidity) should not be readily construed as purporting to do this.[143]

If Croom-Johnson J had kept the above distinction in mind, then according to Goode's line of reasoning, the judge would have exercised a little more caution and would not have been so ready to accept the council's argument.

The third construction is that the assignor is prohibited from assigning the fruits of the contract even after he has received them from the debtor, with

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[138] Ibid.

[139] Supra 263-264.

[140] Goode op cit 554-555.

[141] Goode op cit 555.

[142] Ibid.

[143] Ibid.

the result that the assignee can obtain no rights even as between himself and the assignor.[144]

Goode is of the opinion that this construction is 'repugnant to the creditor's [purported assignor's] ownership and ought not to be countenanced'.[145] As a result it should be devoid of effect. In support of this view he refers to the famous words of Darling J in *Shaw & Co v Moss Empire*.[146]

The fourth construction is that an assignment in contravention of the prohibition constitutes a breach of the contract entitling the debtor to terminate the contract and claim damages from the assignor thereby reducing or extinguishing the assignor's right of payment.[147]

Goode states that this construction would have to be tested against the rules of equity governing forfeiture and would probably be struck down as an unconscionable forfeiture.[148] Lord Browne-Wilkinson also believed that this construction was very unlikely to occur.[149]

Goode then turns to discuss the possible reasons why a debtor may insist on prohibiting assignment. Goode admits that a debtor may have good and legitimate reasons for including a non-assignment clause in a contract.[150] These reasons may include the situation where a debtor overlooks receipt of the notice of assignment and pays to the assignor. Such a payment does not warrant the debtor to a 'good discharge' of the debt and he may be compelled to pay again (to the assignee).[151] Another

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[144] Goode op cit 554.

[145] Goode op cit 556.

[146] Goode op cit 556. The judge's famous words are that such a term 'could no more operate to invalidate the assignment than it could interfere with the laws of gravitation'.

[147] Goode op cit 554.

[148] Goode op cit 554 and 557.

[149] Supra 428.

[150] Goode op cit 553.

[151] Ibid.

reason for including a non-assignment clause is that a debtor cannot set up equities (raise defences) as against the assignee, if such equities arise after he receives the notice of assignment.[152]

Despite admitting these benefits, Goode is critical of the decision in *Helstan Securities Ltd v Hertfordshire County Council* from the viewpoint of commercial efficacy. He is of the opinion that to expect an assignee to make proper enquiries before buying debts (as was argued in this case and accepted by Croom-Johnson J) ignores commercial realities.[153]

The rationale of this criticism is that where there is a continuous flow of receivables as between assignor and assignee, especially when one of the parties carries on business as a factoring company or finance house, scrutinising individual contracts is very impractical.[154]

Goode appreciates the concern of the commercial world and believes that if *Helstan Securities Ltd v Hertfordshire County Council* is to be literally interpreted, it would threaten the security of receivables financing as a whole.[155]

It is also interesting to note that Goode often makes reference to American law. In particular, he states that in America the courts became increasingly hostile to attempts made to prohibit the transfer of receivables so that eventually legislation was passed to render ineffective any term prohibiting the assignment of receivables.[156]

Goode's article was published in 1979 and factoring or the transfer of receivables had been steadily on the rise since before this date. Goode's

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[152] Ibid.

[153] Goode op cit 556.

[154] Ibid.

[155] Ibid.

[156] Goode op cit 557 footnote 11.

concerns thus correctly reflected the realities beginning to bear down on the commercial world at that time.

Although Goode mentions that in America legislation was passed in order to do away with hindering non-assignment clauses, upon a closer inspection of his concerns, it is neither the approach that the English courts adopt nor the provisions in the Property Act that he finds unsatisfactory. Goode's primary concern was that he did not think it wise that a factoring firm or finance house should first have to make enquiries before receiving assignment of debts – as would be the case if the *ratio* in *Helstan Securities* was literally followed.

Goode's concerns were insightful, but he did not advance or purport to advance a radical solution or any kind of revamp of the law governing non-assignment clauses. He merely desired of the English courts to refrain from interpreting *Helstan Securities* literally.

Munday[157] questions the refusal of Croom-Johnson J to apply, as an analogy, the law governing the assignment of leases to the assignment of choses in action. Munday believes that there are equally strong commercial reasons for applying it to choses in action.[158]

Munday argues that the prohibition on assignment, as illustrated in *Helstan Securities Ltd v Hertfordshire County Council*, is a standard clause automatically included in a variety of contracts, specifically government contracts. Thus, firms employed by the government, especially small to medium firms, may temporarily fall on hard times if they cannot sell their debts to raise finance.[159] Further, as the argument goes,

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[157] RJC Munday 'Prohibition against assignment of choses in action' 1979 *Cambridge Law Journal* (vol 38) 50.

[158] Munday op cit 53. Many years later in *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* Lord Browne-Wilkinson, after careful consideration, also rejected this analogy.

[159] Munday op cit 53.

the ramifications of this are massive, since the annual turnover in England from the sale of debts runs into millions, and since obtaining finance in this manner was on the rise at that time.[160]

Munday looks further afield to American law where legislation was passed to allow those engaged in government contract work to finance their undertakings by assigning their debts.[161]

Munday is of the opinion that because *Helstan Securities Ltd v Hertfordshire County Council* directly upheld the non-assignment clause, serious implications await those in the commercial world.[162]

Munday's concerns echo those of Goode and it is remarkable to read that already in 1979 the annual turnover of factoring ran into millions of pounds. Considering the magnitude of this commercial industry, one would have thought that Munday might have suggested some drastic solutions to improve that situation for these commercial entities. Apart from mentioning the import of legislation in American law which prohibits the inclusion of non-assignment clauses, Munday, however, is not forthcoming with suggestions.

Allcock has considered the position of all the parties involved in a non-assignment contract and questions whether the answer lies in legislation.[163] He firstly contemplates the position as between the assignor and the assignee. Allcock claims that even if a non-assignment

[160] Ibid. In 1979 Munday recorded the annual turnover in England to be over £1000 million.

[161] Munday op cit 53.

[162] Ibid.

[163] B Allcock 'Restrictions on the assignment of contractual rights' 1983 *Cambridge Law Journal* (vol 42) 328.

clause can prevent an assignee from acquiring rights against the debtor, it cannot prevent rights arising between the assignee and the assignor.[164]

Secondly, he reflects upon the position as between the debtor and the assignee.[165] Unfortunately Allcock's discussion of the position is unhelpful in taking the matter any further. He reviews past cases on the issue and impliedly draws a conclusion.[166] For Allcock, therefore, a non-assignment clause does not deprive the assignee of all rights, but it can prevent him from enforcing rights directly against the debtor.[167]

Allcock also discusses the possibility of introducing legislation to create legal certainty. He asserts that most disputes revolve around the payment of a sum of money. The task, he says, is to weigh the commercial desirability of freely assignable debts against the harm or inconvenience that the debtor may suffer if the chose in action were freely assignable.[168] He submits that a monetary debt is not of such a personal nature and the difficulties an assignment might cause a debtor are not serious.[169]

He, regrettably, does not come to any express conclusions on whether or not legislation is needed in England, but he does mention that sound arguments can be raised both for and against such a solution, probably resulting in a polarisation of views.[170]

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[164] Allcock op cit 329-330. Surely this must depend on whether the assignee was aware of the non-assignment clause? If the assignee was aware of the non-assignment clause would an action for damages still arise?

[165] Allcock op cit 337-339. From his examination it appears that the assignee is only deprived of some rights, *viz*, the right to claim performance from the debtor. The assignee, however, does not lose the right to claim damages against the assignor.

[166] Allcock op cit 337-339.

[167] Allcock op cit 342.

[168] Allcock op cit 345.

[169] Ibid.

[170] Allcock op cit 346. He does not, however, elaborate on the possible arguments that may be raised.

Even though Allcock does not say it expressly, it appears as though he favours the idea that debts should be freely assigned. I say this because he discusses the position in America where legislation has been passed that renders ineffective any terms that prohibits the assignment of accounts.[171] Further, he brings his article to a close by stating that:

> It will be interesting to see whether the suppliers of commercial credit in England can prompt legislation similar to that in America making all debts assignable regardless of any restriction.[172]

Although these words do not strictly advocate the importation of legislation as a possible solution to the problem faced by factoring firms and finance houses, it is the closest thing to such an assertion that could be found in the writings of English academics.

Since the decision in *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd*, it seems as though the academics are more or less satisfied with the position as to the effect of an assignment made in contravention of a non-assignment clause.

Burrows, who wrote in 1994, one year after the House of Lords' decision in *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd*, maintains that if rights are assigned contrary to a prohibition, the assignment will be invalid as against the debtor.[173]

Relying on *Tom Shaw & Co v Moss Empires Ltd* and *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd*, Burrows adds that a prohibited assignment can still be effective as between assignor and assignee.[174]

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[171] Allcock op cit 345.

[172] Allcock op cit 346.

[173] AS Burrows *Chitty on Contracts* 27ed vol 1 (1994) 971.

[174] Burrows op cit 971-972.

Tettenborn,[175] who welcomed the decision of the House of Lords, has said only that he favours the finding that a non-assignment clause is not against public policy. He is of the opinion that legislation will do a better job of amending the law than the 'blunt instrument of public policy'.[176]

Wallace[177] wrote on the *ratio* in *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* in the context of damages, but unfortunately did not have any new ideas to add to the issue of the effect of a prohibited transfer.

Treitel's account, which was written in 1995, is very brief.[178] He states that if rights are assigned where the assignment is prohibited, not only would this amount to a breach of contract between the assignor and the debtor, but it would also be ineffective in that it would not give the assignee any rights as against the debtor. He adds, however, that the contract may still be binding between the assignor and the assignee.[179]

More recently, the account by Pettit, which was written in 2003, is also very brief. [180] He writes that an assignment made contrary to a contractual prohibition will make the assignment invalid as regards the debtor, but cannot operate to invalidate the contract as between the assignor and the assignee unless it is couched in the clearest of words.[181]

[175] A Tettenborn 'Loss, damage and the meaning of assignment' 1994 *Cambridge Law Journal* (vol 53) 24.

[176] Tettenborn op cit 25.

[177] IND Wallace 'Assignment of rights to sue: Half a loaf' 1994 *Law Quarterly Review* (vol 110) 42.

[178] Treitel op cit 610.

[179] Ibid.

[180] Pettit op cit 61.

[181] Ibid. Although even then it may still be invalid on the grounds of public policy as held in *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd*.

2.1.4 Conclusion

It seems as though the issue in English law is no longer the subject of hot debate. The earlier academics voiced their concerns in relation to the effect of non-assignment clauses in the commercial arena and hinted at a solution being found in legislation. The hints have fallen on deaf ears, as no such legislation was enacted.

Instead, it seems that the relief has come in the form of the authoritative decision from the House of Lords in *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd*. This long awaited elucidation on the issue as between private individuals in general contract is all good and well, but the *ratio* does not actually address or solve the problems in the commercial arena that academics earlier highlighted.

What is striking is that not much has been written about this simple observation. It begs the question whether all the English academics have given up striving for a more liberal state of affairs in the world of commerce? Or have they just accepted that commercial entities will be stuck with the outcome of *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd*?

Whatever the case may be, I am of the opinion that English law can offer little to assist South African law in overcoming the problems surrounding the *pactum de non cedendo*.

2.2 American law

2.2.1 American law of assignment in general

The early stages of the development of the law of assignment in the United States of America followed the same development as the English law of assignment as the American states received the English law as part of their common law.[182]

The history of assignment thus followed the same pattern of being invalid at first, then experiencing a relaxation in the courts of equity (which were influenced by mercantile custom), after which statutes were passed with the effect that choses in action were assignable.[183]

The only difference in the development is that different legislation was passed at slightly different intervals. The legislation had the effect of relaxing the old common law rule which eventually resulted in assignments being effectual in law and allowing the assignee to sue in his own name.[184]

Subsequently, the American Law Institute was formed, not to create new law, but to state the law as it already existed, in a document called the Restatements of Law.[185] It was a codification of common law judge-made legal principles that developed over time through *stare decisis* and covered various areas of law including contracts, torts, property and agency.[186] The Restatement of Contracts was published in 1923. It had

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[182] EA Farnsworth *Contracts* 3ed (1999) 707.

[183] WHE Jaeger *Williston on Contracts* 3ed vol 3 (1960) 7-16; Farnsworth op cit 704-707; JE Murray *Corbin on Contracts* revised ed vol 9 (2007) 133-137.

[184] Farnsworth op cit 707.

[185] Http://www.nationmaster.com/encyclopedia/Restatement (accessed on 27 January 2009); http://en.wikipedia.org/wiki/restatements_of_the_Law (accessed 27 January 2009); http://tarlton.law.utexas.edu/vlibrary/outlines/restatements.html (accessed on 27 January 2009).

[186] Ibid.

the effect of setting out a single set of rules without distinguishing between law and equity.[187]

By this time the assignment of choses in action was fully recognised at common law as it had made its way into the Restatements as an established legal principle accepted by judges without hesitation. This was followed by the Second Restatement of Contracts in 1952 which refined and updated the rules as set out in the previous Restatement.[188]

The Uniform Commercial Code (hereinafter referred to as UCC) is another development unique to American law. The UCC is a body of statutory law that governs certain types of contracts dealing with commercial transactions and payment.[189] It was developed by the American Law Institute and the National Conference of Commissioners on Uniform State Laws. These two organisations began drafting the UCC in the 1940's. A final draft was ready in the early 1950's and it was finally enacted in the 1960's.[190]

The UCC was created in the same spirit as the Restatements of Law as its purpose was to compile a single coherent document where all the legal principles on commercial transactions could be found. Further, different laws had developed in different states which had the result of making cross-state commercial transactions complicated and risky.[191]

The UCC thus endeavoured to unify the laws of commercial transactions across all the states of America. Slowly but surely each state (except for one or two) adopted the code, with only some making alterations.

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[187] Farnsworth op cit 707. See also footnote 20.

[188] Murray op cit 137.

[189] DE Litowitz *Perspectives on the Uniform Commercial Code* 2ed (2007) xi.

[190] Litowitz op cit xii-xiii.

[191] Litowitz op cit xiii.

Consequently, the United States of America has succeeded in unifying its commercial laws across the states.[192]

The current position in America generally favours the free assignability of contractual rights, so much so that no formalities, not even writing, need to be complied with in order to effect an assignment.[193]

2.2.2 Anti-assignment contracts

In American law, like South African law and English law, certain rights are prohibited from being assigned, either because they are against public policy,[194] or because they are prohibited by statute,[195] or because they are of a personal nature (*delectus personae*).[196]

American law also recognises *pacta de non cedendo*, although the terminology used is 'an anti-assignment clause' or 'anti-assignment contract'. The UCC as well as the Second Restatement of Contracts govern anti-assignment clauses. The relevant provisions are as follows:

- Regulation under the Uniform Commercial Code:

  - Article 2 of the UCC covers assignments of rights in contracts of a general nature. Article 2-210(1)(a) of the UCC provides that such

[192] Litowitz op cit xi.

[193] Murray op cit 147. Formalities need only be complied with if prescribed by statute or a contractual provision. See also DJ Brussel and EA Friedler 'The limits on assuming and assigning executory contracts' 2000 *American Bankruptcy Law Journal* (vol 74) 321 333: 'But in modern times, responding to the needs of commercial society, courts and legislatures have not only abandoned the medieval common law presumption against assignment of contract rights, they have reversed it. Today there is a strong presumption in favor of the free assignability of contract rights'.

[194] TL Leming 'Assignments' in *American Jurisprudence* 2ed vol 6 (2004) 186. In some states a chose in action arising out of a tort cannot be assigned before judgment.

[195] Leming op cit 199. The Uniform Consumer Credit Code states that buyer or lessee may not assign his earnings to a seller or lessor as payment or as security for payment of a debt arising from a consumer credit sale or a consumer lease.

[196] Leming op cit 170. An agreement to render professional services, such as those rendered by a physician, a lawyer or an architect cannot be assigned.

anti-assignment clauses are valid. Article 2 of the UCC, however, does not dedicate a section to the effect of an assignment in contravention of an anti-assignment clause when it appears in a general contract.

- Article 9, a completely separate article, was created to govern assignments of a commercial nature, resulting in different law being applicable to different types of assignments.[197] Article 9-406(d)(1) states that notwithstanding any agreement between the debtor and creditor (assignor) an anti-assignment clause will be ineffective if it prohibits assignment of an 'account' (as defined in the UCC), or if it prohibits the creation of a 'security interest' (as defined in the UCC), or if consent is required to effect an assignment of such an account or required to create such a security interest.

- Regulation under the Restatement of Contracts:

The Restatement of Contracts also covers assignments of rights in contracts of a general nature.

- Section 332(1) of the Second Restatement of Contracts provides that unless the circumstances indicate the contrary, a contract term purporting to prohibit assignment of 'the contract' is construed as prohibiting the delegation of performance of a duty or condition and does not prohibit the transfer of rights.[198]

- Section 332(2)(b) states that if a contract prohibits the assignment of rights and a contracting party assigns the rights regardless of the prohibition, then, unless a different intention is manifested, the

[197] See below for a further discussion regarding anti-assignment clauses appearing in commercial contracts. It is interesting to note that South African law does not distinguish between general or commercial cessions. See generally PM Nienaber 'Cession' in *LAWSA* 2ed vol 2 (2003); S Scott *The Law of Cession* 2ed (1991).

[198] *Restatement of the Law (Second)*: *Contracts* 2ed vol 3 (1981) 31-32.

debtor is entitled to damages for breach of the contract, but the breach does not render the assignment ineffective.[199]

- Section 332(2)(c) states that a contract prohibiting the assignment of rights is for the benefit of the debtor and, unless a different intention is manifested, the assignee is not prevented from acquiring rights against the assignor, nor is the debtor prevented from rendering performance as if there were no prohibition.[200]

Thus, the effect of an assignment in contravention of an anti-assignment clause is that ownership of the right passes to the assignee, forcing the debtor to perform to a stranger and leaving him only with a claim for damages against the assignor.[201] This, however, may not be the situation if the contract indicated that the intentions of the parties were otherwise.

The position seems simple enough, yet there are differences in the opinions of American academics. The more noticeable inconsistency is with regard to the lack of consensus at a judicial level concerning which interpretative approach should be adopted[202] as can be seen from the following discussions.

[199] *Restatement* op cit 32.

[200] Ibid.

[201] Although s322(2)(c) seems to leave open the possibility of the debtor performing to the creditor (assignor) as per the original agreement regardless of the cession and the assignee would presumably have a right of action against the creditor (assignor) to recover such performance.

[202] See J Anderson 'Contracts looking for "something": Minnesota's new rule for interpreting anti-assignment clauses in Travertine Corp. v. Lexington-Silverwood' 2006 *William Mitchell Law Review* (vol 32) 1435 1445 where she states that 'the rule for anti-assignment contracts is anything but consistent; the case law is filled with quirks and caveats that depend on the wording of the contract, any applicable statutes, and possibly public policies, apart from the general approach adopted by the state'.

2.2.2.1 General assignments

2.2.2.1.1 The approach of the courts[203]

In *Allhusen v Caristo Construction Corp*[204] Caristo Construction was a general contractor which subcontracted Kroo Painting Company for the carrying out of certain painting work in New York City public schools. The contract contained the following clause:

> The assignment by the second party [Kroo] of this contract or any interest therein, or of any money due or to become due by reason of the terms hereof without the written consent of the first party [defendant] shall be void.[205]

Kroo Painting Company subsequently assigned 'moneys due and to become due' to it under the contract to Marine Midland Trust Company of New York, which in turn assigned the rights to Allhusen. When Allhusen attempted to claim the moneys owing under the contract for work done by Kroo Painting Company, Caristo Construction objected on the basis that a valid anti-assignment clause had been included in the agreement between it and Kroo Painting Company.

In a unanimous judgment Froessel J pointed out that the effect of an anti-assignment clause is an issue that 'has troubled the courts' in many jurisdictions.[206] He further pointed out that the particular construction of

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[203] The older case law (before 1952) dealing with anti-assignment clauses has not been included in this discussion since much confusion existed as to their effect. The general tendency of the courts during this time was to decide a case on a kind of *ad hoc* basis, where the reasons for the effect of an anti-assignment clause appear almost arbitrary and without any adherence to a general approach or theory. It was only with the case of *Allhusen v Caristo Construction Corp* that a specific approach was adopted and subsequently followed by later courts. Thereafter, other specific approaches or theories have been developed and followed. *Allhusen v Caristo Construction Corp* and subsequent cases can thus be described as the case law reflecting the modern view and I have restricted my discussion accordingly. See Anderson op cit 1439-1440; Murray op cit 213-214.

[204] 303 N.Y 446 (1952) decided in the Court of Appeals in New York.

[205] Supra 499.

[206] Supra 450.

the anti-assignment clause in the provision in question had never in the past come before the court.[207]

Froessel J explained that in the past anti-assignment clauses have been held to be a 'personal covenant' or a promise whereby the promisee obtains a right to claim damages should the promisor breach his promise.[208] Alternatively, courts have often held that an anti-assignment clause is 'ineffectual' because unclear language has been used by the parties in the contract.[209]

The judge, however, emphasised that these past decisions merely indicate that in the absence of clear language stating otherwise, a claim for damages arises in favour of the debtor. He explained that an anti-assignment clause may indeed be enforced so that an assignment in contravention confers no rights on the assignee, but the contract language would have to be clear in order for a court to adopt this interpretation.[210] He added that *in casu*, the words used by the parties were in fact clear.

Froessel J held that:

> [W]hile the courts have striven to uphold freedom of assignability, they have not failed to recognize the concept of freedom to contract. In large measure they agree that, where appropriate language is used, assignments of money due under contracts may be prohibited. When 'clear language' is used, and the 'plainest words have been chosen', parties may 'limit the freedom of alienation of rights and prohibit the assignment'…. We have now before us a clause embodying clear, definite and appropriate language, which may be construed in no other way but that any attempted assignment…shall be 'void' as against the obligor [the debtor]. One would have to do violence to the language here employed to hold that it is merely an *agreement* by the

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[207] Ibid.

[208] Ibid.

[209] Ibid. For the sake of clarity 'ineffectual' in this context means without effect. Because the language of the parties is unclear, no effect can be given to a clause which may or may not amount to an anti-assignment clause.

[210] Supra 450.

> subcontractor not to assign. The objectivity of the language precludes such a construction.[211] [My emphasis]

It can clearly be seen that the court distinguished between a restriction on the right to assign (the promise not to assign), where a contravention thereof would lead to damages for breach of contract; and a prohibition on the right to assign where the right becomes non-transferable. Due to the latter being a restriction on the freedom of assignability, the contract would have to be couched in clear language.

The approach adopted in *Allhusen* seems to have been followed in *Pravin Banker Associates Ltd v Banco Popular Del Peru*.[212] Banco Popular was a bank owned by the Republic of Peru. Peru had borrowed funds from various foreign financial institutions in order to aid the functioning of Banco Popular. One of the foreign financial institutions from which Peru had borrowed was Mellon Bank, Pittsburgh, USA.

Banco Popular was subsequently unable to pay back its debts and entered into various negotiations with its creditors. Banco Popular and Mellon Bank agreed that the due date for repayment of the moneys borrowed was to be extended by 360 days (the so-called 'Mellon Letter Agreement'). The Mellon Letter Agreement contained the following clause:

> This letter agreement shall be binding upon you [Banco Popular], your successors and assigns, and shall inure to the benefit of us [Mellon], our successors, transferees and assigns. We [Mellon] may assign all or any part of our interest in this letter agreement to any financial institution.[213]

Due to Banco Popular's financial position it only managed to make interest payments to Mellon Bank. Mellon Bank subsequently assigned the right to

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[211] Supra 452.

[212] 109 F.3d 850 (1997) decided in the Court of Appeals in New York.

[213] Supra 856.

claim the debt from Banco Popular to Pravin Banker Associates Ltd. Initially Banco Popular began making interest payments to Pravin Banker, but later stopped payment altogether. Pravin Banker made a demand for the principal debt and the unpaid interest, but the payment was still not forthcoming.

Pravin Banker consequently instituted legal action and Banco Popular defended the action by arguing that the assignment to Pravin Banker was invalid on the basis that Pravin Banker was not a 'financial institution'.[214]

Referring to *Allhusen*, Calabresi J, who delivered the brief unanimous judgment declared that:

> [T]o reveal the intent necessary to preclude the *power to assign*, or cause an assignment violative of contractual provisions to be wholly void, [a contractual] clause must contain express provisions that any assignment shall be void or invalid if not made in a certain specified way.[215] [My emphasis]

Calabresi J explained that the language used in the Mellon Letter Agreement did not expressly restrict assignment in any manner. It in fact expressly permitted assignment to financial institutions, but did not limit assignment to these entities. An investigation into whether or not Pravin Banker was a financial institution was accordingly unnecessary and the assignment was held to be valid.[216]

Although the *Allhusen* approach was followed in *Pravin Banker* a difference can be noted. Both courts recognise the distinction between prohibiting the assignor's *right* to assign and extinguishing his *power* to assign, but there appears to be a disparity in the interpretation thereof.

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[214] Ibid.

[215] Ibid.

[216] Ibid.

Froessel J was of the opinion that if the contract states that the assignor shall not assign and 'clear language' or the 'plainest of words' are used the assignor's power to assign is contracted away and he can transfer nothing to the assignee. Calabresi J, on the other hand, stated that if the power to assign was to be extinguished the clause must state that a contravention thereof would be 'void' or 'invalid'. Thus one judge was satisfied to extinguish the power to assign by general words provided they are clear and plain, but the other judge required the words 'void' or 'invalid' to appear in the contract.

Herein lies the main problem experienced by the American courts: The vast majority agree that a difference exists between restricting an assignor's right to assign and his power to assign. The courts further agree that both alternatives are valid and that the effect of the former is an action for breach of contract and the effect of the latter is that nothing would pass to the assignee, since the right would be rendered non-transferable. The debate surrounds the *interpretation* of the contract.

Two interpretative theories have so far arisen: Requiring general words as decided in *Allhusen* or requiring specific words as decided in *Pravin Banker*.

Rumbin v Utica Mutual Insurance Co[217] is a typical example illustrating judicial inconsistency, as judges of the same jurisdiction, deciding upon the same set of facts, favoured different interpretations.

In this case Rumbin and Utica Mutual Insurance entered into a settlement agreement to resolve a personal injury claim whereby Rumbin was to receive a lump sum payment from Utica Mutual Insurance followed by a sequence of periodic payments over 15 years. The structured part of the settlement agreement was funded by another insurance company, Safeco Life Insurance, by way of an annuity contract.

[217] 757 A.2d 526 (2000) decided by the Supreme Court in Connecticut.

About six months after the conclusion of the settlement agreement Rumbin lost his employment and could not afford to pay the mortgage on his home. As a solution to his financial difficulties, he assigned his right to the remaining annuity payments under the settlement agreement to JG Wentworth.

Safeco objected to the assignment, *inter alia*, on the basis that the annuity contract contained a clause stating that '[n]o payment under this annuity contract may be… assigned…in any manner by the [plaintiff]'.[218]

The appeal was decided by five judges, two agreeing with the majority judgment delivered by Vertefeuille J and one agreeing with the minority judgment handed down by Norcott J.

Relying on the Second Restatement of Contracts, Vertefeuille J stated that parties may make use of express language in a contract to limit assignments and such anti-assignment clauses would generally be upheld by the courts.[219] He explained that:

> In interpreting antiassignment clauses, the majority of jurisdictions now distinguish between the assignor's 'right' to assign and the 'power' to assign (modern approach). For example, in *Bel-Ray Co. v. Chemrite (Pty.) Ltd.,* 181 F.3d 435, 442 (3d Cir.1999), the United States Court of Appeals for the Third Circuit recognized that numerous jurisdictions followed the general rule 'that contractual provisions limiting or prohibiting assignments operate only to limit [the] parties' *right* to assign the contract, but not their *power* to do so, unless the parties manifest an intent to the contrary with specificity…. The court acknowledged that contracting parties could limit the *power* to assign by including an assignment provision [that] generally state[s] that nonconforming

[218] Supra 529. It must be stated for the sake of completeness that Utica Mutual Insurance was cited as a party to the case, but it was the structured part of the settlement agreement that was assigned – the part that was funded by Safeco. Further, Utica Mutual Insurance never appeared in the court *a quo*, nor explained its failure to appear. Utica Mutual Insurance also did not challenge the appeal nor was it a party thereto; hence Safeco appealed the decision of the court *a quo*.

[219] Supra 531.

> assignments (i) shall be 'void' or 'invalid,' or (ii) that the assignee shall acquire no rights or the nonassigning party shall not recognize any such assignment.' *Id*., at 442. Without such express contractual language, however, "the provision limiting or prohibiting assignments will be interpreted merely as a covenant not to assign.... Breach of such a covenant may render the assigning party liable in damages to the non-assigning party. The assignment, however, remains valid and enforceable against both the assignor and the assignee. [220]

Vertefeuille J dedicated about four and half pages of his judgment to citing case law and quoting the relevant extracts that supported his view. A quotation of note was from *Pravin Banker Associates Ltd* where it was held that to preclude the power to assign, a contractual clause must expressly state that an assignment in contravention would be 'void' or 'invalid'.[221] *Pro Cardiaco Pronto Socorro Cardiologica, SA v Trussell*,[222] was also referred to where the court held that 'assignments are enforceable unless expressly made void'.[223]

This approach, which Vertefeuille J called the 'modern approach' has apparently been adopted by the 'majority of jurisdictions' in the courts of America as a result of its 'evenhandedness'.[224] The modern approach, he argued, allows for assignability of rights together with full protection of the debtor by way of damages should he suffer a loss. Should the parties have a different intention the right may be rendered non-transferable and an assignment in contravention of an anti-assignment clause would be ineffective.[225]

The judge pointed out that the modern approach is not adopted by some courts, where anti-assignment clauses are upheld if a general intention to

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[220] Ibid.

[221] Supra 532.

[222] 863 F.Supp.135 138 (1994).

[223] Supra 532.

[224] Supra 534.

[225] Supra 534 read with 535.

restrict or prohibit assignment has been ascertained.[226] He was in agreement in so far as that parties are free to contract to exclude assignment if 'appropriate contractual language' is used.[227]

The judge, however, did not agree as to the contractual language that must be employed to exclude assignment. For the power to assign to be extinguished he was of the opinion that very specific language must be used – that is – the parties must actually stipulate that an assignment in contravention would be 'void', 'invalid' or 'otherwise ineffective'.[228] A prohibition in general terms would not be sufficient and would in his opinion only restrict the right to assign leading to an action for damages.[229]

Due to the fact that the anti-assignment clause in the annuity contract was couched only in general terms: '[n]o payment under this annuity contract may be… assigned…in any manner by the [plaintiff]', Vertefeuille J decided that only the right to assign was restricted and the power to assign had not been extinguished, as no express language in accordance with the modern approach had been used.[230]

Consequently, the assignment by Rumbin to Wentworth was valid and enforceable and Safeco was invited to sue Rumbin for any damages that it may have sustained as a result of the breach of the anti-assignment clause.[231]

In the minority judgment, Norcott J recognised that contractants may validly agree to limit free assignability, but held that the majority did not,

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[226] Supra 533.

[227] Ibid.

[228] Supra 533 read with 532 and all the cases relied on therein, *inter alia*, *Jacquette v CNA Insurance Cos*, civil action 98-1601 (N.H.P) (D.N.J November 16, 1998) [unreported].

[229] Supra 533. According to Vertefeuille J a prohibition in general terms would be, for example, '[i]nterest in this policy may not be assigned without our written consent'.

[230] Supra 535.

[231] Ibid.

inter alia, strictly adhere to the Second Restatement of Contracts. He explained that the default position in the Restatements is that an assignment contrary to an anti-assignment clause would give rise to damages 'unless a different intention is manifested'. The debate thus involved an interpretation of this intention. [232]

Norcott J acknowledged that such an intention can either restrict the right to assign or extinguish the power to assign and had no quarrel as to the effect of each alternative. He, however, did not agree with the interpretative standard that the majority used in order to determine into which category the contractants' intention falls.[233] According to the judge:

> [T]hat standard imposes on contracting parties an illogical and arbitrary set contractual mantra that must be recited…[234]

The judge, while admitting that cases supporting the majority view do exist, pointed out that there were also many cases which supported his view. He also dedicated some time to consider the *ratio* of these cases. A case of note that did not insist on the use of particular phraseology, but which upheld the anti-assignment clause where the language used by the parties was clear and unambiguous was *Henderson v Roadway Express*,[235] where it was explained that 'the plain language… clearly indicates that the parties intended to forbid [assignment of the rights]'.[236] *Portland Electric & Plumbing Co. v Vancouver*[237] was another case illustrating this, where it was held that:

[w]hen a contract prohibits assignment in 'very specific' and 'unmistakable terms' the assignment will be void against the obligator [the debtor].[238]

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[232] Supra 537 relying on s332(2)(b) of the Second Restatement of Contracts.

[233] Supra 537.

[234] Ibid.

[235] 720 N.E.2d 1108 1110 (1999).

[236] Supra 538.

[237] 627 P.2d 1350 (1981).

[238] Supra 538.

Norcott J explained that 'at the heart' of the rule of freedom of contract is that different parties may employ different language to express their intentions, but provided such language is clear, a court is bound to enforce such intentions.[239] He added that the imposing of 'formulaic restraints' on the contract language which some courts do and which the majority has done 'flies in the face of decades of our jurisprudence'.[240]

The judge therefore concluded that the words of the anti-assignment clause in the annuity contract were 'sufficiently clear' and 'unambiguous' so that the assignment to Wentworth in contravention thereof was ineffective.[241]

Norcott J makes some good points, but he fails to address one issue. By his own admission he finds favour with the view that an assignment can either restrict the right to assign or extinguish the power to assign and he agrees with the effect thereof. He proceeds to explain that in order to extinguish the power to assign 'formulaic' or 'contractual mantra' (like the words 'void', 'invalid' or 'ineffective') need not be recited by the parties, they need only clearly and plainly express their intention that assignment is not to occur.

How then, according to his approach, would the parties only restrict the right to assign? If the parties need only employ general language to extinguish completely the power to assign, how much more general should their language be, or how should their intentions be couched only to restrict the right to assign?[242]

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[239] Supra 539.

[240] Ibid.

[241] Supra 540.

[242] The court in *In re Kaufman* 37 P.3d 845 (2001) decided by the Supreme Court of Oklahoma provides a short discussion of the two different interpretative approaches thus far discussed and favours the *Allhusen* approach, or the approach adopted by the minority in *Rumbin v Utica* supra, but does not address this issue.

In *Bank of America, NA v Moglia*[243] yet a different interpretative approach was adopted. In this case a company called Outboard Marine Corporation was bankrupt and in the process of being liquidated. Among its assets, was a rather valuable asset worth 14 million US Dollars known as a 'rabbi trust'.[244] The trustee of Outboard's bankrupt estate attempted to attach the assets under the rabbi trust for distribution amongst the unsecured creditors.

The Bank of America, however, objected to this on the basis that, *inter alia*, the assets under the rabbi trust were assigned to it as security for credit which was extend to Outboard. The trustee argued that the security assignment was void since the rabbi trust contained an anti-assignment clause: '[Outboard] shall not create a security interest in the Trust Corpus in favour of the Executives, the Participants or any creditor'.[245]

Posner J, delivering the unanimous judgment, recounted the Bank of America's line of reasoning. The bank argued that because the rabbi trust did not specifically state that the creation of a security interest in the assets would be void or ineffectual, the power to assign had not been extinguished. Outboard could still validly assign the assets as security, although an action for damages would arise in favour of the creators of the trust.[246]

To this the judge's response was as follows:

> Nothing would have been added to the trust agreement but *empty verbiage* had it said 'and not only is Outboard forbidden to create a security interest in these assets in favor of any creditor, but if it tries to do so its action shall be null, void, and of no effect.' Of course, if Illinois required those *magic words*, as many states still do, see *Rumbin v. Utica*… and cases cited there, to rebut the

[243] 330 F.3d 942 (2003) decided by the Court of Appeals in Illinois.

[244] Supra 943.

[245] Supra 946.

[246] Supra 947.

> presumption of nonassignability, then Bank of America could argue persuasively that it had relied on their absence when it signed the security agreement. But Illinois does not require them.[247] [My emphasis]

Posner J explained that Illinois follows the 'modern view' as expressed in the Second Restatement of Contracts where an anti-assignment clause is unenforceable against an assignee 'unless a different intention is manifested'.[248] 'Magic words' the judge held, are not required. Relying on comment 'c' in the Restatement, he lastly added that:

> Where there is a promise not to assign but no provision that an assignment is ineffective, the question whether breach of the promise discharges the obligor's duty *depends on all the circumstances*.[249] [My emphasis]

Posner J accordingly considered 'all the circumstances' and the circumstance which convinced him on the outcome was that the alternative remedy would be damages for breach of contract. He held that the anti-assignment clause should be upheld and that the Bank of America consequently had no security interest in the assets under the rabbi trust.

It is interesting to note that the court in *Bank of America v Moglia* criticised the modern approach (as discussed in *Pravin Banker* and *Rumbin v Utica*) as being a 'magic words' approach and instead labelled its approach as the 'modern view'. Further, it can be seen that the court leans more in favour of the *Allhusen* or *Rumbin v Utica* minority approach than the now-termed magic words approach.

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[247] Supra 948.

[248] Ibid.

[249] Ibid.

This case, like many of the others, relied on the Second Restatement of Contracts, except Posner J specifically mentions comment c.[250] Comment c reads as follows:

> The rules stated in this Section do not exhaust the factors to be taken into account in construing and applying a prohibition against assignment. 'Not transferable' has a clear meaning in a theatre ticket; in a certificate of deposit the same words may refer to negotiability rather than assignability. Where there is a promise not to assign but no provision that an assignment is ineffective, the question whether breach of the promise discharges the obligator's duty *depends on all the circumstances*.[251] [My emphasis]

It appears that the Illinois approach or so-termed 'modern view' is in line with the guidelines of the Restatements, although the court may have narrowly construed the meaning of 'all the circumstances'. Was an action for damages as an alternative remedy, such a circumstance as envisaged in comment c? Surely the circumstances referred to in comment c are the surrounding circumstances of the particular facts of the case, gathered not only from written agreements and documents, but also from witness testimony?

To sum up, all the cases from *Allhusen* are seen as following a modern approach, since a distinction between restricting the right to assign and extinguishing the power to assign is clearly made, with both having a different effect. The case law indicates judicial uncertainty as to the interpretative methods or approaches to be adopted when applying this modern approach. Three interpretative approaches can be distinguished:

First, the *Allhusen* approach or *Rumbin v Utica* minority where only general terms are sufficient to extinguish the power to assign, provided the general terms are plain, clear and unambiguous. Secondly, the so-called

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[250] In the Restatements it is customary for there to be comments, examples and references to decided cases to illustrate the functioning or meaning of the various sections.

[251] *Restatement* op cit 33.

'magic words' approach where the power to assign is only considered to be extinguished if specific words are used, for example, that an assignment in contravention would be 'void', 'invalid' or 'of no effect'. Thirdly, the approach used by the court in Illinois in *Bank of America v Moglia*, the so-called 'Illinois approach', where such a strong emphasis should not be placed on specific words used or not used by the parties, and all the surrounding circumstances and factors need to be taken into account when determining whether or not the power to assign has been extinguished.

2.2.2.1.2 Academic opinion

It has been noted that anti-assignment contracts have caused confusion over the years stemming from the *ratio* of the older cases. [252] As opposed to these outdated principles, the modern law of assignment favours the free assignability of rights and frowns on restrictions or prohibitions thereof.[253] Parties may, of course, agree to prohibit assignment, but such agreements are usually narrowly construed.[254]

Academics have pointed out that American courts, relying on the Second Restatement of Contracts, have distinguished between two categories of anti-assignment clauses. Either an anti-assignment clause has an ambit only wide enough to create a duty not to assign by the assignor making a promise to that effect, or the ambit may extend further to the assignor completely surrendering the power to assign.[255]

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[252] Murray op cit 213.

[253] Murray op cit 214.

[254] Murray op cit 214. See also Farnsworth op cit 717 and footnote 28. He uses the case of *Munchak Corp v Cunningham* 457 F.2d 721 (1972) as an example. In this case a contract of a professional basketball player prohibited the club from assigning its rights to another club without the basketball player's consent. The club subsequently assigned its rights to another owner of the club. On determining the validity and effect of the assignment, the court held that the anti-assignment clause did not prevent the club from assigning its rights to another owner of the same club.

[255] Murray op cit 215. See also Anderson op cit 1440-1442.

Although this approach to anti-assignment clauses is the general approach that all courts use, when using this approach, the courts have shown inconsistency when deciding if an anti-assignment clause sufficiently manifests an intention to relinquish the power to assign, or whether it merely constitutes a duty not to assign.[256]

It has rightly been observed that perhaps fault is not to be found with the courts in its inconsistency in applying different interpretative approaches, as the Second Restatement of Contracts only speaks of 'unless a different intention is manifested'[257] and that:

> It is unclear what kind of evidence should be required to demonstrate the manifestation of a different intention. In particular, a question exists whether attention should be focused primarily on the precise language of the clause at issue - drawing very fine distinctions among, for example, clauses that merely state that assignments are 'prohibited', clauses that instead describe assignments as 'void' or 'invalid', and clauses which may specify that non-assignment is a condition precedent of the obligor's duties - or instead should be focused more upon the circumstances surrounding negotiations and the light they shed upon probable intentions of the parties.[258]

Further, each interpretative approach may be criticised for different reasons. The *Allhusen* or *Rumbin v Utica* minority approach has been criticised for not being realistic enough.[259]

Regardless of the criticisms and shortcomings of this approach, it is apparently a very popular and frequently-used approach.[260]

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[256] Anderson op cit 1442.

[257] GS Crespi 'Selling Structured Settlements: The Uncertain Effect of Anti-Assignment Clauses' 2001 *Pepperdine Law Review* (vol 28) 787 799.

[258] Crespi op cit 799-800.

[259] Notably by G Gilmore 'The commercial doctrine of good faith purchase' 1954 *Yale Law Journal* (vol 63) 1057 1119, where Gilmore stated that this approach is 'a monument to the purest type of conceptualism, untainted by a breath of the workaday world'.

[260] Anderson op cit 1441. See Chapter 6 for a further discussion.

The ‘magic words’ interpretative approach has been said to give effect to s332(2)(b) of the Second Restatement of Contracts, as that subsection begins by stating ‘unless a different intention is manifested’. Accordingly, if the magic words are used, then such a different intention has been manifested.[261]

This approach has also met with some criticism,[262] and one such objection has been that a court should not interpret an anti-assignment clause solely by looking at ‘fine verbal distinctions’ of the contract language.[263] Often anti-assignment clauses are standard clauses and not ‘individually tailored’ to the parties, neither are these standard clauses meaningful to the ‘particular circumstances’ of the parties.[264]

From an American law perspective I would imagine the magic words approach to be a clear, certain and simple approach. If the parties intend the assignment to be ineffective they include the magic words, if they intend the assignment to constitute merely a breach giving rise to damages, then they do not include the magic words. The only problem I foresee is that parties who are ignorant of this would be forced to bear consequences that they did not intend or agree to.[265]

The ‘Illinois approach’ as discussed in *Bank of America v Moglia*, which is said to express the modern view, follows the Second Restatement of Contracts exactly. Magic words are not required and a ‘different intention’ being present depends upon all the circumstances.[266]

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[261] Murray op cit 216. See also footnote 15.

[262] As can be seen from the cases, *Bank of America v Moglia* described the magic words approach as ‘empty verbiage’ and consequently rejected it. The minority in *Rumbin v Utica* described the magic words approach as an ‘illogical and arbitrary set of contractual mantra’ and as imposing ‘formulaic restraints on contract language’.

[263] Crespi op cit 815.

[264] Crespi op cit 815-816.

[265] See Chapter 6 for a further discussion.

[266] Murray op cit 216-217.

This is probably the more flexible approach as it views the situation holistically and is guided not only by the words or contract language used by the parties, but also by the surrounding circumstances.[267]

Murray's comments on the general position as can be seen in the following passage:

> The case law reflects an accommodation of the tensions between a strong policy of free assignability and the classic desire to fulfil the intention of the parties by a traditional common law approach of insisting upon clear manifestations of intention in the form of contract language if the favored policy of avoiding restrictions on assignments is to be overcome.[268]

Similarly, Anderson holds the view that:

> In general, restraints on alienation, such as assignments, are disfavored because they increase transaction costs, keeping property out of the hands of the user to whom it is most valuable. Because the obligor [the debtor] is unlikely to incur extra expense, the modern approach of enforcing assignments unless the parties expressly agreed to invalidate them makes economic sense…. [T]he modern approach [in general, that is, without any specific interpretative approach] allows contracting parties who truly believe they would be disadvantaged by an assignment to bargain for and enforce an anti-assignment clause. The modern approach does not infringe on the parties' freedom to contract, it executes what the parties literally agreed. On occasion, the rule might upset the expectations of obligors [debtors] who believed the other party did not have the power to assign the contract, but if the obligor [debtor] actually suffered any injury, those damages still would be recoverable.[269]

2.2.2.2 Commercial assignments

2.2.2.2.1 The approach of the courts

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[267] See Chapter 6 for a further discussion.

[268] Murray op cit 217.

[269] Anderson op cit 1461-1462.

One may have though that American courts would have objected to article 9-406(d)(1) of the UCC, as parties are stripped of their freedom of contract. This, surprisingly, is not the situation. From the case discussions that follow it will be seen that article 9-406(d)(1) has been well received by the American courts and they have been eager to clarify its operation and praise its overall purpose.

In *CGU Life Insurance Co of America v Metropolitan Mortgage & Securities Co*,[270] Mr and Mrs Lytle entered into a settlement agreement with Home Insurance Co (acting on behalf of DP Eddy and Delaney Moving Inc) whereby they were to receive an immediate lump sum and period payments over a certain time span. In terms of the settlement agreement Home Insurance Co had the right to effect a qualified assignment of its liability to make the period payments to CGU Annuity Service Corporation. CGU Annuity Service Corporation, in turn, was entitled to purchase an annuity policy from CGU Life Insurance Company of America in order to fund its obligation.

Although Home Insurance Co was entitled to make an assignment under the settlement agreement, Mr and Mrs Lytle were not permitted to do so:

> Plaintiffs acknowledge that the Periodic Payments cannot be accelerated, deferred, increased or decreased by the Plaintiffs or any Payee; nor shall the Plaintiffs or any Payee have the power to sell, mortgage, encumber, or anticipate the Periodic Payments, or any part thereof, by assignment or otherwise.[271]

About a year after the settlement agreement was concluded the Lytle's experienced some financial difficulties and they required an immediate lump sum. They consequently assigned the right to claim some of the periodic payments to Woodbridge Sterling Capital LLC, which subsequently assigned its rights to Metropolitan Mortgage & Securities Co.

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[270] 131 F.Supp.2d 670 (2001) decided in the District Court in Pennsylvania.

[271] Supra 673.

Sometime thereafter the Lytle's stopped forwarding the periodic payments to Metropolitan and the company took legal action. The court *a quo* held that the assignment was valid and enforceable and ordered that Metropolitan was entitled to collect the payments due and owing directly from CGU Life Insurance Company of America.

CGU Life Insurance Company of America appealed the decision on the basis that the assignment to Woodbridge and then to Metropolitan was invalid due to the anti-assignment provision contained in the settlement agreement. Metropolitan, on the other hand, argued *inter alia* that the assignment to it should be upheld since the anti-assignment clause in the settlement agreement was unenforceable under the Uniform Commercial Code.

Joyner J, who delivered the decision in this case, reflected on article 9-318(4) of the UCC:

> A term in any contract between an account debtor and an assignor is ineffective if it prohibits assignment of an account or prohibits creation of a security interest in a general intangible for money due or to become due or requires the consent of the account debtor to such assignment or security interest.[272]

CGU Life Insurance Company of America asserted that certain transactions are excluded from the application of article 318(4), one being when an interest or claim in or under an insurance policy is transferred, barring, however, the transfer of the proceeds thereof.[273]

The judge pointed out that article 9-104 of the UCC excludes about 12 types of transactions and such exclusions could broadly be categorised as follows: Firstly, transactions subject to 'overriding governmental interests'.

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[272] Supra 676-677. This section is replaced by article 9-406(d) in the revised version of the UCC. The corresponding provision in Pennsylvania law is 13 Pa.C.S.A s9318(d).

[273] Supra 677. Article 9-104 [9-109(d)(8) of revised UCC] equivalent to13 Pa.C.S.A s9104(7).

Secondly, transactions which are 'nonconsensual' and thirdly, transactions which are '*out of mainstream commercial financing*'.[274] [My emphasis]

The judge held that the transaction in this case fell into the third category of exclusions and it was thus only necessary to determine whether it could be argued that the period payments could be construed as 'proceeds'. The period payments to which the Lytle's were entitled were originally funded by a liability insurance policy, where consent had then been given to fund under an annuity policy after an assignment had occurred. In terms of applicable Pennsylvania law,[275] although the Lytle's had an interest under the insurance policy, no security interest in the payments or annuity existed. It was for this reason that Joyner J concluded that the periodic payments did not amount to the meaning of 'proceeds'. The anti-assignment clause was accordingly not rendered ineffective by the article 9 of the UCC.

Notwithstanding the exclusions in the other two categories, the third category of exclusions as mentioned by the court makes it patently clear what type of transactions article 9-406(d)(1) seeks to cover – it only affects a specific type of transaction. Article 9-409(d)(1) will not feature in a transaction between parties where 'mainstream commercial financing' is not the focus.

This sentiment was unmistakably echoed in *Riley v Hewlett-Packard Co.*[276] In this case Clover Technologies Inc and Hewlett-Packard entered into a sub-contractor agreement whereby Clover Technologies was to provide labour, materials and technical services to Hewlett-Packard. The contract contained an anti-assignment clause that read as follows:

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[274] Supra 677.

[275] Supra 677, 13 Pa.C.S.A s9306(a): '…whatever is received upon the sale, exchange, collection or other disposition of collateral or proceeds. Insurance payable by reason of loss or damage to the collateral is proceeds except to the extent that it is payable to a person other than a party to the security agreement. Money, checks [cheques], deposit accounts and the like are "cash proceeds". All other proceeds are "noncash proceeds".'

[276] 36 Fed.Appx. 194 (2002) decided in the Court of Appeals in Michigan.

> Unless otherwise agreed in writing by HP, Subcontractor shall not assign its rights or delegate its responsibilities under this Agreement. Any purported assignment or delegation by Subcontractor, including the attempted subcontracting of all or any portion of the work to provided [sic] under this Agreement, shall be null and void.[277]

During the existence of the subcontract, disputes arose as to whether Hewlett-Packard was liable to pay for certain work performed by Clover, as Hewlett-Packard argued that some of the work carried out was beyond the scope of their agreement.

Sometime during this dispute, Riley, the majority shareholder, sold Clover to Ameritech. The uncollected accounts receivable were assigned to Ameritech as part of the purchase. The parties agreed that any accounts receivable not collected within 15 months would be re-assigned to Riley.

After this time had elapsed the Hewlett-Packard accounts receivable remained uncollected due to the dispute that existed before Clover was sold, and the accounts receivable were re-assigned to Riley. Riley subsequently sued Hewlett-Packard for payment, yet Hewlett-Packard, relying on the anti-assignment clause, objected to liability.

The court held that the anti-assignment clause had clearly been violated and the only remaining issue was whether there was anything in law that would render it unenforceable. Riley argued, *inter alia*, that the anti-assignment clause was invalided by article 9-318(4) of the UCC. The court thus had to determine whether the anti-assignment clause fell within the ambit of article 9.[278]

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[277] Supra 194-195.

[278] This section is replaced by article 9-406(d) in the revised version of the UCC. The equivalent section in Michigan law is Mich. Comp. Laws s440.9318(4).

Upon recounting article 9-318(4) of the UCC, the court pointed out that an anti-assignment clause will be rendered ineffective if the assignment of an account is prohibited or if the creation of a security interest in a general intangible is prohibited, or if consent is required to make an assignment or create a security.[279]

Article 9-318(4) of the UCC is subject to certain exclusions which can be found in article 9-104. According to the court, article 9-318(4) does not apply to a 'sale of accounts' or 'chattel paper' when they are sold as a part of a business.[280] The court held that:

> The purpose of the…exclusions was to ensure that *Article 9 did not become entangled with transactions that have nothing to do with commercial financing.* The sale of accounts attached to the sale of a business differs widely from, for example, the sale of accounts to factoring companies that is the meat and drink of the accounts receivable market.[281] [My emphasis]

The court consequently came to the conclusion that the anti-assignment clause was not rendered ineffective by article 9-318(4) of the UCC.

In *Bank of America N.A. v Moglia,*[282] it will be remembered that Outboard Marine Corporation was bankrupt and there was a dispute between the trustee of the bankrupt estate and the Bank of America over certain assets under a so-called 'rabbi trust' which Outboard had assigned to the bank as security. The rabbi trust, however, was subject to an anti-assignment clause, and in addition to other assertions, the Bank of America argued that the anti-assignment clause was ineffective due to article 9-406(d)(1).

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[279] Supra 196.

[280] Supra 197. The exclusion being article 9-109(d)(4) under the revised version of the UCC. The equivalent section in Michigan law is Mich. Comp. Laws s440.9104(f).

[281] Supra 197.

[282] Supra (discussed above).

Posner J remarked that this argument was 'thoroughly frivolous'.[283] Surely it was obvious to Bank of America that the rabbi trust could not be seen as an 'account' so as to bring it under article 9-406(d)(1) of the UCC? The judge nonetheless took the opportunity to clarify the position as follows:

> Accounts and other simple written promises to pay are important collateral in modern commercial transactions, and their value as collateral is maximized by stripping them of encumbrances, such as an antiassignment clause unlikely to be noticed in the haste of transacting.[284]

Posner J held that the trust was not the kind of instrument that could be brought under article 9-406(d)(1), and besides that, the trustee could not have been seen as Outboard's debtor.

The 'frivolous' argument of course failed, but this *dictum* confirms that American courts accept that anti-assignment clauses appearing in commercial transactions are ineffective.

2.2.2.2.2 Academic opinion

As mentioned above, article 2 of the UCC covers anti-assignment clauses concluded in contracts of a general nature. Article 9 of the UCC covers anti-assignment clauses concluded in contracts of a commercial nature. The most common of these commercial contracts is the factoring contract.

This occurs when the accounts of a business are ceded to a factoring house or finance company for the purpose of commercial financing or as security for a loan. In other words instead of a business enforcing its own claims ('book debts' or 'accounts') against its debtors, it cedes them to a factoring house who immediately provides the business with a percentage of their face value. In this way the business can obtain a quick source of finance. The factoring house, now the owner of the accounts,

[283] Supra 948.

[284] Supra 948-949.

consequently enforces them against the debtors for their full value thereby making a profit. [285]

Article 9 provides that no matter how clearly an anti-assignment clause is phrased in a contract falling within the ambit of article 9, it will be rendered ineffective.[286] Murray notes that the American legislators have drafted article 9 in this manner as a 'modern credit economy' requires contractual rights to be freely assignable in order to function properly. [287]

Murray explains the situation as follows:

> When goods are sold to consumers or merchant buyers on credit, the seller has a contractual right called an 'account' that can be assigned. An 'account' is defined as a right to payment of a monetary obligation, earned or not yet earned by performance, for property that has been or is to be sold, leased, licensed, assigned, or otherwise disposed of, for services rendered or to be rendered, or for other obligations.[288] Typical sellers have neither the means nor the expertise to finance the sales they must make on credit. Sellers require funds to pay for their inventories and other expenses. They are not in the finance business. Their principal assets are accounts – the monetary obligations of their buyers that will mature over a certain period. The sellers borrow money from commercial lenders to whom they provide their accounts as collateral to secure their repayment of the loans.

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[285] See Chapter 5 for a more detailed explanation of the definition and operation of the factoring contract. See Murray op cit 219-220: 'The paradigmatic assignment of accounts under Article 9 is the sale of accounts to a "factoring" firm that buys accounts at a discount, thereby assuming the risks of delay or loss in their collection. As the lifeblood of commercial financing, such factoring assignments of accounts are precisely the kind that may not be prohibited under Article 9. Prohibiting assignments of the rights to accounts that are part of the sale of one's business, however, does not interfere with commercial financing'.

[286] Farnsworth op cit 718; Murray op cit 218.

[287] Murray op cit 149.

[288] Murray op cit 149 footnote 4. The other obligations include a right to payment for a policy of insurance issued or to be issued, a secondary obligation incurred or to be incurred, for energy provided or to be provided, for the use or hire of a vessel under a charter or other contract, obligations arising from the use of a credit or charge card or information contained on or for use with the card, winnings in a lottery or other state-sponsored gaming, and health care insurance receivables. The definition of 'account' does *not* include rights to payment evidenced by chattel paper or an instrument, commercial tort claims, deposit accounts, investment property, letters of credit or rights thereunder, or rights to payment for money or funds advanced or sold other than rights out of the use of a charge or credit card. See article 9-102(2).

> They may grant security interests in these accounts to their lenders, but they will often sell (assign) these accounts. Such a financing arrangement is often carried on for many years between the same parties.[289]

Thus, an account, provided it falls within the definition of article 9, may not be prohibited from being assigned. If an account is prohibited from being assigned, such an assignment is rendered ineffective by article 9-406(d).[290]

It has also been pointed out that should anti-assignment clauses applicable to factoring contracts or mainstream commercial financing transactions be enforced, it would have a 'chilling effect' on the economy as it would require an assignee to scrutinise each and every contract it acquires to determine if the rights thereunder are subject to anti-assignment clauses. This, it is argued, is impractical if rights are assigned in bulk.[291] It has been further argued that any loss which a debtor may suffer due to the violation of the anti-assignment clause seems not only preventable, but 'highly speculative' and 'probably outweighed by the benefit' of assignability.[292]

Anderson makes the noteworthy observation that because American courts try to uphold anti-assignment clauses in the interest of giving effect to the intention of the parties, they will not willingly invalidate anti-assignment clauses in the absence of legislation specifically invalidating the clauses.[293] Thus article 9 does not have as its purpose the interference of anti-assignment clauses when appearing in contracts of a

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[289] Murray op cit 149-150.

[290] In the revised post-1999 version of the article 9-406(d) has replaced article 9-318(4).

[291] BD Hull 'Symposium on revised article 1 and proposed revised article 2 of the Uniform Commercial Code: Harmonization of rules governing assignments of right to payment' 2001 *Southern Methodist University Law Review* (vol 54) 473 483.

[292] Ibid.

[293] Anderson op cit 1444.

general nature. An anti-assignment clause will only be ineffective due to article 9 under limited and specific circumstances.

2.2.3 Conclusion

American law differentiates between assignments involving general contracts, which are usually once-off transactions and assignments between business and factoring houses or finance companies, which serve a 'continuous commercial financing purpose'.[294]

The former is governed by the Second Restatement of Contracts and by Article 2 of the UCC. Such anti-assignment clauses are usually valid and their effect depends upon which interpretative approach a court in a particular state prefers. This uncertain variable matters little, as although none of the three approaches are perfect, all are workable and relatively equitable, and one can be confident that justice will prevail in every case, regardless of the approach adopted.

The latter type of assignment is governed by article 9 of the UCC and is incapable of being prohibited or restricted in any way. Such anti-assignment clauses are accordingly invalid and ineffective. The treatment of anti-assignment clauses in this instance is extremely fitting, as the commercial financing industry in America relies on assignment to function – without assignment the commercial financing industry would not exist. It would be ludicrous, to say the least, to impede the very mechanism that drives this industry.

The manner in which American law differentiates between the types of assignments and deals with them accordingly is very effective.

Earlier it was mentioned that South African law does not distinguish between general and commercial cessions. Perhaps the problems in the

[294] Murray op cit 220.

South African law of *pacta de non cedendo* can be remedied by looking to American law.[295]

[295] See chapter 6 for further discussion.

CHAPTER THREE

THE *PACTUM DE NON CEDENDO* THROUGH THE CASES

In this Chapter the *pactum de non cedendo* as it appears in South African case law will be considered.

3.1 Early South African cases

The first case in South African courts dealing with a *pactum de non cedendo* was the case of ***South African Railways v The Universal Stores Ltd***.[296] In this case the Universal Stores sued the South African Railways for certain wages (including other wages not relevant to this discussion) that had been ceded to it by the employees of South African Railways.

South African Railways argued that the Railway Board, acting under Act 20 of 1908, passed certain regulations on 28 May 1912, which were published by the General Manager of South African Railways in the weekly circular of 21 June 1912. These regulations prohibited railway employees from ceding their wages. Act 20 of 1908 provided that:

> [T]he Board may from time to time make regulations not inconsistent with this Act with respect to, *inter alia*, the pay and the conditions of employment….[297]

Curlewis J handed down the judgment. After scrutinising the minutes of the Board's meeting, Curlewis J held that the Board did not intend to make such a regulation as, if such a regulation had been intended, the minutes

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[296] 1914 TPD 280.

[297] Supra 283.

would have been differently and more clearly worded.[298] The cessions of wages to The Universal Stores were therefore valid.

Curlewis J was, however, of the opinion that the prohibition of cession was a reasonable prohibition, as it protected the employer from conflicting claims in respect of employees' wages and saved him from the 'inconvenience and annoyance' that would accompany a large number of employees ceding their wages.[299]

The prohibition was also considered to be in the interest of the employees, as it prevents imprudent employees, who earn very little, from getting into debt by being able to obtain credit through ceding their wages.[300]

This case is the earliest known case that deals directly with a *pactum de non cedendo*. It is interesting to note that the court makes reference to the 'interest requirement' without referring to Sande and Voet.[301] When passing comments on the interest requirement the judge merely seems to have drawn the remarks from common sense.

3.2 The watershed case: *Paiges v Van Ryn Gold Mines Estates Ltd*

In ***Paiges v Van Ryn Gold Mines Estates Ltd,***[302] Mr Klein was employed by Van Ryn Gold Mine Estates on 27 August 1919. Upon employment, Mr Klein signed a contract containing the following clause (clause 8):

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[298] Supra 284. The minute in question read as follows: 'Powers of attorney, cessions, or other equivalent documents issued by railway servants. Noted and approved recommendation by General Manager that the terms of Weekly Notice 425 of 16th April, 1910, paragraph 6015, and Weekly Notice 432 of 21st May, 1910, paragraph 6145 be re-issued to the staff employed in the Transvaal and Orange Free State Provinces.'

[299] Supra 286

[300] Ibid.

[301] That is, that the *pactum de non cedendo* will be valid if the debtor (the employer in this case) can show that he has an interest in the prohibition. In this case the interest would be preventing the inconvenience and annoyance that would accompany many employees ceding their wages. See Chapter 4 for a further discussion on the interest requirement.

[302] 1920 AD 600.

> Save as herein otherwise provided from and after the date of this agreement the employed except with the consent in writing of the management, may not, and he hereby undertakes not to cede or assign his right and claim to any wages or moneys due or to become due hereunder, and it is agreed that any wages earned by the employed, or money due to him under this agreement shall only be paid to the employed personally….[303]

The only exception to this clause was if the employee was absent due to authorised leave of absence, illness or death.

On 23 June 1919, before Mr Klein was employed by Van Ryn Gold Mines Estates, he ceded to Paiges, a general dealer, his salary or wages then due or which thereafter may become due, as security for a debt.

On 5 September 1919 Paiges gave notice of the cession to Van Ryn Gold Mine Estates, but it invoked clause 8 and refused to recognise the cession. Paiges consequently sued Van Ryn Gold Mine Estates in the magistrate's court for the money ceded to him by Mr Klein, and was successful. The magistrate was of the opinion that every right of action can be ceded and, if a cession occurs, the cessionary cannot be prejudiced by an 'underhand' agreement between the cedent and the employer.[304]

3.2.1 The Transvaal Provincial Division

Van Ryn Gold Mine Estates appealed to the Transvaal Provincial Division, which overturned the earlier judgment of the magistrate's court and decided against Paiges.

The majority judgment was given by Gregorowski J, with Curlewis J concurring and Wessels J dissenting.

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[303] Ibid.

[304] Supra 601.

Gregorowski J disagreed with the reasoning of the magistrate as the cessionary would, as a result of the cession, be put in a better position than that of the cedent and would be entitled to claim something other than that which was ceded to him.[305] He continued to state that the 'underhand' agreement:

> … is the only agreement under which the debtor is bound, and it is of this agreement that the cessionary has obtained the cession, it is part and parcel of what has been ceded to him.[306]

The judge pointed out that Paiges did not object to clause 8 because it was prejudicial to him, but that stipulations such as clause 8 were illegal or against public policy. Gregorowski J rejected this argument. His reasons are threefold.

First he argued, a *pactum de non cedendo* is not against public policy as the right of cession is a right that an employee may elect to exercise or not to exercise – it is a voluntary act that cannot be forced by a creditor and should an employee elect not to exercise this right, but to waive it instead, he is fully entitled to do so.[307] He explained that:

> As a rule parties are free to contract as they please. The law permits perfect freedom of contract. Parties are left to make their own agreements, and whatever the agreements are the law will enforce them provided they contain nothing illegal or immoral or against public policy.[308]

Gregorowski J could see no reason why an employer (the debtor) should be barred from concluding a *pactum de non cedendo* as contained in clause 8, as an employer can:

> …employ the workman or not as he pleases and surely he can engage him on his own conditions, and if the workman agrees, it

[305] Ibid.

[306] Ibid.

[307] Supra 603.

[308] Supra 601.

> is difficult to understand on what grounds a third person can interfere and complain and upset the terms of the contract and bind the employer in a manner in which the employer has expressly stipulated he should not be bound.[309]

He substantiates this by adding that the cessionary still has all available remedies at his disposal, for instance the cessionary can sue the cedent and obtain a garnishee order from the court.[310]

Secondly, according to the judge, a *pactum de non cedendo* is not against public policy because a cession would force the employer (the debtor) to endure the inconvenience of performing to the cessionary, a party with whom he did not contract and probably would never have contracted. The cession consequently 'creates a privity [between the debtor and the cessionary] which did not previously exist'.[311]

This inconvenience, as the argument went, can translate into a serious burden, especially if the employer employs a large number of workers. Further, the cessionary may turn out to be an unscrupulous person who causes disorder where disorder would not have otherwise occurred.[312]

Thirdly, the judge continued, a *pactum de non cedendo* is not against public policy as it was not against public policy for the Government to put into place legislation preventing mine workers from ceding their wages. Further, it was similarly not against public policy for the Railway Department to pass bylaws which prevented the railway employees from ceding their wages.[313]

Gregorowski J reasoned that if Government and the Railway Department could validly include a *pactum de non cedendo* into the employment contract of employees, then there is nothing to prevent large companies

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[309] Supra 603.

[310] Supra 602.

[311] Ibid.

[312] Supra 603.

[313] Ibid.

from doing the same since the benefit of the *pactum de non cedendo* in both cases would be the same. He used the following quote from Curlewis J in *South African Railways v The Universal Stores,*[314] as authority for this view:

> It does not seem an unreasonable provision that an employer shall stipulate that one of the conditions of the servant's employment will be that he shall receive his wages personally and the employer will not recognise any power to receive or any cession of such wages when the servant is able to attend and draw his wages in person.[315]

The benefit of the *pactum de non cedendo*, as mentioned above, is not only for the employer, but also for the employee, in the form of protection. The judge stated that the *pactum de non cedendo* prevents the employee from losing interest in his job, as he would if he had already ceded his earnings before they were due; it protects the employee against improvidence at the hands of unscrupulous moneylenders; it protects the employee from obtaining credit to dabble in matters in which he cannot afford to dabble, like racing or gambling; and generally, it prevents the employee from overwhelming himself with avoidable debt.[316]

After stating his reasons as to why the *pactum de non cedendo* was not against public policy, he turned to consider authority on the issue and noted that:

> …[t]here does not appear to be much authority upon the question in our law. I would imagine that the reason is that it was always accepted that a person could renounce a right in his own favour.[317]

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[314] *South African Railways* supra 286.

[315] Supra 604.

[316] Supra 603-604.

[317] Supra 604.

Fortunately, the lack of case law on the issue did not convince the judge to stop his investigation, as he turned to consider the common law writers. With reference to Sande *De Prohibita* Gregorowski J stated that:

> If therefore the person making the pact or stipulation has an interest in that the owner shall not alienate his own property, a pact to the effect that the property shall not be alienated is valid.[318]

The judge summed up Sande's words by concluding that:

> …[W]e cannot by pact take away from an owner the power of alienating his own property unless we have some interest in it.[319]

Gregorowski J pointed out that on the facts of the case Van Ryn would have a very substantial interest in including a *pactum de non cedendo* in the contract.[320]

He subsequently considered the English case of *Brice v Bannister,*[321] where Bramwell LJ explained the legal position as follows:

> It does seem to me a strange thing and hard on a man that he should enter into a contract with another and then find that because the other has entered into some contract with a third, he, the first man, is unable to do that which is reasonable and just he should do for his own good. But the law seems to do so, and anyone who enters into a contract with A must do so with the understanding that B may be the person with whom he will have to reckon – whether this can be avoided I know not; may be, if in the contract with A it was expressly stipulated that an assignment to B shall give no rights to him such a stipulation would be binding. I hope it would be.[322]

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[318] Ibid.

[319] Ibid.

[320] Ibid.

[321] [1878] 3 QBD 569 580.

[322] Supra 604.

Gregorowski J concluded his investigation into authority on the issue by mentioning that he could not find any other references, although there did exist authorities that seemed to assume that a *pactum de non cedendo* would not be null and void.[323]

He lastly mentioned the American case of *William Barringer v Bes Line Construction Co*[324] and extracted the following quotation:

> The purpose for this statute (providing for assignment of contract) was not to prohibit parties from contracting that their contracts shall not be assignable. The intention of the statute and of similar statutes as they exist in other states is to remove the restriction of the common law rule upon choses in action which prevented their transfer, and to permit the assignee to maintain suit in his own name.[325]

According to Gregorowski J this case illustrated that American courts have held that parties to a contract of service or other contract are not prevented from restricting the transfer of rights of action which are capable of being ceded.[326]

Wessels J, who delivered the dissenting judgment in the Transvaal Provincial Division, held that there was no difference between the cession of wages and the cession of any other debt.[327] The authorities do not distinguish between different kinds of debt, unless the element of personality is involved. According to Wessels J, a claim for wages is no more personal than a claim for money that was lent or paid as rent.[328]

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[323] Ibid. The judge did not mention these authorities and his failure to investigate them can be seen as a crucial shortcoming of the judgment.

[324] L.R.A 1909 vol 21 N.S 597.

[325] Supra 605-606.

[326] Supra 605.

[327] Supra 606.

[328] Supra 608.

Consequently, when answering the question of validity of the *pactum de non cedendo* in respect of wages, the scope of the enquiry should be extended to cover the general question of whether any prohibition with regard to any debt would be valid.[329]

Wessels J asserted that he could see no difference between a restraint on alienation of a corporeal and a restraint on alienation of an incorporeal, and submitted that he did not think that our law recognised a restraint on alienation where the restriction is not in favour of a particular person.[330]

Relying on Sande *De Prohibita*[331] he stated that:

> A pact entered into with the owner of property to the effect that he shall not alienate his own property is of no legal effect.[332]

The judge then used the following passage from Sande *De Prohibita*[333] as an explanation for the general rule:

> For there is no causa upon which such a pact can be supported: and utility which is the mother of all good and equity demand that those pacts shall not be valid which impede all commerce and take away from us without any consideration the use of our own property; so also we cannot by a pact take away from an owner the power of alienating unless we have some interest in it… From such an agreement therefore, that the owner shall not be allowed to alienate his property, even if the stipulation is a valid one, not even a personal action can arise.[334]

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[329] Supra 606.

[330] Ibid.

[331] 4 1 1.

[332] Supra 607.

[333] 4 1 1.

[334] Supra 607.

Wessels J is emphatic in his belief that no authority could support a finding that if a right of action was ceded contrary to a *pactum de non cedendo*, the cessionary would be unable to enforce his right against the creditor.[335] The more likely case would be that if the right was ceded contrary to the *pactum de non cedendo*, the cessionary would acquire the creditor's right against the debtor and would enforce this claim against him as opposed to the creditor.[336]

According to the judge, the provision that the creditor must claim personally from the debtor is not part of the debt itself, but rather a subsidiary right, which, if enforceable, could only give rise to damages at most.[337]

From the above Wessels J abruptly concluded that:

> … [A]ccording to our law it is contrary to public policy to enforce a pact by which a person agrees not to alienate or cede part of his property. A fortiori therefore it would be contrary to public policy to prevent the cessionary of a debt, especially one who is ignorant of the fact that the cedent has contracted not to cede it, from recovering such debt from the debtor.[338]

Wessels J then turned to consider English law and noted that the difference between South African law and English law was that where English law regards all *pacta de non cedendo* as valid, South African law regards all *pacta de non cedendo* as invalid and against public policy unless the *pactum de non cedendo* is in favour of a particular party.[339]

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[335] Ibid.

[336] Ibid.

[337] Ibid.

[338] Ibid. Would the situation then be different if the cessionary was aware of the *pactum de non cedendo*?

[339] Supra 607.

Returning to discuss the position under South African law and relying on Voet and Sande as authority, Wessels J asserted that if a right to claim monies is ceded, once the monies become due, the rights and interests of the cedent cease. The rights and interests are accordingly transferred to the cessionary who becomes the only person entitled to claim the monies.

Further, a cession would still be completely valid even if the cession was made without the knowledge of the debtor, against his will or without giving him notice.[340]

Using the above as a basis, Wessels J concluded that once wages have accrued to an employee, a cession of the wages will effect the passing of the right to claim such wages to the cessionary, regardless of the fact that the employer might object to the cession by reason of it being a breach of contract between the employer and the employee.[341]

The judge continued to explain that if by ceding his wages, the employee breaches the contract that he concluded with his employer, the employer may have recourse to an action for damages against the employee,[342] but a contractual prohibition of cession cannot deprive the cessionary of the right to claim the wages from the employer.[343]

It is interesting to compare these conflicting judgments in the Transvaal Provincial Division. It appears that Gregorowski J was of the opinion that a *pactum de non cedendo* is generally valid and not against public policy,

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[340] Supra 608. It is interesting to note that a cession against the will of the debtor would be valid, but if the debtor's will is evidenced in a *pactum de non cedendo*, a cession would be invalid (unless an interest exists).

[341] Supra 608.

[342] Supra 609.

[343] Supra 608. Why did Wessels J not refer to the authorities who 'seem to assume that a provision against assignment would not be null and void' in support of his argument which Gregorowski J mentioned, but failed to investigate? See *Paiges* supra 604 and footnote 323.

yet Wessels J viewed a *pactum de non cedendo* as invalid and against public policy unless it is in favour of a particular person.

Also, as to the effect of *pacta de non cedendo*, Wessels J argued that a cession contrary to the *pactum de non cedendo* would indeed transfer ownership of the right to the cessionary, leaving the debtor (the employer) with an action for damages for breach of contract. Gregorowski J on the other hand, was of the opinion that a valid *pactum de non cedendo* had the effect of rendering the personal right non-transferable, thus resulting in the cessionary receiving nothing from the cession.

3.2.2 The Appellate Division

Paiges, having been unsuccessful in the High Court consequently appealed. The unanimous judgment, in favour of Van Ryn Gold Mine Estates in the Appellate Division, was delivered by De Villiers JA.

De Villiers JA held that there was no direct prohibition of *pacta de non cedendo* in Roman or Roman-Dutch law, so a finding that such *pacta de non cedendo* are invalid, must be based on a principle restricting the freedom of contract,[344] or on a principle rendering it contrary to public policy.[345]

De Villiers JA considered, first, whether a *pactum de non cedendo* can be rendered invalid due to a principle restricting freedom of contract. In doing so he referred to Sande and Voet respectively:[346]

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[344] Supra 614.

[345] Supra 615.

[346] Sande *De Prohibita* 4 1 1 and 4 2 1 and Voet *Commentarius* 2 14 20.

> [A]n agreement with the owner that he shall not alienate his own property, is without force (*inutile*), for the reason that the person who imposes the restriction has no interest in it.[347]

And:

> [A]greements which take away from the owner the free right of dealing with his property are of no effect.[348]

The judge explained that the general rule, that *pacta de non cedendo* are invalid, only applies in cases where the debtor has no interest in the restriction.[349] If, however, the stipulation can be shown to 'serve a useful purpose' to the debtor, it is valid and binding upon the parties to the contract.[350]

De Villiers JA concluded that Van Ryn Gold Mine Estates had a 'very real interest' in the *pactum de non cedendo*.[351] Following the *ratio* in *South African Railways v The Universal Stores*,[352] the reason for this conclusion is that:

> [t]o a company employing numbers of workmen it may be a matter of serious concern whether it is only liable to its own workmen or whether it can be called upon by strangers to pay the workmen's wages. All kinds of difficult and complicated questions of law and of fact may arise, which in its own interests an employer might legitimately wish to avoid.[353]

The answer, therefore, to the first enquiry is that *pacta de non cedendo* cannot be rendered invalid due to a principle restricting freedom of

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[347] Supra 615.

[348] Ibid.

[349] Ibid.

[350] Ibid. Thus 'an interest' and a 'useful purpose' have been used synonymously.

[351] Supra 615.

[352] *South African Railways* supra 286.

[353] Supra 615. One wonders exactly what these 'complicated questions of law' really are.

contract if the restriction is for the benefit of the party imposing the interest. In this case the employer had a 'very real interest' so the *pactum de non cedendo* was not invalid on this basis.

De Villiers JA considered, secondly, whether *pacta de non cedendo* are contrary to public policy. He noted that the explanation put forward for this argument is that a *pactum de non cedendo* is 'highly detrimental' to the employee as 'it places him at the mercy of the employer' if he requires an advance on his wages.[354]

The judge admitted that this argument does indeed carry some weight, but pointed out that the *pactum de non cedendo* may actually provide distinct advantages to the employee (as Gregorowski J before him also pointed out).[355] In this regard he referred to the fact that the East and West India Companies imposed such a *pactum de non cedendo* on their employees, as well as the fact that legislation and by-laws were passed which prevented mine workers and railway employees from ceding their wages.[356]

De Villiers JA was of the opinion that the advantage to the employee waters down the argument that the *pactum de non cedendo* is against public policy and balances the outcome in favour of enforcing the restraint.[357] He continued, however, that the presence or absence of an advantageous gain to the employee by the inclusion of a *pactum de non cedendo* is not the conclusive answer to the question of whether the restraint is contrary to public policy.[358]

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[354] Supra 615.

[355] Supra 615-616.

[356] Supra 616.

[357] Ibid.

[358] Ibid.

According to De Villiers JA, the answer was to be found in the fact that a court cannot declare an agreement that was freely entered into by the parties as contrary to public policy.[359] Albeit large employing companies may abuse their contracting power by including certain terms, like a *pactum de non cedendo*, into an employment contract, this would be a matter for the legislator to address and not the court.[360]

The answer, therefore, to the second enquiry is that a court cannot render *pacta de non cedendo* against public policy and thus invalid if the parties freely entered into a contract containing such a restriction, only the legislator may intervene to this extent. An advantage or benefit of the *pactum de non cedendo* to the creditor (the employee), although not compelling, is apparently considered to be persuasive. On this point the Appellate Division thus preferred the view of Gregorowski J in the court *a quo*.

The facts of this case show that the parties freely entered into an employment contract which contained a *pactum de non cedendo* and the creditor himself also derived some benefit from the restraint, or so it was argued. The *pactum de non cedendo* was thus not against public policy and was consequently not invalid on this basis either.

De Villiers JA went on to state that a cession places the cessionary at most in 'the shoes of the cedent'[361] and albeit the cessionary may be prejudiced by a *pactum de non cedendo* of which he had no knowledge, the cessionary 'can have no greater rights than the cedent himself has'.[362]

De Villiers JA summed up this point as follows:

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[359] Ibid.

[360] Ibid.

[361] Ibid.

[362] Ibid.

> When the cedent [creditor] therefore has parted with the right to cede the debt, no other party can obtain any rights to it. The right which the creditor obtains, being circumscribed by the terms of his agreement with the debtor, becomes by the agreement between the parties a strictly personal right, and cannot be ceded.[363]

In determining the effect of a cession in contravention of a *pactum de non cedendo* De Villiers JA relies on Windscheid, a German authority, as according to the judge 'the question is not dealt with in the Roman law'.[364] The view of Windscheid and of the judge is that a cession in contravention of a *pactum de non cedendo* is void.[365]

The reason for De Villiers' JA opinion is evident from the following passage:

> The stipulation against cession is part and parcel of the agreement creating the right, and the right is limited by the stipulation.[366]

In other words, a contract and the *pactum de non cedendo* included therein would be so closely linked that the one cannot be separated from the other. The result is that the *pactum de non cedendo* is considered as an overarching stipulation which prevents the transfer of ownership, as the party benefiting from the *pactum de non cedendo* (the debtor) no doubt intended.

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[363] Ibid. Has De Villiers JA not erred in this passage? As a general rule all personal rights can be ceded, barring a few exceptions.

[364] Supra 616. Of course the effect of a cession in contravention of a *pactum de non cedendo* was an issue not dealt with in Roman law – cession was a concept that was not recognised in Roman law and authority on the *pactum de non cedendo* was accordingly non-existent. Surely what the judge meant to say was that the question is not dealt with in the *Roman-Dutch* law?

[365] Supra 617. De Villiers JA mentions in passing that Seuffert, another German authority, has a different opinion, *viz*, that a cession in contravention of such a prohibition is not void.

[366] Ibid.

The *pactum de non cedendo* is thus not treated as a mere term of the contract, where ownership nevertheless passes to the cessionary and where the debtor is left with an action for damages, but the result is the personal right being rendered non-transferable.

The approach that the Appellate Division adopted consequently enforces the fundamental purpose of including a *pactum de non cedendo* in a contract; as to do otherwise, the court probably reasoned, would result in cession-prohibiting-agreements that do not, in fact, prohibit cessions.

In terms of this approach, it is the cessionary who suffers the loss of a right of action which he *bona fide* contracted to acquire and it is the cessionary who is forced to be satisfied with an action for damages against the cedent for breach of contract. Once more, the Appellate Division confirmed the opinion of Gregorowski J in the court *a quo*, ignoring the view of Wessels J.

Despite the fact that I have a different view to that of the Appellate Division regarding the validity and effect of *pacta de non cedendo* (which will be discussed in later Chapters), it is important to point out here already that the authorities upon which the court so heavily relies, are not properly adhered to.

Sande clearly wrote that the jurists were undecided as to whether ownership passes to the cessionary, but expressly stated that the more correct view was that ownership did pass, leaving the debtor with an action for damages against the cedent.[367]

[367] *De Prohibita* 4 2 11 and 4 2 14. See Chapter 1.

Voet also wrote that ownership passes to the cessionary despite the inclusion of a *pactum de non cedendo*. For Voet, the purpose of the *pactum de non cedendo* is to enforce that a person remains faithful to his promise, with an action for damages arising should he dishonour it.[368]

Strangely enough the court in *Paiges* forsakes the views of Sande and Voet and prefers the writings of German authorities, even though Wessels J in the court *a quo* was of the opinion that the Roman-Dutch writers were worth adhering to.

What is also surprising, as will be seen from the case studies that follow, is that none of the cases after *Paiges* challenged or even expressly questioned the Appellate Division's failure to properly adhere to the principles laid down by Sande and Voet.

3.3 Cases after *Paiges v Van Ryn Gold Mines Estates Ltd*

In the case of ***Northern Assurance Company Ltd v Methuen***,[369] a Southern Rhodesian case, Franco and Baglietto carried on business as motor transporters and insured their vehicles with Northern Assurance Company. The insurance policy contained a third party risk clause in respect of accidental bodily injury caused to any person caused by the insured vehicles.

Mr Methuen was fatally injured by one of the insured vehicles and his widow was successful in an action for damages against Franco and Baglietto. The latter ceded to Mrs Methuen their rights under the contract of insurance so that she could claim her damages from Northern Assurance Company.

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[368] *Commentarius* 2 14 20. See Chapter 1.

[369] 1937 SR 103.

Northern Assurance Company refused to recognise Mrs Methuen's claim and argued that the cession was not valid on the basis of clause 14 contained in the insurance policy. Clause 14 read as follows:

> Nothing contained herein shall give any rights against the Company to any person other than the insured, and the Company shall not be bound by any passing of the interest of the insured otherwise than by death, unless and until the Company shall by endorsement hereon declare the insurance to be continued.[370]

The issue, *inter alia*, was whether clause 14 could be construed as a *pactum de non cedendo*.

The insurance company argued that if clause 14 was found to be a *pactum de non cedendo,* then it would be void as such restrictions were against public policy.[371]
The presiding judges McIlwaine and Lewis, held that clause 14 could not be construed as a *pactum de non cedendo*. They both agreed on this point, but had slightly different reasons for their finding.

The basis of the judgment of McIlwaine ACJ was simply that clause 14 could not by its general terms prohibit the common law right of assignment, as it contained no specific provision to that effect, especially when it is the duty of the insurance company to make its terms clear.[372]
The judge continued that if the insurance company genuinely wanted to prohibit a cession, it would have been easy to include a passage in the contract making their wishes instantly recognisable and unambiguous. Thus, clause 14 was too general in its construction to be construed as a *pactum de non cedendo*.[373]

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[370] Supra 107.

[371] Supra 111.

[372] Supra 109.

[373] Ibid. I tend to agree with the judge on this point. The phrasing of clause 14 almost seems to refer to prohibition on the transfer of Mr Methuen's insurable interest in the insurance policy and not to a *pactum de non cedendo*.

Lewis J, in turn, held that clause 14 could not be construed as a restraint prohibiting cession as the construction of clause 14 merely emphasised the insurance company's right to insist on its *delectus personae* and it thus prohibited substitution.[374]

According to the judge, clause 14 did not signify that rights of action which had accrued to the insured could not be transferred. If this interpretation was not the intention of the insurance company then, according to the judge, it should have used appropriate words to express its intentions in a manner that made the intended meaning clear.[375]

Lewis J noted that the *pactum de non cedendo* in this case could serve a useful purpose to the insurance company. The provision would ensure that the company could avoid defending actions against unknown parties who might not be able to pay the costs of the action should they be unsuccessful.[376]

The judge also pointed out that another possible benefit of the *pactum de non cedendo* to the insurance company would be to have as an opponent in a legal action the party with whom it contracted, as it is this party who can best address the matters at issue in a disputed claim.[377]

Citing *Paiges v Van Ryn Gold Mine Estates*, Lewis J stated that:

> I am satisfied that under Roman-Dutch law such a pact is not void, provided that it can be shown to serve a useful purpose to the debtor, and in English law it is also valid apparently without such proviso.[378]

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[374] Supra 112.

[375] Ibid.

[376] Ibid.

[377] Ibid.

[378] Ibid.

Lewis J added that even if clause 14 could be construed as a *pactum de non cedendo* it would not be invalid on the ground of public policy. The rationale for this finding was based on an analogy of one of the writings of Sande.[379] The judge reasoned that Sande[380] was of the opinion that if the cession was fraudulent, or if the cessionary was a 'quarrelsome or a pettifogging' person, the debtor could refuse to litigate with him and demand that the cedent bring the action himself.[381]

In such a situation, therefore, it would be allowable to overlook the fact that the right of action was no longer the property of the cedent, but to force him nevertheless, to bring the action himself so that the debtor was protected.

From the aforementioned Lewis J concluded that if Sande's submission, which affords protection to the debtor,

…be good law to-day, how much more valid would be the right to stipulate in advance [that is through a *pactum de non cedendo*] to secure a similar protection.[382]

The court in this case seems to have simply applied the *ratio* in *Paiges*. A few years after this case, however, the Appellate Division had the opportunity to revisit the principles governing the *pactum de non cedendo*.

In ***Estate Fitzpatrick v Estate Frankel and others; Denoon and another v Estate Frankel and others***,[383] Frankel leased certain premises subject to a clause (clause 8) which stated that he was prohibited from assigning the lease or sub-letting the premises without the consent of the lessor.

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[379] Supra 111-112.

[380] *De Cessione* IX.

[381] Supra 111.

[382] Ibid.

[383] 1943 AD 207.

Frankel, after obtaining the consent of the lessor, sub-let the premises. He also ceded the right to claim rent to a creditor, Fitzpatrick, as security for the repayment of a loan with interest, but this he did without obtaining the consent of the lessor. The sub-lessee was notified and duly paid rent to Fitzpatrick.

Thereafter, Fitzpatrick ceded its rights to claim rent to a third party, Denoon. The sub-lessee was notified and duly paid to Denoon.

Soon thereafter Frankel's estate was sequestrated and Frankel's trustee and lessor, who was in fact a creditor in his estate since Frankel had defaulted on rent payment, brought actions for, *inter alia*, declaring the cession by the lessee null and void and of no effect as the cession was made contrary to clause 8 of the lease agreement.

Unanimous judgment was delivered by Centlivres JA.

The judge, using *Paiges v Van Ryn Gold Mine Estates* as authority, held that rights may be freely ceded, but that this principle may be subject to certain qualifications.[384]

The judge noted that the argument was raised that clause 8 operated to prevent only voluntary assignments and sub-leases, but not assignments brought about by the operation of law through sales in execution or in liquidation.[385]

Centlivres JA held a forced sale would not result in a breach of the lease agreement because the parties to the lease did not construct the agreement so as to extend the application of clause 8 to sales that were involuntary.[386]

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[384] Supra 217.

[385] Supra 218. See also the cases referred to therein.

[386] Supra 219.

The judge concluded that:

> …[T]he cases cited show that the words 'the lessee shall not assign his lease' must be interpreted as referring only to voluntary assignments.[387]

Interestingly, the judge was asked to extend the interpretation of the above to include a voluntary act by the lessee which eventually results in an involuntary assignment.[388] Centlivres JA refused to do so, stating that 'such a wide interpretation' would not be 'justified'.[389]

Turning to consider the validity of the cession, the judge held that what Frankel actually ceded was the right to claim rent from the sub-lessee. He did not cede the lease itself. Since clause 8 only referred to the ceding of the lease itself and not the rent, Frankel had not breached the lease agreement and the cessions were held to be valid.[390]

One year later the Appellate Division had another occasion to consider the principles governing *pacta de non cedendo*, this time in a contract of sale.

In the case of ***Friedlander v De Aar Municipality***,[391] Wulf Friedlander and Isaac Friedlander were co-owners of a farm which they converted into building plots for the purpose of laying out a township. In 1907 the Friedlanders had entered into a contract of sale with the municipality of De Aar, whereby the former sold to the latter two pieces of land known as the

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[387] Ibid.

[388] Ibid.

[389] Ibid. See Chapter 5.

[390] Supra 219. It must be mentioned that this reasoning of Centlivres JA is somewhat contrived. If clause 8 expressly prohibited the sub-letting of the premises, then a prohibition on the cession of 'the lease' could certainly have referred to nothing other than the right to claim rent under the lease? Surely, then, Frankel's ceding of the rent amounted to a ceding of the lease?

[391] 1944 AD 79. See also Chapter 5.

Commonage. The municipality was to hold the Commonage in trust for the erfholders of the Friedlander township.

The cause for dispute arose primarily from clause 3 of the contract of sale which stated that the municipality was prohibited from alienating or disposing of any portion of the land without the prior written consent of the Friedlanders or their 'heirs, executors or assigns'.[392]

In 1940 the municipality wanted to sell a portion of the Commonage and entered into long and complicated negotiations with Johanna Friedlander in her capacity as a cessionary of the rights of the Friedlander partnership, as executrix of the deceased estate of one of the deceased partners and as a representative of the heirs of the deceased estate of a deceased partner.

The negotiations eventually led to an agreement of sale for consideration where Johanna Friedlander ceded to the municipality the rights that were reserved in clause 3 of the contract.

Certain conditions first had to be fulfilled before the agreement was binding. During the course of fulfilling these conditions, the municipality received legal advice that it was entitled to alienate any portion of the Commonage, subject only to the approval of the Administrator in terms of ss170 – 173 of Ordinance 10 of 1912.[393]

The court *a quo* ruled in favour of the municipality and Johanna Friedlander consequently appealed.

Greenberg JA handed down the unanimous judgment. The issue before the court was, *inter alia*, whether the municipality was entitled to alienate the Commonage, subject only to the approval of the Administrator and if

[392] Supra 83.

[393] Supra 86.

not, whether such alienation was valid with the consent of Johanna Friedlander.

Greenberg JA, whose discussion of the *pactum de non cedendo* was very brief, relied mostly on Sande as authority for his judgment.[394] The judge held that since prohibitions on alienations were valid and since the Friedlanders had an interest in the prohibition, it was valid.[395]

Further, said the judge, the rights of the Friedlanders were transmissible as the nature of the contract did not involve a *delectus personae* and the contract itself expressly alluded to this.[396]

Greenberg JA concluded, *inter alia*, that the municipality indeed required the consent of Johanna Friedlander in order to alienate the property and the alienation was void.[397]

Unfortunately the Appellate Division once again missed an opportunity to establish certainty on the *pactum de non cedendo* and for the next 24 years, these were the principles applied to *pacta de non cedendo*. [398]

In the case of ***Richter N.O v Riverside Estates (Pty) Ltd***,[399] the late Richter was the registered owner of 1000 ordinary shares in Riverside Estates. No money passed between the parties upon purchase of the shares, but Richter passed a bond over his farm to the value of the purchase price of the shares as security for payment.[400]

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[394] Supra 92-93.

[395] Supra 93.

[396] Supra 93.

[397] Ibid.

[398] The Appellate Division had the occasion to consider the *pactum de non cedendo* in the case of *Trust Bank of Africa Ltd v Standard Bank of South Africa Ltd* 1968 (3) SA 166 (A).

[399] 1946 OPD 209. See also Chapter 5.

[400] Supra 219

Upon excussion of the security there remained an unpaid balance owing to Riverside Estates under the bond. The executrix testamentary of Richter's deceased estate sold the shares to one Goodrick. Goodrick paid the purchase price and the transfer form was delivered to him. The company, however, refused to accept or register the transfer of the shares.[401]

The executrix testamentary applied to the court for, *inter alia*, an order declaring that the company was not entitled to decline to register transfer of the shares to Goodrick.[402]

The unanimous judgment was written by Van den Heever AJP. His point of departure was to refer to the company's articles of association which provided that:

> The Director or Directors may, at any time in their absolute and uncontrolled discretion and without assigning any reason therefor, decline to register any proposed transfer of a share or shares in the company.[403]

Van den Heever AJP implied that this article amounted to a *pactum de non cedendo* because Richter, he pointed out, had become a member of the company subject to this express condition.[404] Against the background of *Paiges v Van Ryn Gold Mine Estates* he held that:

> If the *pactum de non cedendo* is valid…then there can be no question of the validity of a pact, not against the alienation of the bonitary rights to a share, but against the registration of its transfer which entails the admission of an unwanted member of the company.[405]

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[401] Supra 218.

[402] Supra 219.

[403] Supra 218.

[404] Supra 226.

[405] Ibid.

According to Van den Heever AJP, the English case of *In re Smith and Fawcett Ltd*,[406] dealt with a similar dispute.[407] In that case Lord Green refused to read a non-assignment clause into a document that was drafted in such wide terms.[408] Van den Heever AJP pointed out that there was no reason why the *ratio* of the court could not be applied in South Africa and dismissed the application.

It is evident that this court, following the style of the recent cases in the Appellate Division, was not too forthcoming with notes and commentary on the *pactum de non cedendo*. In the next case, however, the judge made an interesting observation.

In ***Du Plessis v Scott***,[409] Scott entered into a contract with Swanepoel in terms of which the latter was to build Scott a house. Swanepoel failed to complete the house and the parties consequently agreed that Scott would complete it and deduct the cost of completion from the contract price.

As an express or implied term of the new agreement, Scott was to render a complete and full account of the cost of completion to Swanepoel. Scott completed the building of the house and drew up an account; by this time Swanepoel had ceded his right of action under the contract (as varied) against Scott to Du Plessis.[410]

Du Plessis claimed that Scott had generally not rendered a full and complete account and denied two items appearing therein. Scott, in his declaration, excepted to the claims made by Du Plessis on the ground that they, *inter alia*, failed to disclose a cause of action considering the

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[406] 1942 Ch.D L.R 304.

[407] Supra 226.

[408] Ibid.

[409] 1950 (2) SA 462 (W). See also Chapter 4.

[410] Supra 463.

inclusion of clause 10 in the contract which, as the argument went, amounted to a *pactum de non cedendo*.

Clause 10 read as follows:

> Die kontrakteur mag nie enige van sy regte hieronder oormaak of onderverhuur nie, nog enige sessie uitreik, of enige orders aan die werkgewer oordra waaronder enige gelde wat aan die kontrakteur verskuldig is, deur enige persoon volgens wet kan word nie.[411]

The case was decided by Blackwell J, who pointed out that Du Plessis argued that clause 10, or the *pactum de non cedendo*, was not enforceable unless the party claiming to enforce it could prove that the restriction served a 'useful purpose' to the debtor.[412]

Du Plessis' argument was based on the following words of De Villiers JA in *Paiges* v *van Ryn Gold Mines Estates Ltd*:[413]

> The principle therefore only has application in the case where the debtor has no interest in the matter. In other words, if the stipulation can be shown to serve a useful service to the debtor, it is valid and binding on the parties to the contract.[414]

This argument prompted Blackwell J to investigate the *ratio* in *Paiges* and that court's reliance on Voet and Sande. His understanding of the old authorities is clear from the following passage:

> It was in relation to these two authorities that the passage from the judgment of De Villiers JA, quoted above, followed. I read the passages from *Sande* and *Voet* as meaning that the Courts will not enforce an agreement which I may make with a stranger which fetters my right to dispose of my own property, but, if the

[411] Supra 464.

[412] Ibid.

[413] Supra 615.

[414] Supra 464.

agreement is made with a person who has an interest in the matter, it may be binding. [415]

Blackwell J then proceeded to ask two questions:[416]

1. Did the Court of Appeal *intend* to lay down the same rule in regard to agreements not to cede or assign, as Sande and Voet *appear* to indicate in regard to restraints upon the alienation of property generally?

[A]nd

2. *Assuming* that question 1 is answered in the affirmative, does a person seeking to enforce a prohibition against cession have to allege and prove that the prohibition served a useful purpose to him, or can the Court, especially in a case like the present, look to the contract itself, and form its own conclusions upon the matter, if there are sufficient data? [My emphasis]

Blackwell J failed to answer question one expressly and it is a pity that the judge did not take his question any further. Unfortunately he assumed that there is no difference between restraints on the alienation of corporeals and restraints on the alienation of incorporeals. The fact that the judge asked this question, however, can surely be interpreted to mean that he had some doubt that the right under discussion in *Paiges* and the right that Sande and Voet wrote about were not the same, otherwise why would he pose the question?

As to question two, even though he admits it is unclear, Blackwell J believed that evidence was taken in the magistrate's court in *Paiges* and was used by the appeal court.[417] He concluded that:

If therefore the judgment of the Court of Appeal in *Paiges'* case means that an agreement by one of the parties to a contract not to cede his rights thereunder cannot be enforced without some proof that it was made for the benefit, not of a stranger, but of an interested party, then I hold that the Court is entitled to look to the

[415] Supra 646-465.

[416] Supra 465.

[417] Supra 465.

> nature of the contract itself in order to determine this point, and if this appears sufficiently from the contract then formal averment and proof is unnecessary.[418]

Blackwell J was thus of the opinion that without other evidence, but by looking at the contract itself, the reason for the prohibition of cession in clause 10 of the contract was obvious, as Scott had a 'genuine interest' in limiting his dealings to Swanepoel alone.[419] The exception was consequently allowed.

The Appellate Division decision in the following case may have departed from the *ratio* in *Paiges*.

In the case of ***Trust Bank of Africa Ltd v Standard Bank of South Africa Ltd***,[420] Mrs Davidoff was a customer of Trust Bank and from time to time she deposited money with Trust Bank. In respect of each of these deposits, Trust Bank issued Mrs Davidoff with a deposit voucher recording the terms of the transaction. The deposit vouchers were standard in form and identical, barring information relating to the date and the amount deposited. Clause 5 of the deposit vouchers stated that the deposit voucher was issued subject to the conditions endorsed overleaf.[421]

There were three conditions overleaf, but only condition one is relevant to this discussion. Condition one stated that the deposit voucher was 'neither transferable nor negotiable'.[422]

Subsequently, Mrs Davidoff became indebted to Trust Bank and undertook to repay this debt in monthly instalments. Mrs Davidoff also executed a deed of pledge in favour of Trust Bank as security for repayment of the debt. The pledged items were eight deposit vouchers

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[418] Supra 466. This line of reasoning was also argued in the later case of *Vwada v Vawda* 1980 (2) SA 341 (T) below.

[419] Supra 466.

[420] 1968 (3) SA 166 (A). See Chapters 4 and 5 for a further discussion.

[421] Supra 177.

[422] Ibid.

which were ceded, pledged and delivered to Trust Bank. Some time later the deposit vouchers were released to Mrs Davidoff without any endorsements being made on them.

Mrs Davidoff thereafter required credit facilities in her capacity as director of Chermedine Clothing Corporation (Pty) Ltd and she approached Standard Bank in this regard. Standard Bank agreed to extend credit facilities to Mrs Davidoff and as security she ceded, pledged and delivered the eight deposit vouchers. Standard Bank was at all material times unaware that Mrs Davidoff had already ceded and pledged the deposit vouchers to Trust Bank.

Trust Bank argued, *inter alia*, that condition one referred to in clause 5 constituted a *pactum de non cedendo* which consequently precluded Mrs Davidoff from conferring any rights upon Standard Bank.

Hill J, in the court *a quo*, held in favour of Standard Bank and did not pursue the *pactum de non cedendo* argument.[423] Trust Bank successfully appealed.

Ogilvie Thompson JA, who gave the dissenting judgment, discussed the possibility of condition one amounting to a *pactum de non cedendo* and admitted that all rights of action may be ceded unless parties contract to restrict cession.[424] Mentioning *Paiges v Van Ryn Gold Mine Estates*, he added that a *pactum de non cedendo* 'will, in appropriate cases, be enforced', but because of its restricting nature, it must be expressed in 'clear and unequivocal terms'.[425]

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[423] Supra 188H.

[424] Supra 181F-G.

[425] Supra 181G-H.

Ogilvie Thompson JA held that the words of condition one were not sufficiently clear and unequivocal so as to render the condition a *pactum de non cedendo* and therefore it did not invalidate the cession.[426]

His reasons were twofold. First, if it was genuinely the intention of Trust Bank that condition one should amount to a *pactum de non cedendo*, then Trust Bank should have used more explicit language so as to convey that intention.[427]

Secondly, the words 'deposit voucher' pertained to the document itself and not the rights recorded therein and 'neither transferable nor negotiable' should be understood as meaning that mere transfer of the document itself confers no title against Trust Bank. However, although the judge did not spell this out, transfer of the rights therein by way of cession can confer such a claim against the bank.[428]

Botha JA gave the majority judgment. He held that the *pactum de non cedendo* argument that Trust Bank raised was indeed a valid and complete defence to Standard Bank's claim.[429]

The judge came to this conclusion by establishing from the outset that Mrs Davidoff ceded the deposit vouchers to Standard Bank *in securitatem debiti* and that the only question which arose therefrom was whether the cessions were valid considering that the deposit vouchers were 'neither transferable nor negotiable'.[430]

With reference to *Paiges v Van Ryn Gold Mine Estates*, the judge explained the law in the following *dictum*:

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[426] Supra 181G-H and 182E.

[427] Supra 182A.

[428] Supra 182C.

[429] Supra 189A.

[430] Supra 189C.

> The rule of our law is that all rights *in personam*…can be freely ceded, but an owner's right of free disposal of his property may be restricted by a *pactum de non cedendo*. The effect of such a *pactum* depends upon the circumstances. *Voet* 2.14.20 and Sande, *Restraints*, 4.1.1, and 4.2.1, point out that an agreement whereby an owner deprives himself of the free right to deal with his own property, is without effect unless the other contracting party has an interest in the restriction…. These principles *do not, however, apply where the right is created with a restriction against alienation, and the restriction is contained in the very agreement recording the right*, for in such a case the right itself is limited by the stipulation against alienation and can be relied upon by the debtor for whose benefit the stipulation was made.[431] [My emphasis]

Thus, according to Botha JA, an interest is not required to be present when the *pactum de non cedendo* is created at the same time that the contractants enter into the agreement.

Botha JA concluded that condition one did constitute a *pactum de non cedendo* as Trust Bank, for whose benefit the condition was made, had a clear interest in the prohibition and the bank could raise this defence against any action instituted by the cessionary.[432]

That question having been answered, Botha JA turned to answering the next question of whether the prohibition, subject to which the deposit vouchers were issued, related only to the document recording the right, or whether it could also be said that the prohibition related to the rights evidenced in the vouchers.[433]

The judge's response to this question was that condition one of the deposit vouchers did, indeed, reflect an attribute of the rights recorded therein, *viz*, that they are 'neither transferable nor negotiable'.[434] The

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[431] Supra 189D-F.

[432] Supra 189H.

[433] Supra 189H and 190A.

[434] Supra 190C.

reason was that if it were not the case, '…it would be difficult to appreciate what object the appellant intended to achieve with the stipulation against transfer'.[435]

Botha JA further added that:

> …[T]he words 'neither transferable nor negotiable'…should be given their ordinary literal meaning, namely that they are not to be transferred – in the only way in which they are capable of being transferred in law, i.e. by cession under the common law – from one person to another.[436]

Is the judgment of Botha JA a departure from the *ratio* as laid down by the Appellate Division in *Paiges v Van Ryn Gold Mine Estates*? Can the interest requirement be disregarded if the *pactum de non cedendo* is created in the agreement recording the right? This question is not settled as can be seen from the cases that follow.[437]

In ***Italtrafo SpA v Electricity Supply Commission,***[438] Escom was successful in its application to attach *ad fundandam jurisdictionem* a personal right which Italtrafo had against Escom. Italtrafo subsequently applied for the setting aside of this attachment on the ground that at the time Escom made the application for attachment, the right was no longer a part of Italtrafo's estate, since it had ceded the right in *securitatem debiti* to the Bank of Naples.

Escom, however, argued that the contract between Italtrafo and Escom contained a *pactum de non cedendo* in terms of which:

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[435] Ibid.

[436] Supra 191B-C.

[437] The recent case of *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd* 2008 (4) SA 510 (C) appears, however, to have interpreted *Trust Bank* as a departure and in fact relies on this departure in its judgment. The Appeal Court has yet to pronounce on the issue, so the matter is still uncertain.

[438] 1978 (2) SA 705 (W).

> …[Italtrafo] shall not assign or make over the contract or any part thereof or any share or interest therein to any other person without the written consent of Escom which may be refused without any reason being given.[439]

Escom asserted that no written consent was given to Italtrafo and that the cession to the Bank of Naples was consequently invalid.

King AJ, who presided over the case, summarised the *ratio* of *Paiges v Van Ryn Gold Mine Estates* as follows:

> …[S]uch a restraint will be enforced against a party claiming to be a cessionary if the debtor had a material and reasonable interest in making the stipulation.[440]

King AJ subsequently looked at the facts of the case and pointed out that Escom employed the services of a skilled manufacturer for the production of large pieces of equipment. Escom would use that equipment for the production of its goods and services and it would cause Escom great loss if such equipment was defective.[441] The judge thereafter concluded that Escom 'must have a material and reasonable interest' in the *pactum de non cedendo*.[442]

With reference to *Trust Bank v Standard Bank*, King AJ summed up the possible departure made therein as follows:

> …[W]here the restriction against the transfer of the rights formed part of the contract in question, the person claiming to be the cessionary could not acquire the cedent's rights without the debtor's consent. Any rights obtained by the person claiming to be the cessionary would be subject to such a restraint.[443]

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[439] Supra 708D.

[440] Supra 710G.

[441] Supra 710H.

[442] Ibid.

[443] Supra 710H-711A.

The judge also expressly stated that *Trust Bank v Standard Bank* seemed to have departed from the interest test as established in *Paiges*.[444] King AJ offered no further comment on the issue and in one simple sentence followed the new precedent:

> As I have already found as a matter of probability that the restraint against cession formed part of the contract in respect of the transformer… the cession is not a valid one.[445]

The court in *Italtrafo SpA* is clearly of the opinion that the *ratio* in *Trust Bank v Standard Bank* amounted to a departure from *Paiges*. Having said that, it has to be mentioned that *Italtrafo SpA* has itself deviated slightly, in a different way, from the *ratio* in *Paiges*.

In *Paiges*, Gregorowski J in the Transvaal Provincial Division explained that for the *pactum de non cedendo* to be valid the debtor had to have 'some interest'.[446] Wessels J, in turn, stated that the restriction must be 'in favour of a particular person'[447] or that the restriction had to be to the 'benefit'[448] of the debtor. In the Appellate Division De Villiers JA, citing Sande and Voet with agreement, held that the debtor must have 'an interest'[449] and further stated that the restriction must serve a 'useful purpose'.[450] To emphasise the degree of Van Ryn Gold Mine Estate's interest, De Villiers JA described it as a 'very real interest'.[451]

[444] Supra 711A.

[445] Supra 711A-B.

[446] Supra 604.

[447] Supra 606, 607 and 608.

[448] Supra 609.

[449] Supra 615.

[450] Ibid.

[451] Ibid.

In the same vein, with reference to *Paiges*, Lewis J in *Northern Assurance Company Ltd v Methuen* spoke of the restriction serving a 'useful purpose'.[452]

In keeping with the trend and with reference to *Paiges*, Blackwell J in *Du Plessis v Scott* held that the debtor must have 'an interest'.[453] To emphasise the degree of Scott's interest, Blackwell J described it as a 'genuine interest'.[454]

Similarly, Botha JA in *Trust Bank v Standard Bank*, citing Sande and Voet with approval, held that the debtor must have 'an interest'[455] or that the restriction must be to the debtor's 'benefit'.[456] To emphasise the degree of Trust Bank's interest, Botha JA described it as a 'clear interest'.[457]

King AJ in *Italtrafo SpA* did not speak of the interest requirement in any of the abovementioned terms, but instead held that the debtor must have a 'material and reasonable interest in making the stipulation'.[458] It is interesting to note that the judge made that statement with direct reference to *Paiges v Van Ryn Gold Mine Estates*.

The term 'material and reasonable' interest, however, does not appear anywhere in *Paiges*, nor does the term appear in any of the cases that follow. Further, Sande and Voet spoke of 'an interest', 'some interest', and 'any interest'.[459] Sande also expressly stated that:

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[452] Supra 111.

[453] Supra 465.

[454] Supra 466.

[455] Supra 189E.

[456] Supra 189F and 189H.

[457] Supra 189H.

[458] Supra 710G.

[459] See Chapter 1.

> Now, the interest of the person making such a pact should not be too strictly judged; for he has sufficient interest who can in every case say that he would not otherwise have alienated his property.[460]

Surely 'material and reasonable' does not mean the same as 'an interest', 'some interest', 'any interest', 'in favour of', 'useful purpose', 'to the benefit of'. The question may rightfully be asked whether this is a new interpretation of the interest requirement? If so, has it effectively increased the standard of proof?

Where the debtor could ordinarily show that he had an interest or at least some interest in the restriction, must he now go further and prove that the degree of this interest is in fact material and reasonable. Is this new interpretation not judging the interest too strictly – something Sande expressly advised against?[461]

Two years after *Italtrafo SpA* the *pactum de non cedendo* came under discussion again in the Transvaal Provincial Division where three concurring judges decided the case; and the outcome was rather noteworthy.

In ***Vawda v Vawda and others***,[462] the Community Development Board sold Mr Vawda certain immovable property, the purchase price of which was to be paid off in instalments. Clause 11 of the agreement read as follows:

> During the currency of this agreement the purchaser shall be bound and obliged personally to occupy the property hereby sold, and he shall not, without the written consent of the seller having been first had and obtained, let, lease, mortgage, assign or pledge or in any way encumber the property or any part thereof, nor pass any general bond or any bond containing a general

[460] *De Prohibita* 4 1 7. See Chapter 1.

[461] See also Chapter 4 where this particular issue is briefly mentioned again.

[462] 1980 (2) SA 341 (T). See also Chapter 4.

clause or cede, transfer, or make over his rights under this agreement.[463]

After purchasing the property Mr and Mrs Vawda occupied the property and Mrs Vawda paid some of the monthly instalments. Some time later matrimonial difficulties arose between the couple and Mrs Vawda learned that her husband was attempting to sell the property to finance his emigration.

To prevent the sale, Mrs Vawda agreed to give Mr Vawda R2000 in exchange for him ceding all rights and interest in the property to her. Despite having ceded all rights and interest in the property, Mr Vawda sold the property to a third party.

Upon becoming aware of this information, Mrs Vawda applied for an interdict prohibiting transfer to the third party.

The application was dismissed by Nicholas J in the court *a quo* on the ground that the cession to Mrs Vawda was not valid.[464] Mrs Vawda consequently appealed to the full bench where Boshoff AJP delivered the unanimous judgment.

Boshoff AJP considered Mrs Vawda's argument, which centred around the viewpoint that clause 11, the *pactum de non cedendo*, was invalid and ineffective.[465] Relying on *Paiges v Van Ryn Gold Mine Estates*, *Trust Bank v Standard Bank* and *Italtrafo SpA v Electricity Supply Commission*, Mrs Vawda contended that a *pactum de non cedendo* is only binding if it can be shown that the restriction serves a 'useful purpose' to the debtor.[466]

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[463] Supra 343.

[464] Supra 344F-G.

[465] Supra 345B-C.

[466] Supra 345C-D.

The argument continued that the onus of proving the nature and degree of the interest rests upon the party seeking to enforce the *pactum de non cedendo*.[467] According to *Du Plessis v Scott*, so the argument went, the court may look at the contract itself to determine if an interest exists. It was contended that if the present contract was carefully examined, no reason could be found upon which an interest for the Community Development Board could exist.[468]

Further, the party in a position to claim an interest was not Mr Vawda, but the Community Development Board and the latter had made no attempt to establish such interest. Thus, due to the fact that no interest was present, the *pactum de non cedendo* should be held to be invalid and ineffective.[469]

Relying on *Paiges v Van Ryn Gold Mine Estates*, Boshoff AJP's point of departure to this argument was that the entire agreement of sale must be looked at in order to determine the extent of Mr Vawda's rights thereunder.[470]

The judge however felt that, although Mrs Vawda's argument regarding the interest requirement was correct, the defect therein was that it considered the *pactum de non cedendo* to be something separate from the agreement of sale, when in fact, the *pactum de non cedendo* is 'part and parcel of the agreement creating the right, and the right is limited by the stipulation'. [471] [472]

Boshoff AJP held that apart from the interest requirement, one should also keep in mind the contents of 4 1 1, 4 1 6 and 4 1 7 in Sande's *De*

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[467] Supra 345D.

[468] Supra 345E-F.

[469] Supra 345F-G.

[470] Supra 346A.

[471] *Paiges* supra 617.

[472] Supra 346A.

Prohibita.[473] With reference to the views of Botha JA in *Trust Bank* Boshoff AJP subsequently added that:

> … [the judge] recognised this difference and did not depart from the test of material and reasonable interest laid down in *Paiges*' case as suggested by King AJ in *Italtrafo SpA v Electricity Supply Commission*.[474]

The judge thereafter concluded that clause 11 indeed amounted to a valid and enforceable *pactum de non cedendo* and the cession to Mrs Vawda was consequently invalid and unenforceable.

Two noteworthy points can be learned from this case. The first is that the judge followed the new precedent of 'material and reasonable' interest as expressed by King AJ in *Italtrafo SpA*.

The second is that contrary to what was held in *Italtrafo SpA,* Boshoff AJP was of the opinion that *Trust Bank v Standard Bank* did not, in fact, amount to a departure from *Paiges*.

In the same year that *Vawda v Vawda* was decided, the *pactum de non cedendo* was again before the Appeal Court in the *MTK Saagmeule* case. Perhaps the time was right for the Appeal Court to provide clarity on the standard of the interest requirement and shed some light on the question of whether *Trust Bank* was a departure from the *ratio* in *Paiges*.

In ***MTK Saagmeule (Pty) Ltd v Killyman Estates (Pty) Ltd***,[475] the Department of Forestry accepted a tender by Killyman Estates to purchase wood from two farms that was to be harvested and removed. On 18 July 1973 the parties entered into a contract of sale which was subject to numerous written conditions. One such condition was contained in

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[473] Supra 346D-H. See Chapter 1.

[474] 346H.

[475] 1980 (3) SA 1 (A).

clause 27 and stated that the purchaser was prohibited from ceding his rights under the contract without the written consent of the seller.[476]

The operation of the contract was from 1 August 1973 to 31 July 1975.

On 11 January 1974 Killyman Estates entered into a contract with MTK Saagmeule. In terms of the contract, Killyman Estates was to assign to MTK Saagmeule all rights, obligations and liabilities under its contract with the Department of Forestry. Killyman Estates was to continue making payments to the Department and MTK Saagmeule was to pay Killyman Estates a certain sum of money and to harvest and remove the wood.

The Department was unaware of the cession and thus did not give its written consent thereto. MTK Saagmeule subsequently fell behind schedule in its harvesting and removal of the wood. Killyman Estates approached the Department requesting an extension of the contract. It was during this time (around April 1975) that the Department became aware of the cession. The Department refused to grant Killyman an extension on the ground that Killyman Estates had breached their contract by contravening clause 27.

The court *a quo* held that the agreement between the parties was valid and enforceable, that they had never intended a full substitution and consequently gave judgment in favour of Killyman.

MTK Saagmeule appealed, alleging that the intention of the parties was that a cession would be effected. MTK Saagmeule's argument was that because the Department did not give its consent to the transfer, the contract between MTK Saagmeule and Killyman Estates was void.[477]

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[476] Supra 8H.

[477] Supra 9H.

It argued further that the effect of a *pactum de non cedendo* in this case was that a cession without the written consent of the debtor would be invalid. There were however, as MTK Saagmeule's argument went, two exceptions.[478]

The first, on the authority of *Trust Bank* and *Italtrafo SpA*, was where the prohibition of transfer was encapsulated in the agreement which created the right. The second, with *Paiges* and *Du Plessis* as authority, was where the party who benefited from the inclusion of the *pactum de non cedendo* had a material and reasonable interest ('wesenlike en redelike belang') therein.[479]

Against this background MTK Saagmeule asserted that the *pactum de non cedendo* in the present case was indeed encapsulated in the written agreement, that the Department of Forestry quite clearly had an interest in the prohibition and the *pactum de non cedendo* was consequently valid.[480]

Rumpff CJ, handing down the unanimous decision, held that the *pactum de non cedendo* argument put forward by MTK Saagmeule was unacceptable on two grounds.[481] The first ground was that the present case was not an instance of the cessionary suing the debtor – as was the situation in all the cases relied upon by MTK Saagmeule in its argument.[482]

The judge explained that in the present case the cessionary was suing the cedent and in this regard the cedent cannot respond to a *pactum de non cedendo* argument as the *pactum de non cedendo* was not included in the contract for his benefit and he thus has no interest therein. Also, the

[478] Supra 9H-10A.

[479] Supra 10A-C.

[480] Ibid.

[481] Supra 10D.

[482] Supra 10E.

pactum de non cedendo encapsulated in the agreement creating the right was between the cedent and the debtor and not the cessionary.[483]

The second ground for Rumpff CJ finding that the argument was unacceptable was that even if MTK Saagmeule sued the Department of Forestry, the latter would be able to rely on the fact that the cession was unenforceable due to an absence of written consent.[484]

The judge explained that it would make no difference if MTK Saagmeule sued the Department of Forestry because the cession to MTK Saagmeule would still have been invalid; not on the basis of a *pactum de non cedendo*, but on the basis of non-compliance with a contractual formality. The *pactum de non cedendo* accordingly had no scope to feature in the present case and the argument as submitted by MTK Saagmeule was of no relevance.[485]

It must be mentioned that the Appeal Court unfortunately had no reason to provide clarity as to the standard of the interest requirement or to decide whether or not *Trust Bank* departed from *Paiges*, since it had ruled out the application of the *pactum de non cedendo*. Any comments made by the court in this regard can be seen as *obiter dictum* at best.

Interestingly enough, the Appeal Court added another ground for invalidity. According to the reasoning of the court, a contractant wishing to include a *pactum de non cedendo* in an agreement can avoid the complex legal rules that accompany it, for the purpose of interpreting its validity and effect, by merely stipulating in the contract that a cession shall be subject to written consent. In this manner, any cession in contravention thereof will be found to be invalid simply on the basis of non-compliance with a contractual formality.

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[483] Supra 10E-G.

[484] Supra 10H-11A.

[485] Ibid.

This alternative, however, may not be a reliable solution as it depends upon how a particular judge will view the matter. Boshoff AJP in *Vawda v Vawda* took a completely different approach.

In the *Vawda* case, clause 11 in the contract between Mr Vawda and the Community Development Board stated that Mr Vawda was prohibited from ceding his rights without first obtaining the written consent of the Board. This case is very similar to *MTK Saagmeule* as in both instances written consent was required before a cession could be effected.

The very stark difference between the cases is that Boshoff AJP in *Vawda v Vawda* made absolutely no mention of non-compliance with a contractual formality, even though this alternative would have very simply resolved the issue. Instead, Boshoff AJA reviewed the relevant cases and decided, with the aid of *Paiges*, that because the *pactum de non cedendo* was 'part and parcel of the agreement creating the right', the right was limited by the stipulation.[486]

Surely this new found ground for invalidity would be made use of by contractants and argued by litigants in the future?

In the case of ***Govender v Tongaat Town Clerk and others***,[487] the third respondent concluded a contract with the Town Board of the Township of Tongaat. In terms of the contract the third respondent purchased immovable property for a sum payable by monthly instalments.

The third respondent's rights in the immovable property were attached at the instance of the applicant and were sold in execution. At the sale in execution the applicant purchased the third respondent's rights in the property and was eager to pay the balance owing under the contract.

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[486] Supra 346.

[487] 1986 (4) SA 184 (D).

The Town Clerk, however, argued that the applicant's purchase was not valid and that he was not obliged to transfer the property to the applicant. The Town Clerk relied on clause 12 of the contract between him and the third respondent which, according to the Town Clerk, protected the third respondent against his rights being sold at a sale in execution and purchased by a third party. Clause 12 read as follows:

> During the term of this agreement the purchaser shall be bound and obliged personally to occupy the property continuously and as his place of residence, together with the persons approved in writing by the seller and nominated in the application submitted by the purchaser to the seller in connection with the acquisition of property, the truth and correctness of which application the purchaser hereby warrants as correct. The purchaser shall be deemed to be in breach of this agreement if any information contained in such application transpires to be incorrect. The purchaser shall not, without the written consent of the seller first having been had and obtained let, part with possession of or any portion of the property or make over his rights under this agreement or purport to do any of the aforegoing. If the purchaser does any of the foregoing he shall be deemed to be in breach of this agreement.[488]

The Town Clerk and the third respondent contended that clause 12 amounted to a *pactum de non cedendo* and relying on *Vawda v Vawda*, argued that the *pactum de non cedendo* could be enforced against the applicant as its effect was expressly, or alternatively impliedly, to preclude a sale in execution.[489]

The applicant consequently applied to the court for a declaratory order declaring that the purchase was valid and that transfer should be effected.

The case came before Friedman J, who disagreed as to the express interpretation of clause 12. The judge was of the opinion that clause 12

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[488] Supra 185F-H.

[489] Supra 185H-J.

clearly and unambiguously prevented the third respondent himself from ceding his rights under the contract.[490]

Friedman J held that the third respondent did not play an active role in the sale of the rights, nor was the messenger of the court who sold the rights to the applicant acting as the third respondent's agent. The messenger of the court was, in fact, disposing of the third respondent's rights in accordance with the statutory duty imposed upon him.[491]

As to the implied interpretation of clause 12, the judge held that although he could understand how such an implied interpretation might be reasonable, such an implied interpretation could not be recognised in the interest of business efficacy.[492]

Relying on *Paiges v Van Ryn Gold Mine Estates*, the judge stated that:

> In other words, it seems to me that the prohibition contained in clause 12 contemplates only something in the nature of a voluntary relinquishment by the third respondent of his rights and not a forced loss of those rights such as occurred at the sale in execution.[493]

Friedman J concluded that since there was no merit in the Town Clerk and the third respondent's argument, the purchase was valid and the Town Clerk was ordered to effect transfer.

It is interesting to observe that the new ground for invalidity came before this court some six years after *MTK Saagmeule*. The Town Clerk and the third respondent could have argued that because the required prior written consent was not obtained the cession was invalid due to non-compliance with a contractual formality. The latter, however, did not rely on this

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[490] Supra 186A-B.

[491] Supra 186B-D.

[492] Supra 186D-E.

[493] Supra 186F.

argument. Perhaps the facts in this case did not justify such a reliance as clause 12 provided that the contract would be breached if consent was not first obtained. That having been said, no other case to my knowledge uses or makes reference to this new ground of invalidity.

The case does raise another important question: Is a trustee on insolvency or deputy-sheriff of the court bound to a *pactum de non cedendo*? Judging from the approach of Friedman J in *Govender v Tongaat Town Clerk*, the terms of the contract should be considered to determine this. Other cases have also discussed this issue.

In ***Lithins v Laeveldse Koöperasie Bpk and another***,[494] Lithins sued the Laeveldse Koöperasie for the recovery of damages which arose from a breach of the contract between it, as seller of timber, and ARC Mining Timber (Pty) Ltd, as purchaser.

ARC Mining Timber was duly wound up and the liquidator ceded to Lithins the claim for damages that ARC Mining Timber had against Laeveldse Koöperasie. Laeveldse Koöperasie, however, denied the validity of the cession on the basis that the contract between it and ARC Mining Timber contained a *pactum de non cedendo* in clause 10 that was subject to prior written consent, which was not obtained.

After considering the case law on the issue, Olivier J who presided over the matter, stated the following:

> I think it can safely be deduced from these cases that there is a general principle in our law to the effect that the *pactum de non cedendo* does not bind the trustee or liquidator in insolvency, unless it appears in a lease, in which case s37(5) of the Insolvency Act applies, or unless it appears from the *pactum* that it would also be applicable in the case of insolvency. In the latter case, the question will then arise whether such a wide clause is valid.[495]

[494] 1989 (3) SA 891 (T). See Chapter 5 for a further discussion.

[495] Supra 895H.

Olivier J held that in the present case there was nothing in clause 10 which would have the effect of extending the *pactum de non cedendo* to the liquidator in insolvency.[496]

He further added that the contract prohibited cession by one of the parties to the contract and since the liquidator was not one of the parties to the contract he could not be bound thereby.[497] Lithins thus succeeded in being allowed to bring the action for damages against Laeveldse Koöperasie.

This case illustrates that where the *pactum de non cedendo* appears in a lease, the trustee on insolvency would be bound as if he were the lessee due to s37(5) of the Insolvency Act.[498] If the contract is one of a general nature and not a lease, then the trustee would only be bound if the *pactum de non cedendo* specifically stated that it should apply in the case of an involuntary cession.

In ***Britz NO v Sniegocki and others***,[499] the court dealt with *pacta de non cedendo* appearing in the transfer of shares. Sniegocki and Van Lingen were partners in a business and on 7 November 1986 they agreed that Sniegocki would sell her 40% share in the business to Van Lingen. They also agreed that she would lend Van Lingen R8 000.

Hawthorne owned shares in Point Smith Shareblock Ltd and, acting as surety and co-principal debtor, pledged these shares to Sniegocki as security for Van Lingen's monetary obligations arising out of the sale of the business and the loan. Hawthorne subsequently delivered the share

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[496] Supra 895I.

[497] Ibid.

[498] Act 24 of 1936.

[499] 1989 (4) SA 372 (D). See Chapter 5 for a further discussion.

certificate to Sniegocki, with the company being unaware of the security cession.

On 1 April 1987 and unbeknown to Sniegocki, Hawthorne entered into an agreement with the second claimant whereby he sold him the same shares that he had pledged to Sniegocki. Hawthorne subsequently handed to the second claimant, *inter alia*, a declaration to the effect that the share certificate had been lost, mislaid or destroyed; a completed and signed share transfer form; and written consent to the transfer granted by the directors of Point Smith Shareblock Ltd.

Some time later Sniegocki issued a writ resulting in Britz, the deputy-sheriff, attaching the shares in execution of debt. The second claimant, however, disputed Sniegocki's claim to the shares and sought an order that the attachment be set aside and a declaration that he be entitled to the shares.

The second claimant argued, *inter alia*, that according to Point Smith Shareblock Ltd's articles of association, the company's consent was required before shares could be ceded, and because Hawthorne had not obtained the company's consent, the pledge was not effective.[500]

Booysen J delivered the written decision and noted that article 10(b) of the company's articles of association read as follows:

> Save as otherwise provided in these articles, no share may be transferred to any transferee without prior consent and approval of the directors of the company, which consent shall not, however, be unreasonably withheld.[501]

Sniegocki's response to this, as Booysen J recounted, was that article 10(b) does not render rights incapable of cession without the consent of

[500] Supra 376A-B.

[501] Supra 381B.

the company, as the articles of association does not operate as between the cedent and cessionary.[502] Rather, article 10(b) operates as between the company and the purported cessionary seeking to obtain registration.[503]

In essence the argument was that article 10(b) can have no effect on a pledge or cession *in securitatem debiti* itself; the article only finds effect when the cessionary or pledgee attempts to register the shares in the register of members.[504]

On the strength of the *ratio* in *Paiges v Van Ryn Gold Mine Estates* and *Trust Bank v Standard Bank,* the judge agreed that, as a general rule, all contractual rights – including shares – may be freely ceded. Using the aforementioned two cases and *Friedlander v De Aar Municipality* as authority, he added that freely cedable rights may not be freely cedable if subject to a *delectus personae* or a valid *pactum de non cedendo*.[505]

He explained that a *pactum de non cedendo* can also function to restrict transfer; it does not only function to render a right absolutely intransferable.[506] To illustrate this, he used the example of a situation where a right may not be ceded without the consent of the debtor.[507] In this example there is a possibility of transfer, *viz*, if the debtor consents to it. On the other hand, a prohibition that is not subject to consent or any other requirement first being fulfilled holds no possibility of a cession and the right would thus be absolutely intransferable.

[502] Supra 381D.

[503] Ibid.

[504] Supra 381E.

[505] Supra 382E-F.

[506] Supra 382F-G.

[507] Ibid.

Booysen J held that the freely cedable nature of Hawthorn's shares had to be subject to the restriction in the company's articles of association.[508] The judge rejected Sniegocki's argument and held that article 10(b) does in fact prevent a pledge or cession *in securitatem debiti* of the shares.[509]

Booysen J concluded that:

> It seems to me that the rights constituting the shares were created with conditional restrictions against alienation. These restrictions are contained in the document recording it and the right itself is limited by the conditional stipulation against alienation.[510]

According to the judge, owing to article 10(b) of the company's articles of association, Hawthorn could not pledge or cede the shares without prior consent of the directors and because such consent was not obtained, the transfer was 'incomplete' or 'ineffective'.[511] The judge consequently ruled in favour of the second claimant.

In the case that followed the court was once again faced with the effect of a *pactum de non cedendo* in a case of insolvency. The question, however, was not whether the trustee of an insolvent estate was bound by a *pactum de non cedendo*, but whether the deputy-sheriff of the court was bound.

In ***Van der Berg v Transkei Development Corporation***,[512] the deputy-sheriff sold shares in a private company, Three Crowns Wholesale Supermarket (Pty) Ltd, in a sale in execution to Transkei Development Corporation.

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[508] Supra 382G.

[509] Supra 382H-383B.

[510] Supra 383B.

[511] Supra 383D-E.

[512] 1991 (4) SA 78 (Tk). See Chapter 5 for a further discussion.

One of the existing shareholders of Three Crowns Wholesale Supermarket (Pty) Ltd, Van der Berg, brought an application to determine whether the deputy-sheriff's sale was subject to the terms of the articles of association of the company.

White J handed down the brief judgment, the outcome of which was the same as in *Britz v Sniegocki*, although that case was never mentioned.

White J stated that a private company is, in terms of s20 of the Companies Act,[513] compelled to restrict the transfer of its shares.[514] Article 11 of the articles of association of Three Crowns Wholesale Supermarket (Pty) Ltd stated that the directors had the power to refuse to register a transfer of shares[515] and article 22 obliged a member wishing to sell his shares to offer it first to the existing members, thus giving existing members a right of pre-emption.[516]

White J considered possible constructions of the sale of the shares,[517] but concluded that irrespective of which construction was favoured, in each case the requirement of the articles of association still found application. The judge therefore held that the requirements as set out in the articles of association had to be met before the shares could be registered in the name of Transkei Development Corporation.[518]

The deputy-sheriff of the court was therefore bound by the provisions of the articles of association which amounted to a *pactum de non cedendo*, even though, as held in *Lithins*, the *pactum de non cedendo* did not specifically state that it should apply in the case of an involuntary transfer.

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[513] 61 of 1973.

[514] Supra 79D-F, 80A-B.

[515] Ibid.

[516] Ibid.

[517] Supra 80D-F.

[518] Supra 81G.

Why should different rules apply to the trustee on insolvency? This question had an opportunity to be addressed in the following case.

In the case of ***Goodwin Stable Trust v Duohex (Pty) Ltd and another***,[519] Goodwin Stable Trust had entered into a building contract with Woodmill Homes Trust, which was sequestrated just before the building was completed. Amongst the assets of Woodmill Homes Trust were monetary claims against Goodwin Stable Trust in respect of work done on the building construction.

The trustee of the insolvent estate ceded Woodmill Homes Trust's claims against Goodwin Stable Trust to Duohex (Pty) Ltd. Consequently, Goodwin Stable Trust brought an application that the court declare the cession unenforceable against it, *inter alia*, on the ground that clause 19 of the building contract contained a *pactum de non cedendo* which tacitly included the trustee on insolvency.

Judgment was given by Selikowitz J, who relied on *Lithins v Laeveldse Koöperasie* for holding that a trustee in insolvency is not bound by a *pactum de non cedendo* unless perhaps it is clear that the parties to the agreement intended it to bind the trustee.[520]

The judge also noticed that Olivier J in *Lithins v Laeveldse Koöperasie* seemed to be doubtful of the possibility of the parties extending the application of the *pactum de non cedendo* to the trustee, who has a statutory duty to administer the insolvent estate by making the most financially sound decisions in favour of the insolvent estate and in the best interest of the creditors.[521] Olivier J, as the judge observed, left the question open.[522]

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[519] 1996 All SA 558 (C). See also Chapter 5.

[520] Supra 563I.

[521] Supra 563I-J.

[522] Ibid.

Selikowitz J was of the opinion that there was nothing in the interpretation of clause 19 to lead him to conclude that its application extended to the trustee on insolvency. The judge therefore held that the cession was valid and enforceable against Goodwin Stable Trust. Unfortunately, nothing was said in this case to correct the inconsistency.

The effect of a *pactum de non cedendo* on the cession of shares came under scrutiny once more in the case of ***Smuts v Booyens*; *Markplaas (Edms) Bpk en 'n ander v Booyens*.**[523] Markplaas (Edms) Bpk was incorporated in 1983 with Smuts and Roux as the promotors, equal holders of the issued shares, as well as the sole directors.

In 1993 Roux entered into an agreement with Booyens whereby Booyens would buy Roux's shareholding in Markplaas. This agreement was entered into without Smuts's knowledge and was in conflict with a right of pre-emption in the articles of association of the company.

In January 1994 Roux signed an agreement in terms of which he ceded his shares as security for a loan. Roux was provisionally liquidated in September 1994 and in October 1994 the sequestration order was made final. Roux subsequently collected the share certificate from Markplaas's auditors and delivered it to Booyens.

In the court *a quo* an application for the setting aside of the sale agreement was brought, *inter alia*, by the trustee of Roux's insolvent estate and Smuts. The trustee later ceased to be a party, so his objection was no longer in issue.

Smuts's objection to the sale agreement, which was still in issue, was founded on the ground that Roux had failed to adhere to Markplaas's articles of association regarding the sale of shares. The court *a quo* held

[523] 2001 (4) SA 15 (SCA). See Chapter 5 for a further discussion.

that the mere agreement of sale made Booyens entitled to the shares and *prima facie* entitled, therefore, to have his name entered into the register of members.

Smuts consequently appealed, arguing once again that the company's articles of association created an agreement not to transfer the rights (a *pactum de non cedendo*) and that failure to comply with the procedure laid down in the articles of association precluded Booyens from becoming entitled to the shares.

Cameron JA delivered the unanimous judgment.

The judge explained that s20 of the Companies Act[524] obliges a private company in its articles of association to place restrictions on the right to transfer its shares,[525] and that this restricted transferability is an essential characteristic of a private company. [526]

Cameron JA made it clear that the restriction on transfer in the Companies Act meant that 'transfer' in the 'full' and 'technical' sense of the word is restricted.[527] Transfer, the judge said, comprises of a series of steps, *viz*, an agreement to transfer, the execution of a deed of transfer, and the registration of the transfer.[528] If the restrictions imposed by the Act and the articles of association of the company (which encompass this threefold meaning of the term 'transfer') are not complied with, then according to the judge, the shares are not transferable at all.[529]

[524] 61 of 1973.

[525] Supra 21A-D.

[526] Supra 21D.

[527] Supra 21G.

[528] Supra 21H relying on the words of Rumpff JA in *Inland Property Development Corporation (Pty) Ltd v Cilliers* 1973 (3) SA 245 (A) 251C.

[529] Supra 22D ('glad nie oordraagbaar nie').

The judge stated that articles 21 - 24 of the model articles of association contained in Table B of Schedule 1 of the Act contain restrictions on the transfer of shares.[530] He stated if a private company adopts the model articles of association a contract is created between the shareholders and according to s20, their right to transfer the company's shares is limited by requiring that the stated procedure in articles 21 – 24 to be first complied with before the shares may validly be transferred to a party who is not a shareholder. [531]

Cameron JA cautioned that if the procedure is not complied with, no rights in respect of the shares could be transferred to a purchaser.[532] The reason for this was because in such a case the right would 'from its inception, lack the attribute of transmissibility'.[533] In finding favour with the argument of Smuts the judge held that Table B of Schedule 1 therefore contains an absolute prohibition in the form of a *pactum de non cedendo*.[534]

The Appeal Court thus authoritatively confirmed what was stated in earlier cases dealing with share transfer restrictions.

Recently the *pactum de non cedendo* once again arose in the context of insolvency.

In ***Any Name 451 (Pty) Ltd v Capespan (Pty) Ltd***,[535] Any Name 451 brought an application that it be substituted for Chance Brothers (Pty) Ltd and Club Champion Investments (Pty) Ltd as claimant in the latter company's arbitration proceedings against Capespan.

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[530] Supra 23B-G.

[531] Supra 24E.

[532] Supra 24F.

[533] Supra 24G with the judge quoting from *LAWSA*.

[534] Supra 24H-25A.

[535] 2007 JOL 19402 (C). See Chapter 5 for a further discussion.

Chance Brothers and Champion Investments entered into a marketing contract with Capespan and subsequently a dispute arose between the parties with the former alleging that Capespan had breached the contract.

Before the matter could be heard the two companies were liquidated. The liquidators were not interested in pursuing the pending proceedings, apparently since there were insufficient funds to do so. Any Name 451 was consequently incorporated for the purpose of acquiring and prosecuting the claim. The liquidators subsequently ceded to Any Name 451 all rights, title and interest in their claims against Capespan.

Capespan objected to the substitution on various grounds. The ground relevant to this discussion was to be found in clause 16 of the marketing contract between Capespan and the two companies. Clause 16 prohibited cession and read as follows:

> Save as herein expressly otherwise provided, neither this agreement nor any part, share or interest therein nor any rights or obligations hereunder may be ceded, assigned or otherwise transferred without prior written consent of the other party, provided that Capespan shall have the right to cede, assign or transfer this agreement, either in whole or in part, to an associated or subsidiary company of Capespan without the consent of the supplier. [536]

Zondi AJ adjudicated the matter and, relying on *Paiges v Van Ryn Gold Mine Estates*, held that the prohibition only contemplated a voluntary cession and did not find application where the cession was involuntary.[537] Thus, the *pactum de non cedendo* did not prevent the liquidators from ceding the right to Any Name 451.[538]

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[536] Supra 26.

[537] Ibid.

[538] Ibid.

Relying on *Lithins v Laeveldse Koöperasie Bpk and another*, Zondi AJ said:

> A *pactum de non cedendo* does not bind the liquidator who alienates and cedes the contractual right pursuant to his duties as liquidator in insolvency unless it appears in a lease, in which case section 37(5) of the Insolvency Act applies, or unless it appears from the *pactum* that it would also be applicable in the case of insolvency.[539]

After considering clause 16, the judge concluded that, since nothing in the clause indicated that the *pactum de non cedendo* was to bind any person other than the companies, it could not be construed as binding the liquidators on insolvency.[540] The liquidators were thus free to cede the right to Any Name 451.

This decision appears to be in line with what has been held in earlier cases. The noteworthy development in this regard occurred when Capespan appealed against the decision of the court *a quo*.

In the unanimous judgment in ***Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd***, [541] Thring J took an entirely different view, thereby reversing the outcome.

Thring J agreed with Zondi AJ that a *pactum de non cedendo* would not always prevent an involuntary cession and that there were instances where an involuntary cession would be ineffective.[542]

Thring J also agreed that two such instances, as explained by Zondi AJ, are when a lease contains a stipulation which prohibits the transfer of any right under the lease as set out in s37(5) of the Insolvency Act; and where

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[539] Ibid.

[540] Ibid.

[541] 2008 (4) SA 510 (C). See Chapter 5 for a further discussion.

[542] Supra 513A.

it is clear from the agreement prohibiting the cession that such a prohibition was to prevail in a case of insolvency.[543]

The judge was of the opinion that Zondi AJ had mistakenly overlooked a third possible instance where the *pactum de non cedendo* may triumph against insolvency.[544]

This oversight, it would seem, stemmed from Zondi AJ believing *Paiges* to be authority for the proposition that a *pactum de non cedendo* cannot prevent an involuntary cession.[545]

According to Thring J, De Villiers JA in *Paiges* was simply stating that a *pactum de non cedendo* could not prevent a right from vesting in the trustee upon insolvency as this occurs through the operation of law. According to the judge, De Villiers JA was not laying down authority that the *pactum de non cedendo* prevents an involuntary cession.

In building a foundation leading to the third instance, Thring J began by discussing the possible departure from the *Paiges* judgment by the court in *Trust Bank v Standard Bank*,[546] where that court held that where the prohibition against cession was created with the right an interest need not be proven as the right is limited by such a stipulation.[547]

The judge subsequently quoted Scott, one of the leading academics on the law of cession, who supports the *Trust Bank* departure. Scott suggests that where a right is created as non-transferable *ab initio*, even

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[543] Supra 513B-C.

[544] Supra 513C.

[545] Supra 513H – 514A. *Paiges* supra 616: 'But the prohibition only contemplates a voluntary cession and does not prevent the right to the wages vesting in the trustee in insolvency'.

[546] *Trust Bank* supra 189D-G.

[547] Supra 514C-F.

an involuntary cession is ineffective.[548] Thring J was in complete agreement with Scott's view for the reasons that it was consistent with the judgments of previous cases and the views of other academics, and that it gives effect to the principle of freedom of contract.[549]

Further, freedom of contract was the principle underlying the judge's statement that a trustee or liquidator can acquire no greater rights against the debtor than the creditor had before insolvency.[550] It was also the principle underlying the judge's view that *Lithins*[551] and other cases which state the law too broadly should be overruled.[552]

Thring J was thus of the opinion that Zondi AJ failed to recognise the third instance which exists if the *pactum de non cedendo* was inserted into the agreement creating the right from the outset.[553]

In conclusion, Thring J found that the *pactum de non cedendo* in this case was included in the agreement creating the prohibition *ab initio*. Accordingly, the liquidators were bound by the *pactum de non cedendo* and the judge consequently held that the cession by the liquidators was invalid and ineffective.[554]

The court in *Capespan* thus expanded the application of the *pactum de non cedendo* to the trustee in insolvency because now, if the personal right does not arise from a lease and if the *pactum de non cedendo* does

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[548] Supra 514G – 515B.

[549] Supra 515B-J.

[550] Supra 518D-E.

[551] *Lithins v Laeveldse Koöperasie Bpk and another* 1989 (3) SA 891 (T). A case expressly mentioned by Thring J was *Goodwin Stable Trust v Duohex (Pty) Ltd and another* 1998 (4) SA 606 (C).

[552] Supra 518F-H.

[553] Supra 518C-E. See Chapter 4 for a detailed discussion of the two possible constructions of the *pactum de non cedendo* – that is – either when appearing in the agreement creating the right *ab initio*, or when super-imposed on an already existing agreement at a later stage.

[554] Supra 521E-G and 521I-J.

not expressly include involuntary cessions, the trustee will still be bound if the *pactum de non cedendo* appeared in the agreement creating the personal right *ab initio*.

3.4 Conclusion

As can be observed from the above case discussions, there are many uncertainties in the principles governing *pacta de non cedendo*.

As has already been pointed out, the judgment in the leading case, *Paiges v Van Ryn Gold Mine Estates*, is not convincing, yet no court has attempted to correct it. No court since *Paiges* has even expressly suggested the possibility that the Appellate Division may have erred. This state of affairs is clearly unsatisfactory and academics have accordingly developed their own views of the rules governing *pacta de non cedendo*. This can be seen in the next Chapter which considers the views of the academics in detail.

CHAPTER FOUR

THE SOUTH AFRICAN ACADEMICS' VIEWS ON THE *PACTUM DE NON CEDENDO*

In Chapter 3 the courts' approach to *pacta de non cedendo* was discussed in detail. This Chapter considers academic opinion. In what follows, it shall be shown that the academics' views on *pacta de non cedendo* are not necessarily in line with the courts' view.

Ever since *Paiges v Van Ryn Gold Mine Estates*,[555] our courts have, for the most part, followed the position espoused by De Villiers JA: That a *pactum de non cedendo* is only valid and binding if the debtor can show that he has an interest in it. The effect of a valid *pactum de non cedendo* is that the personal right is rendered non-transferable. If the personal right is ceded in contravention of the *pactum de non cedendo*, such a cession is thus ineffective to transfer ownership of the right to the cessionary.[556]

Strangely enough, the *ratio* has rarely been criticised by other judges. The criticisms by academics, however, are in abundance. The main criticisms can be distinguished as follows:

4.1 The interest requirement and the two possible forms of *pacta de non cedendo*

The court in *Paiges v Van Ryn Gold Mine Estates* made no mention of the possibility that the *pactum de non cedendo* could manifest itself in different constructions. *Paiges* only recognised a *pactum de non cedendo* that was

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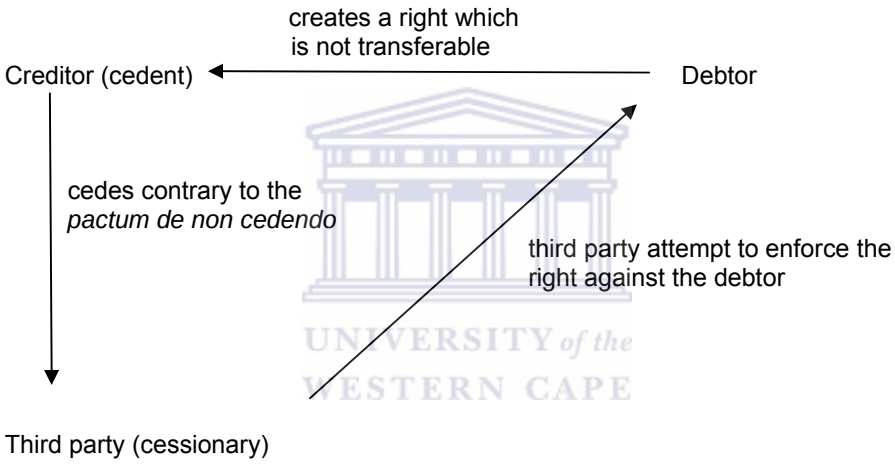
[555] 1920 AD 600.

[556] Presumably with an action for damages arising against the cedent for breach of contract.

entered into between the debtor and creditor at the time of creating the right.[557]

Trust Bank v Standard Bank[558] was the first case to recognise another possible construction,[559] although many courts refuse to follow this purported departure.[560]

According to Nienaber,[561] the first construction arises when the *pactum de non cedendo* is concluded between the debtor and the creditor at the time that the right is created.[562]



[557] Supra 617: 'The stipulation against cession is part and parcel of the agreement creating the right, and the right is limited by the stipulation'.

[558] *Trust Bank of Africa Ltd v Standard Bank of South Africa* 1968 (3) SA 166 (A) 189F.

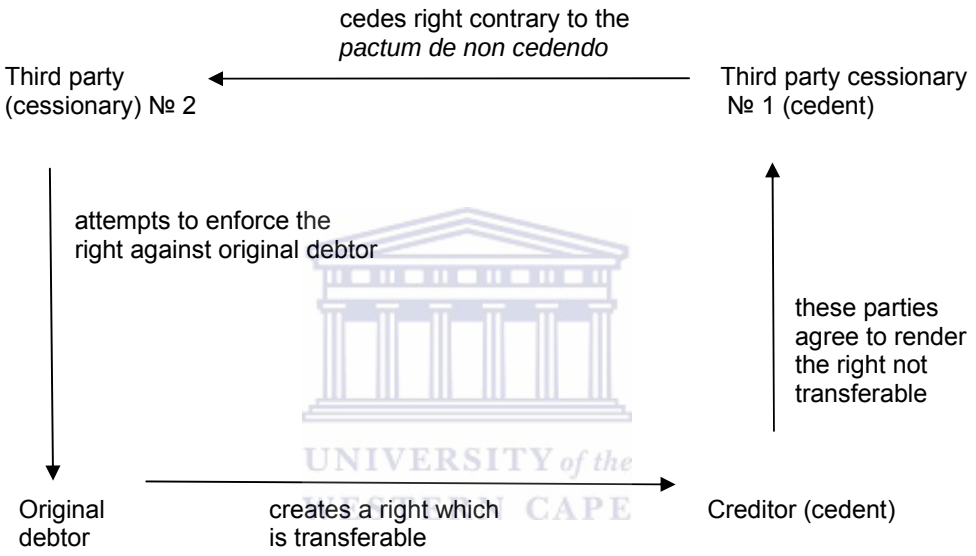
[559] King JA in *Italtrafo SpA v Electricity Supply Commission* 1978 (2) SA 705 (W) expressly agreed with that *ratio*. See also L Tager 'General principles of contract' 1978 *Annual Survey* 129.

[560] See *Vawda v Vawda* 1980 (2) SA 341 (T) and subsequent cases. Recently, a full bench in the case of *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd* 2008 (4) SA 510 (C) expressly accepted the two possible constructions. Whether this express recognition will be accepted by the Supreme Court of Appeal remains to be seen.

[561] PM Nienaber 'Cession' in *LAWSA* 2ed vol 2 (2003) para 37.

[562] S Van der Merwe et al *Contract General Principles* 2ed (2003) 443 footnote 165. This type of *pactum de non cedendo* is far more common than the alternative, probably because the alternative form has a limited scope of application. It is this construction which the court in *Paiges* recognised.

The second construction arises when the *pactum de non cedendo* is concluded between the cedent and the cessionary at the time that the agreement preceding or accompanying the cession was concluded.[563] In this construction the cedent and cessionary agree that the cessionary will not cede the right further. The original debtor, therefore, is not in the *pactum de non cedendo* equation.



In the first construction the restraint is 'a characteristic of the right itself and from its inception the right lacks transferability'.[564] In the second construction the restriction 'is superimposed on a right that already existed'.[565]

In recognising a second possible construction, the court in *Trust Bank v Standard Bank* necessarily departs from *Paiges* because with the

[563] Nienaber op cit para 37.

[564] Ibid.

[565] Ibid

recognition of the two possible constructions comes a differentiation regarding the validity of the *pactum de non cedendo*.

According to the *ratio* in *Trust Bank*, the interest requirement does not apply to the first construction, *viz*, the debtor does not have to show that he has an interest for the *pactum de non cedendo* to be valid; it is automatically valid:

> …[t]hese principles do not, however, apply where the right is created with a restriction against alienation, and the restriction is contained in the very agreement recording the right, for in such a case the right itself is limited by the stipulation against alienation and can be relied upon by the debtor for whose benefit the stipulation was made.[566]

Many of our academics have since favoured the existence of two possible constructions and the elimination of the interest requirement for the validity of the first construction.[567]

Van der Merwe et al[568] point out that if the majority of academics who are in support of the differentiation of the two constructions and the supposed departure by Botha JA in *Trust Bank* are to be followed by the Supreme Court of Appeal, then 'it would constitute a significant departure from the *Paiges* case' since 'in the majority of cases the *pactum de non cedendo* will be agreed upon by the parties *ab initio*'.[569]

In other words, Van der Merwe et al illustrate the fact that if it becomes settled law that the interest requirement can be done away with when the *pactum de non cedendo* is created from the inception of the contract, the interest requirement will disappear almost completely as most *pacta de*

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[566] *Trust Bank v Standard Bank* supra 189F.

[567] S Scott *The Law of Cession* 2ed (1991) 205 and 214 (hereinafter referred to as '*Cession*'). See also RH Christie *The Law of Contract in South Africa* 5ed (2006) 464.

[568] Van der Merwe et al op cit 443 footnote 165.

[569] Ibid.

non cedendo are inserted into a contract from its inception, as opposed to being super-imposed on the contract at a later stage.

In my opinion the *ratio* in *Trust Bank* indeed amounts to a departure from the legal principles laid down in the *Paiges* case. If the courts can be persuaded to accept this, no possible harm would come to the law of cession.

Since a *pactum de non cedendo* underlies an agreement, if contractants agree to the prohibition, why should the debtor have to show, over and above that consensus was reached, that he has an interest in the *pactum de non cedendo*?

4.2 The interest requirement and freedom of contract

The interest requirement has been described as limiting contractants' rights to freedom of contract: If a contractant does not have an interest in the *pactum de non cedendo* the cession may be held to be invalid, even though the contractants wish it to be valid.[570] Thus, the contractants' intentions are not given effect to with the result that the court imposes on the parties a contract they never wanted.

Lubbe and Murray[571] question why such an interest requirement exists for the validity of an ordinary contract. Roussouw[572] also asks why this particular prohibition should be treated differently from any other prohibition.

[570] *Paiges v Van Ryn Gold Mine Estates* supra 614 and 615, *Northern Assurance Co Ltd v Methuen* 1937 SR 103 111, S Scott 'Pacta de non cedendo' 1981 *Tydskrif vir Hendendaagse Romeins-Hollandse Reg* 159 (hereinafter referred to as 'Pacta'), RS Welsh 'General principles of contract' 1950 *Annual Survey* 81.

[571] GF Lubbe and CM Murray *Farlam & Hathaway: Contract Cases, Material and Commentary* 3ed (1988) 655.

[572] SR Roussouw 'Pacta de non cedendo' 1991 *Responsa Meridiana* 54-55.

Roussouw compares *pacta de non cedendo* to a limitation on the alienation of rights in the context of the law of things. He states that an owner's right to alienate may not only be limited by recognised real rights, but also by personal rights.[573] As examples, Roussouw lists an option, a right of pre-emption, a restraint on alienation or a fideicommissum.[574]

These restrictive personal rights are completely valid and some, the argument goes, are so strongly binding that they are perceived (from an historical and jurisprudential point of view) as an encumbrance on immovable property and can be registered as real rights.[575]

The conclusion that Roussouw reaches is that if these agreements are regarded as valid and can lead to legitimate personal rights, then there should be no reason why agreements which prohibit the transfer of a personal right should not be valid without the addition requirement of an interest.[576]

Roussouw makes a good point. If contractants in other instances are free to include as a term of their contract a particular prohibition, why must a burden be placed on the debtor to show that he has an interest when both parties wish to include a *pactum de non cedendo* as a term of their contract?

On the assumption that the contract is valid in every other respect, surely our courts should recognise the *pactum de non cedendo* as valid, regardless of the absence or presence of an interest? Is that not the cornerstone of the principle of freedom of contract ('*pacta sunt servanda*') to which our law subscribes?

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[573] Roussouw op cit 54.

[574] Ibid.

[575] Roussouw op cit 54-55.

[576] Roussouw op cit 55.

Not all academics are of the opinion that the interest requirement limits a contractant's freedom of contract. Welsh[577] questions the rationale of the interest requirement in relation to the case of *Du Plessis v Scott.*[578]

In that case the court held that it was unnecessary for the defendant to prove that the *pactum de non cedendo* was genuinely in his interest and not merely an idle stipulation, since this was obvious from the contract between the parties.

In view of the above, Welsh writes that:

> The decision may lead one to reflect whether this supposed 'limitation upon the freedom of contract' really has any practical content or significance in our law.[579]

De Wet and Van Wyk are of the opinion that no real meaning has been attached to the interest requirement as laid down in *Paiges* and that it is effectively an unconvincing argument.[580]

Admittedly, De Villiers JA in *Paiges* spoke only of the contractant having 'an interest'; no court has subsequently given any further explanation as to what 'an interest' means – except for one or two judges who, without giving any reasons, took it upon themselves to term 'an interest' a 'material and reasonable' interest,[581] also without giving any further useful explanation of the term.

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[577] Welsh op cit 82

[578] 1950 (2) SA 614 (W) 618.

[579] Welsh op cit 82.

[580] JC De Wet and AH Van Wyk *Kontraktereg* 4ed (1993) 254 footnote 16.

[581] *Italtrafo SpA v Electricity Supply Commission* 1978 (2) SA 705 (W) and *Vwada v Vawda* 1980 (2) SA 341 (T). See Chapter 3 where it is questioned whether a 'material and reasonable' interest is a new interpretation which raises the debtor's standard of proof. It appears that only the case of *Vawda* has since used this term. Further, in light of my proposed solution (to be found in Chapter 6) any issues presently arising from the interest requirement matter not, since I propose that the interest requirement be done away with.

De Wet and Van Wyk argue further that, because the interest requirement is not defined, but broad and vague, all contractants would consequently have some interest in the *pactum de non cedendo* as it would surely always be of importance to the debtor to know the identity of the creditor.[582] The interest requirement therefore does not go far to limit a contractant's freedom of contract.

Scott seems to agree on this point as she states that the discussion of De Villiers JA of the instances when an interest will exist may lead to an interpretation that an interest will almost always be present.[583] She is also of the opinion that it is in the interest of any debtor that he know the identity of the person to whom he has to pay his debt.[584]

It can thus be accepted that in the vast majority of cases, most debtors would have *some* interest in the *pactum de non cedendo* being valid. The pertinent question is: Under what circumstance does some interest become 'an interest' for the *pactum de non cedendo* to be upheld by our courts?

Sande and Voet spoke of 'an interest', 'some interest', 'any interest' and Sande cautioned that the interest should not be 'too strictly judged'.[585] This supports the view that the interest requirement does not pose much of an obstacle to the debtor when attempting to enforce the *pactum de non cedendo*. The requirement can therefore easily be shown to exist, and the *pactum de non cedendo* will accordingly be upheld as the contractants originally intended it to be – freedom of contract prevailing.

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[582] De Wet and Van Wyk op cit 254 footnote 16.

[583] S Scott 'Italtrafo SpA v Electricity Supply Commission 1978 (2) SA 705 (W)' 1978 *Tydskrif vir Hendendaagse Romeins-Hollandse Reg* 334 (hereinafter referred to as 'Italtrafo SpA'); Scott *Cession* 206.

[584] Ibid.

[585] See Chapter 1.

Since a contractant would be inconvenienced by having to adduce some kind of evidence to show that the prohibition is in his interest should the matter end up in court, it is understandable why some would consider the interest requirement to be limiting freedom of contract. True freedom of contract would only require the contractant to show that the parties were *ad idem*.

In reality, however, the interest requirement is so vague and ill-defined that it would be relatively easy to show that an interest exists. Consequently freedom of contract remains more or less intact. Seen from this point of view the interest requirement seems rather redundant.[586]

4.3 The interest requirement and the alternative arguments

It is clear that *pacta de non cedendo* set two conflicting freedoms up against each other, *viz*, freedom of contract and freedom of trade.[587] Scott states that the problems encountered when determining the validity of *pacta de non cedendo* relate to the approach one adopts towards cession as a legal notion.[588]

She argues that there are two possible approaches: A law of things approach, also known as a law of property approach ('sakeregtelike benadering') or a law of obligations approach ('verbintenisregtelike benadering').[589] In terms of the law of property approach, cession brings about the transfer of an incorporeal asset, where ownership is transferred.

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[586] It is submitted, however, that if one subscribes to a law of property approach the interest requirement does gain some relevance, as according to the general principle laid down by Sande and Voet, *res in commercio* should not be withdrawn from commercial dealings without a good reason. See below for a further discussion as well as Scott *Cession* 209.

[587] It must be noted from the outset that the term 'freedom of trade' in this context means the right to transfer one's property or rights freely; or to conduct business through the free transfer of such property or rights. It does not mean the freedom to choose one's profession or occupation.

[588] Scott 'Pacta' 149.

[589] Ibid.

In terms of the law of obligations approach, cession brings about a replacement of the creditor, where the personal right is transferred.[590]

Scott explains that if one follows a law of property approach, the validity of the *pactum de non cedendo* is determined according to the basic principle of ownership that an owner may freely dispose of his property.[591] Further, it is public policy that things should not be withdrawn from commercial dealings.[592]

If one follows a law of obligations approach, the validity of the *pactum de non cedendo* is determined according to the basic premise that parties to a contract are, in principle, free to determine the content of a personal right through agreement and that contracts usually do not apply to third parties.[593] Scott stresses that either one or the other approach should be adopted consistently, and not a mixture of the two.[594]

4.3.1 Joubert's argument

As a solution to the controversial interest requirement, Joubert offers an interesting alternative. He submits that the issue of the validity of a *pactum de non cedendo* does not involve a choice between the two conflicting freedoms, *viz*, freedom of trade (Scott's law of property approach) and freedom of contract (Scott's law of obligations approach).[595] The issue is rather how these two conflicting freedoms may

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[590] Ibid.

[591] Ibid.

[592] Scott 'Pacta' 150.

[593] Ibid.

[594] Scott 'Pacta' 162.

[595] N Joubert *Die Regsbetrekking by Kredietfaktorering* (1985) LLD Thesis Randse Afrikaanse Universiteit 464 footnote 144 (hereinafter referred to as '*Kredietfaktorering*'); N Joubert 1986 'Boekskuldfinansiering en pacta de non cedendo' *Modern Business* 110 (hereinafter referred to as 'Boekskuldfinansiering').

be reconciled with one another.[596] Joubert's solution can be seen in the following extract:

> 'Daar word aan die hand gedoen dat dit nie nodig is om met besondere reels te werk waarmee die geldigheid van *pacta de non cedendo* beoordeel moet word nie. Al wat nodig is, is om aan die hand van die normale geldigheidsvereistes vir 'n kontrak vas te stel of 'n *pactum de non cedendo* geldig is. Veral die geoorloofheidsvereiste kom in hierdie verband ter sprake. In die Suid-Afrikaanse reg is 'n kontrak onder andere ongeoorloofd indien dit in stryd met die openbare belang is'.[597]

Joubert is of the opinion that it is not against the interest requirement that the *pactum de non cedendo* should be judged and it is therefore unnecessary to select and be consistent with a particular approach. The *pactum de non cedendo* should be judged against the general validity requirements of a contract.[598] One of these requirements is that a contract must not be unlawful, or more specifically, it must not be against public policy.[599]

To illustrate his submission, Joubert relies on *Magna Alloys and Research SA (Pty) Ltd v Ellis*.[600] In this case the court was not faced with a *pactum de non cedendo*, but with a restraint of trade clause. The court held that restraint of trade clauses are *prima facie* valid unless it can be shown that the restraint of trade clause would be contrary to public policy, and a restraint which is unreasonable would be contrary to public policy.[601] Only in such a case would the clause be invalid and unenforceable.[602] For Joubert, a factor which may indicate unreasonableness is when the

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[596] Ibid.

[597] Joubert *Kredietfaktorering* 463.

[598] Joubert *Kredietfaktorering* 463; Joubert 'Boekskuldfinansiering' 111.

[599] Ibid.

[600] 1984 (4) SA 874 (A).

[601] Supra 886I-887; 891A-B.

[602] Ibid.

person in whose favour the restriction applies, has no interest in the restraint of trade clause.[603]

He thus compares the *pactum de non cedendo* to the restraint of trade clause which is governed by public policy. As the comparison goes, if the person in whose favour the *pactum de non cedendo* applies has an interest in it, then according to the decision in *Magna Alloys and Research v Ellis*, the *pactum de non cedendo* will not be invalid as it will not be against public policy, since the presence of an interest renders the restraint reasonable.[604]

Joubert cites *Paiges* in support of the view that our courts judge the validity of *pacta de non cedendo* against the same criterion as that of an agreement in restraint of trade, *viz*, the requirement of lawfulness or public policy. He uses the judgments of Gregorowski J and Wessels J in the court *a quo* as an illustration, since both judges, although reaching different conclusions, assessed the *pactum de non cedendo* in light of public policy.[605]

Joubert points out that Gregorowski J was of the opinion that the *pactum de non cedendo* was not against public policy since the employer had an interest in the restriction, which may also serve to be beneficial to the employee.[606]

He also observes that Wessels J, on the other hand, was of the opinion that the *pactum de non cedendo* was against public policy since the employee was deprived of financing possibilities with the only option being

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[603] Joubert *Kredietfaktorering* 464; Joubert 'Boekskuldfinansiering' 111.

[604] Joubert *Kredietfaktorering* 465; Joubert 'Boekskuldfinansiering' 111. Joubert adds that this should also be the case where the *pactum de non cedendo* appears in the agreement creating the right.

[605] Joubert *Kredietfaktorering* 466; Joubert 'Boekskuldfinansiering' 111.

[606] *Paiges* supra 603. Joubert *Kredietfaktorering* 466; Joubert 'Boekskuldfinansiering' 111.

to obtain credit from his employer, which may not have been given at a fair and equitable rate.[607]

Joubert also notes that the Appeal Court in *Paiges* considered how public policy would affect a *pactum de non cedendo*. The position, as declared by De Villiers JA, is that a *pactum de non cedendo* that has been freely entered into is valid and not against public policy until such time as the legislature states otherwise.[608]

In my opinion, although the courts sometimes discuss public policy with regard to *pacta de non cedendo*, they do this because it is argued by the party seeking to escape the *pactum de non cedendo* that the prohibition is against public policy.

Lubbe and Murray, in a sceptical discussion, question whether a restraint of trade clause is sufficiently akin to a *pactum de non cedendo* to allow for such an analogy.[609] I believe that the two constructions are sufficiently similar to justify a comparison and as Joubert has pointed out, a restraint of trade clause and a *pactum de non cedendo* are both restraints voluntarily agreed to by parties in the commercial arena.

The validity of a *pactum de non cedendo* has primarily been assessed by the presence of an interest to the debtor and, as an aside, the presence of an advantage to the creditor may be persuasive. As mentioned above, the court in *Magna Alloys* held that unreasonableness is a factor indicating that the restraint may be against public policy. What I find problematic is that Joubert seems to associate the *pactum de non cedendo* with this factor, as 'reasonableness' or 'unreasonableness' has never been a factor against which the *pactum de non cedendo* has been judged.

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[607] *Paiges* supra 609. Joubert *Kredietfaktorering* 466; Joubert 'Boekskuldfinansiering' 111.

[608] Supra 616.

[609] Lubbe and Murray op cit 655. See also Scott *Cession* 212.

I tend to agree with the succinctly stated critique that the problem with Joubert's submission is that he attempts to bring the *pactum de non cedendo* under the umbrella of the *Magna Alloys* decision.[610]

Perhaps Joubert should not have made his suggestion of judging a *pactum de non cedendo* against public policy so specific and so heavily dependent on *Magna Alloys,* the restraint of trade clause and reasonableness.

Roussouw's main concern with Joubert's argument is that the shift from the *pactum de non cedendo* to the restraint of trade clause cannot be made spontaneously.[611] One of the reasons for this is that a restraint of trade clause is valid unless the contrary is proven. The *pactum de non cedendo*, on the other hand, is invalid unless the debtor has an interest in the restriction.[612]

Another reason that Roussouw advances is that the two constructions contemplate different interests. A restraint of trade clause is concerned with freedom of contract in direct conflict with the right to freedom of trade. A *pactum de non cedendo* is concerned with freedom of contract in direct conflict with the right to freely dispose of an asset.[613]

Roussouw, however, fails to recognise that the two interests or constructions are more similar than different. He already accepts that the notion of freedom of contract plays a role in both constructions. He, however, overlooks the fact that in the commercial and mercantile arena, disposing of assets for financial gain *is* trading. Thus, not being able to freely dispose of an asset for financial gain is a restraint on freedom of

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[610] Roussouw op cit 61.

[611] Roussouw op cit 60: '[D]aar [kan] na my mening nie sonder meer so 'n sprong vanaf die pactum de non cedendo na die "restraint of trade" gemaak word nie'.

[612] Ibid.

[613] Roussouw op cit 60-61.

trade. By the same token, one of the ways that a person's freedom of trade may be restricted is by restraining a person's ability to dispose of assets for financial gain.

Perhaps if Joubert had suggested that the *pactum de non cedendo* should be judged against public policy in general, and used a restraint of trade clause, as illustrated in *Magna Alloys* as a mere example, his view might have been better received by other academics.

4.3.2 Roussouw's argument

It seems that Roussouw has drawn some inspiration from Joubert's argument and has come up with a suggestion of his own. Roussouw submits that to achieve the result that Joubert endeavours to achieve, one need not rely solely on *Magna Alloys and Research v Ellis*, and that one can do away with the interest requirement completely. [614]

The *pactum de non cedendo* need only be judged against public policy in general with the central question being which freedom should be favoured – freedom of contract or freedom of trade? Roussouw is of the opinion that an approach of this nature is preferable in changing times, since public policy is a flexible concept that can change from time to time and from case to case.[615] He also adds that judging the validity of *pacta de non cedendo* against a single element may bring about more certainty.[616]

There are, however, two points of interest that should be mentioned. These points concern public policy, so the meaning and content of public policy must first be considered before the two points can be discussed:[617]

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[614] Roussouw op cit 61.

[615] Roussouw op cit 63; see also *Magna Alloys and Research v Ellis* supra 891H.

[616] Roussouw op cit 64.

[617] See generally S Van der Merwe and GF Lubbe 'Bona fides and public policy in contract' 1991 *Stellenbosch Law Review* (vol 2) 91.

4.3.2.1 Public policy

In the case of *Printing and Numerical Registration Co. v Sampson*,[618] Jessel MR stated the following:

> If there is one thing which, more than another, public policy requires, it is that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts, when entered into freely and voluntarily, shall be held sacred and shall be enforced by our courts of justice.[619]

This *dictum* has since been cited, in some form or another, in many cases thereafter.[620] More recently in *Sasfin (Pty) Ltd v Beukes*, [621] Smalberger JA held that:

> No court should therefore shrink from the duty of declaring a contract contrary to public policy when the occasion so demands. The power to declare contracts contrary to public policy should, however, be exercised sparingly and only in the clearest of cases, lest uncertainty as to the validity of contracts result from an arbitrary and indiscriminate use of the power. One must be careful not to conclude that a contract is contrary to public policy merely because its terms (or some of them) offend one's individual sense of propriety and fairness… In grappling with this often difficult problem it must be borne in mind that public policy generally favours the utmost freedom of contract. [622]

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[618] 1875 LR 19 Eq 462 465.

[619] Similarly, Innes CJ in *Law Union and Rock Insurance Co Ltd v Carmichael's Executor* 1917 AD 593 598 stated: '[P]ublic policy demands in general full freedom of contract; the right of men freely to bind themselves in respect of all legitimate subject matters'.

[620] *Wells v South African Alumenite Company* 1927 AD 69; *Sasfin (Pty) Ltd v Beukes* 1989 (1) SA (AD) 1; *De Klerk v Old Mutual Insurance Co Ltd* 1990 (1) All SA 371 (E); *Joosub Investments (Pty) Ltd v Maritime and General Insurance Co Ltd* 1990 (3) SA 373 (C).

[621] 1989 (1) SA 1 AD 2A-B.

[622] This quotation has been applied or referred to in many cases, for example, *Botha (now Griessel) and another v Finanscredit (Pty) Ltd* 1989 (2) All SA 401 (A); *De Klerk v Old Mutual Insurance Co Ltd* 1990 (1) All SA 371 (E); *Joosub Investments (Pty) Ltd v Maritime and General Insurance Co Ltd* 1990 (3) SA 373 (C).

Hopkins[623] has recognised that in the law of contract public policy has acquired its own meaning. He comments that the words from *Printing and Numerical Registration Co. v Sampson* 'captured the essence of public policy in contract law' and submits that 'the sanctity of contract rule … [has become] the epitome of public policy in contract law'.[624]

From the case law it is very clear that if the validity of *pacta de non cedendo* were to be judged against public policy, they would more often than not be found to be valid, since public policy (as seen by the courts) seems to put the principle of '*pacta sunt servanda*' on a very high pedestal.

The first point of interest that should be mentioned is that, although the concept of public policy is flexible enough to accommodate changing times and values, most of the above cited cases have stated at some point in the judgment that public policy is 'vague'[625], 'imprecise'[626] and 'elusive'[627] to quote just a few descriptions. Determining the validity of *pacta de non cedendo* against public policy might become obscured in a court's attempt to establish what public policy requires in that particular case.

The second point of interest concerns the caution expressed by Nicholas AJA in *Longman Distillers v Drop Inn Group of Liquor Supermarkets*,[628] where he stated that when a court is faced with the question of public

[623] K Hopkins 'The influence of the Bill of Rights on the enforcement of contracts' 2003 *De Jure* (vol 32) 134.

[624] Ibid.

[625] *Law Union and Rock Insurance Co Ltd v Carmichael's Executor* 1917 AD 593 598.

[626] *Longman Distillers Ltd v Drop Inn Group of Liquor Supermarkets (Pty) Ltd* 1990 (2) SA 906 (A) 913F.

[627] Ibid.

[628] Supra 913H-I.

policy it should keep in mind the well known words in *Richardson v Mellish*,[629] where Burrough J held that:

> I, for one, protest…against arguing too strongly upon public policy; - it is a very unruly horse, and when once you get astride it you never know where it will carry you. It may lead you from the sound law. It is never argued at all but when other points fail.[630]

More recently, a South African judge has similarly remarked:

> Our Courts have recognised that public policy can be 'an unruly horse' unless the judicial reins are tightly held.[631]

There is definitely some truth in this. Public policy is often included as an alternative argument only, in the fear that the main argument does not succeed – the last resort or the fall-back argument. Due to the fact that the concept of public policy is broad and insufficiently defined, it very easily functions as a 'catch all' net.

Further, as Burrough J mentions, if courts too readily embark on a consideration of public policy in a particular issue, the results may not be desirable ('you never know where it will carry you') as public policy is itself not law. Public policy is the community's sense of justice which may not be 'sound law'.

4.3.3 Conclusion

Roussouw's submission is to judge *pacta de non cedendo* against public policy with the central question being whether freedom of contract or freedom of trade should be favoured. The enquiry is futile since our courts clearly favour freedom of contract above freedom of trade, and have always insisted that public policy favours freedom of contract.

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[629] [1824] 130 ER 294 303.

[630] *Longman Distillers* supra 913I-914J.

[631] Per Seligson AJ in *Joosub Investments* supra 385D-E.

Thus, if freedom of contract must prevail because public policy so dictates, then in terms of Roussouw's alternative submission, *pacta de non cedendo* that are freely entered into, would generally be valid and enforceable.

It must, however, be remembered that public policy is an 'unruly horse' and judging the *pactum de non cedendo* against it is risky and can lead to undesirable results.

Albeit interesting, Joubert's argument also cannot be seen as a solution,[632] and neither of the two submissions thus bring the *pactum de non cedendo* any closer to a solution.

Returning to Scott's submission, it seems as though the solution to the validity of *pacta de non cedendo* does *indeed* involve a choice between the two approaches and our courts have made their choice. Our courts have impliedly adopted the freedom of contract approach (Scott's law of obligations approach) and accordingly it seems as though a restraint of trade approach (or law of property approach) will rarely triumph.

4.4 The interest requirement and the interpretation of Sande and Voet

When our courts[633] are faced with *pacta de non cedendo* they rely on Sande De *Prohibita Rerum Alienatione* and Voet *Commentarius ad Pandectas* as authority. Scott has advanced two noteworthy criticisms in this regard.[634] These two criticisms are discussed as follows:

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[632] That is, the reasonableness or unreasonableness factor against which he judges the *pactum de non cedendo* and the fact that the submission is too heavily reliant on the *Magna Alloys* case as well as the concept of restraint of trade, both of which should rather have been used as a general analogy.

[633] *Paiges v Van Ryn Gold Mine Estates* and all the subsequent cases.

[634] See generally Scott 'Italtrafo SpA'; Scott 'Pacta' and Scott *Cession*.

4.4.1 Applying two conflicting legal systems

Scott raises the objection that our courts apply two conflicting legal systems in determining the validity and effect of *pacta de non cedendo*. To determine the validity of *pacta de non cedendo*, the views of Roman-Dutch jurists, Sande and Voet are followed, yet the view of German jurists, Windscheid[635] and Dernburg,[636] are followed to determine the effect.[637]

According to *Paiges* and subsequent cases, which base their reliance on Sande and Voet, a *pactum de non cedendo* will be valid if the debtor has an interest in the prohibition. Sande and Voet require the debtor to have an interest in the prohibition since they follow a law of property approach where a restriction of the free disposal of things in commercial dealings has to be justified.[638]

As to the effect, Sande and Voet state that a cession in contravention of the *pactum de non cedendo* still transfers ownership of the personal right to the cessionary, but the debtor has an action for damages against the cedent.[639]

This effect has been rejected by our courts in favour of the German law approach.
Paragraph 399 of the German Civil Code[640] provides that a *pactum de non cedendo* is valid without the requirement that it has to be in the interest of the debtor.[641] This is so because the German legal system follows a law

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[635] B Windscheid *Lehrbuch des Pandektenrechts* 8ed (1900) 358 footnote 5.

[636] H Dernburg *Pandekten* 3ed vol 2 (1892) 138.

[637] Scott 'Italtrafo SpA' 335; Scott 'Pacta' 159; Scott *Cession* 210.

[638] Scott 'Pacta' 155 footnote 69 and 156.

[639] See Chapter 1.

[640] Known as the Bürgerliches Gesetzbuch (hereinafter referred to as the 'BGB').

[641] Scott 'Italtrafo SpA' 335. Paragraph 399 of the BGB states that: 'A claim is not assignable if the performance cannot be effected in favour of any person other than the original creditor without alteration of its substance, *or if the assignment is excluded by*

of obligations approach, where parties are free to determine the content of their contracts through agreement.[642]

In Germany, therefore, *pacta de non cedendo* are valid *ex mero moto* as a *pactum de non cedendo* can only occur when the right is created by agreement between the creditor and the debtor. The right is thus created as a non-transferable right from the outset. Should the right be transferred contrary to the prohibition, the effect is that the cessionary receives nothing, with ownership still vesting in the cedent.[643]

Scott's main objection to applying two different legal systems in South Africa is that the Roman-Dutch legal system follows a law of property approach and the German legal system follows a law of obligations approach which may be jurisprudentially unsound.[644] She argues that whichever approach is to be preferred, it should be dogmatically pure with the validity and effect both being dealt with either under the law of property or under the law of obligations.[645]

Scott's solution is that a clear distinction should be drawn between a *pactum de non cedendo* that was entered into between the debtor and creditor at the time of creating the right and a *pactum de non cedendo* that was super-imposed onto an already existing agreement.[646] As the suggestion goes, different legal principles should be applied depending on which type of *pactum de non cedendo* one is dealing with. If the

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agreement with the debtor'. [My emphasis] See IS Forrester, SL Goren and H Ilgen *The German Civil Code* (1975) 64 for the English translation.

[642] Scott 'Pacta' 160 and 161.

[643] Scott 'Italtrafo SpA' 335; Scott 'Pacta' 154-155 who relies on K Larenz *Lehrbuch des Schuldrechts* 11ed (1976) and W Fikentscher *Schuldrech*t 6ed (1976).

[644] Scott 'Italtrafo SpA' 335; Scott 'Pacta' 160 and 161; Scott *Cession* 210-211 where she adds that: 'By the time of Windscheid and Dernburg the German law of cession had undergone a distinctive development, which the Roman-Dutch law of cession never reached'.

[645] Scott 'Pacta' 161.

[646] Scott *Cession* 213.

prohibition is super-imposed on existing rights then the views of Sande and Voet should be purely applied to both the validity and the effect.[647]

This means that the prohibition is only valid if it can be shown that the other party has an interest in it, as the law of property requires that property should not be withdrawn from commercial dealings without a good reason. In terms of the effect, it is only binding on the parties themselves and has no bearing on third parties. Thus, a cession in contravention of the *pactum de non cedendo* gives rise to damages in favour of the party who has an interest in the prohibition (the debtor). Ownership of the right, however, passes to the cessionary.[648]

If the *pactum de non cedendo* was entered into at the time that the personal right was created, the German law view should be purely applied to both the validity and the effect.[649] This means that the prohibition is automatically valid as the law of obligations favours freedom of contract. In regard to the effect, the right is non-transferable by its very nature, so a cession in contravention of the *pactum de non cedendo* is void.[650]

It is submitted that legal principles governing *pacta de non cedendo* should be as pure as possible,[651] and applying partially Roman-Dutch law for its validity and partially German law for its effect is undesirable.

In my opinion, one set of rules stemming from one legal system should govern all *pacta de non cedendo* and it should not make a difference

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[647] Ibid.

[648] Scott *Cession* 213-214.

[649] Scott *Cession* 214, see also footnote 288.

[650] Ibid.

[651] Although the legal system in South Africa is generally mixed in nature, and although this is generally not problematic, the *pactum de non cedendo* is one of those instances where mixed legal principles make the situation unnecessarily more complex.

whether the *pactum de non cedendo* was created from the inception of the right or whether it was super-imposed on an already existing right.[652]

4.4.2 Misinterpretation of Sande and Voet

Scott is of the opinion that the court in *Paiges v Van Ryn Gold Mine Estates*, and the subsequent cases also relying on Sande and Voet, have applied the writings of these old authorities incorrectly.[653] She believes that in their writings Sande and Voet were, first, referring to existing property and, secondly, that they were referring to corporeal property.

From the manner in which Sande and Voet use the word 'property', Scott states that Sande and Voet had already existing or pre-existing property in mind.[654] The implication is that the personal right would first have to come into existence through a cession agreement, before a restraint could be imposed upon it.

Thus, if Sande and Voet were indeed referring to already existing property, only once the cession has been concluded and the personal right is brought into existence, can a *pactum de non cedendo* be imposed on that agreement.[655]

The problem with this is that the prohibition would fall into the second form of *pacta de non cedendo*, a category not recognised by Voet.[656] It would

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[652] See Chapter 5.

[653] Scott 'Italtrafo SpA' 335; Scott *Cession* 208.

[654] Scott 'Pacta' 156 and footnote 81 and 158 as well as footnote 95; Scott *Cession* 208-209 and footnote 257. Scott bases this assertion on the fact that the old authorities refer to phrases like the 'owner's property' or an owner disposing of 'his own property'.

[655] Scott 'Pacta' 157.

[656] In this category the cedent, upon cession, adds the prohibition that the cessionary may not cede the right further. See above as well as Chapter 1.

also cause the first form,[657] which both Sande and Voet recognise, and which is the most common form of *pactum de non cedendo*, to fall into desuetude.[658]

It is unnecessary for me to express an opinion as to whether or not Voet and Sande were referring to already existing property, as my view of the discussion of Scott's second criticism disposes of the matter.

As mentioned above, Scott asserts that Sande's and Voet's treatises covered only corporeal property and not incorporeal property.[659] She bases this assertion on the fact that Sande expressly refers to corporeal things in the introductory chapter of *De Prohibita*.[660] Scott further states that although it is not clear, Voet's discussion probably also applies to corporeals only, as he continuously uses the word '*res*' ('thing') and that when he gives examples he uses the word '*traditio*' ('delivery' of a corporeal movable).[661]

A contradiction, however, appears in Scott's opinion, as in a later work she states that 'Voet probably included incorporeal things under the term "*res*"'.[662] Perhaps she changed her mind, or was influenced by the fact that it was widely accepted that at the time of Voet's treatise an

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[657] It will be remembered that the first form is where the *pactum de non cedendo* comes into existence in the agreement which creates the personal right that is concluded by the debtor and the creditor. See above as well as Chapter 1.

[658] This is so because the personal right is not already in existence when the *pactum de non cedendo* is imposed.

[659] Scott 'Pacta' 156-157, 158; Scott *Cession* 209. Scott noticed something that many judges and academics were either oblivious to, or just accepted without question. The result is that our courts have probably been applying the law on the restraint of transfer of corporeals to instances where the transfer of an incorporeal is has been restrained.

[660] Scott 'Pacta' 156. See also footnote 79 where she quotes the said passage in the introduction to *De Prohibita*: '*Dominium vulgo definiri solet, esse jus de re* corporali *statuendi, ut si quis velit, nisi jure prohibeatur*'. [My emphasis]

[661] Scott 'Pacta' 158 and footnote 96.

[662] Scott *Cession* 209.

incorporeal right was considered to be a thing just as much as a corporeal right was.[663]

Be that as it may, Scott nevertheless holds the view that in their treatises Sande and Voet were referring to *pacta de non aliendo*, rather than *pacta de non cedendo*.[664]

Despite the apparent contradiction, the criticism that our courts have misinterpreted Sande and Voet can be fully supported.

Dealing first with Voet, he indeed refers to '*traditio*' (of land) in one of his examples. This does lead one to believe that he was referring to corporeals; if he were referring to incorporeals he would have used the word 'cession' as ownership of incorporeals is delivered or transferred in this manner.

Furthermore, the heading of *Commentarius* 2 14 20, that introduces Voet's discussion which follows, is translated as:

> Agreements depriving owners of management of own property without effect, unless other party has interest.[665] (Gane's translation)

His discussion that follows begins with the following sentence:

> Agreements also by which an owner deprives himself of discretion and control as to his own property….[666] (Gane's translation)

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[663] Admittedly, this is a valid point in favour of the argument that Voet's writings (at least) do cover incorporeals, but as can be seen from the discussion which follows, the more likely situation is that Voet's writings do not include incorporeals.

[664] Scott *Cession* 209. That is, an agreement not to alienate (a corporeal) as opposed to an agreement not to cede (an incorporeal).

[665] P Gane *The Selective Voet being the Commentary on the Pandects by Johannes Voet and the Supplement to that work by Johannes van der Linden* (1955) 434.

[666] Ibid.

According to the general principles of cession, when a right is ceded, for example, a right to claim monetary performance, complete ownership of the right is transferred to the cessionary.[667] The cessionary alone owns the right to claim the debt from the debtor. Even if a partial debt is ceded, that part of the debt which is ceded is owned by the cessionary alone.[668]

The above-quoted passages from *Commentarius* imply that the owners of property are not deprived of their right of *ownership* in that property, but deprived merely of their right to, in some way, manage, control or exercise discretion over their property. No mention is made of a transfer of the right of ownership of the property. Cession transfers ownership, thus Voet could not have been referring to cession, but rather alienation of one or some of the rights of ownership in corporeal property.

Voet goes on to state that if such an agreement to limit an owner's right of ownership is entered into, one of the parties must have an interest in this agreement if an action is to arise from a breach thereof. The examples he uses to illustrate this point are examples where an owner's right is limited and not where an owner is divested of ownership.

The examples used are that, without an interest, no person can enter into an agreement whereby an owner shall not have the power to consecrate his own place, or that he shall not have the power to bury a corpse in his own ground, or that he shall not have the power to part with his land without the consent of his neighbour.

It is also interesting to note that Voet in *Commentarius* 2 14 20 refers to Sande's *De Prohibita* part 4,[669] the part that supposedly covers *pacta de*

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[667] Barring, of course, a cession *in securitatem debiti* where the pledge construction is preferred. See Chapter 5.

[668] Nienaber op cit para 45-46.

[669] It is likely that because Voet refers to Sande's *De Prohibita*, a treatise that our courts mistakenly thought covers restraints on cession, our courts assumed that Voet was also referring to restraints on cession.

non cedendo. Therefore, if it can be shown that Sande was writing of *pacta de non aliendo*, it will strengthen the argument that Voet, too, was writing on *pacta de non aliendo*, since he associates his work with that of Sande.

Sande was well known as an authority on the law of cession and his treatise, *De Cessione Actionum*, covers the general principles of cession. Since a treatise covering the general principles would normally be published first and another treatise dealing with prohibitions published thereafter, it can, therefore, be understood how our courts could mistakenly assume that *De Prohibita* deals with the restraints upon cession.[670]

If one considers Sande's writings in *De Prohibita*, it indeed appears that he expressly refers to corporeal property.[671] This argument becomes even more convincing upon a reading of all the examples as a whole:

Sande's examples (as Voet's) deal also with partial restrictions on ownership upon alienation, like a right of pre-emption or some type of servitude. To illustrate this, one of the examples Sande uses is where a person alienates (through donation) his slave to another person on the condition that the slave shall not come into the possession of certain people, for instance the brother of the donee. Such an agreement on the restraint of alienation is valid.[672]

Of the examples that deal with a complete restriction on alienation, it is clear from the wording that what is being restricted is the sale of the

[670] It is a possibility that the dates of publication do not necessarily reflect the dates when the treatises were written, that is, Sande may have written *De Prohibita* first, but published it after *De Cessione*. In my opinion, there is nothing to suggest that this was the case.

[671] *De Prohibita* Introduction: '*Dominium vulgo definiri solet, esse jus de re* corporali *statuendi, ut si quis velit, nisi jure prohibeatur*'. [My emphasis]

[672] *De Prohibita* 4 1 7. PC Anders *Commentary on Cession of Actions by Johannes à Sande* (1906) 296.

corporeal object itself (usually land) and not cession of the rights in respect of the thing. To illustrate this, one of the examples Sande uses is where a mortgagor places a restraint on the owner of the mortgaged land that the owner shall not alienate his land.[673] Thus, the restriction covers alienation of the land, not the cession of the rights to the land.

Another observation worthy of note is that both Sande and Voet never mention the words 'cession' or 'cedent' or 'cessionary'. They use only words like 'alienate', 'purchaser', 'seller' or 'lessor'. In fact, Sande actually used the term '*pactum de non alienando*'.[674]

Further, in Sande's earlier work,[675] *De Cessione Actionum*, he wrote quite extensively on the cession of actions. Therein he included a chapter (Chapter 5) on the kinds of actions which are capable of cession and those which are not. If Sande was truly an authority on *pacta de non cedendo*, this chapter would have been his opportunity to deal with this issue, yet he said nothing.

The obvious question is why would Sande write an entire treatise dealing with just *pacta de non cedendo* (supposedly *De Prohibita*) when he already had an opportunity to address the issue in *De Cessione*?

Further, even if in the 10 years between *De Cessione* and *De Prohibita*, Sande was of the opinion that the *pactum de non cedendo* was so extensive that it warranted its own treatise, he surely would have by way of introduction explained how *De Prohibita* was an extension of *De Cessione*. And, if this unlikely scenario was the case, surely Sande would still have, for the sake of completeness, briefly mentioned *pacta de non cedendo* in *De Cessione*?

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[673] *De Prohibita* 4 1 3. Anders op cit 294-295.

[674] *De Prohibita* 4 2 2.

[675] About 10 years earlier.

Lastly, why would Sande have altered his terminology in *De Prohibita*? If his first treatise is about cession in general and it is titled '*De Cessione Actionum'*, and if his second treatise is (supposedly) about the restrictions on cession, why did he not title his second treatise something like '*De Prohibita Rerum Cessione'* – restraints upon *cession*, as opposed to '*De Prohibita Rerum Alienatione'* – restraints upon *alienation*?

4.4.3 Conclusion

These unexplained vexing questions lead one to believe that Voet in *Commentarius* and Sande in *De Prohibita* were in fact, as Scott points out, referring to corporeal things and not incorporeal things.

One is thus inclined to wonder what exactly the thought process was in the minds of the judges in *Paiges v Van Ryn Gold Mine Estate*. Were they aware of the probability that these old authorities were writing about corporeal things?

Their application of similar, yet incorrect legal principles was most likely an oversight. On the other hand, it is bothersome that *all* the judges in *Paiges* made an oversight error, as well as *all* the other judges who have ever had the occasion to consider the issue,[676] as well as *all* the academics (barring Scott of course) who have written on the *pactum de non cedendo*.

As a consequence, much of the historical development as considered in Chapter 1 cannot be said to be the historical development of the *pactum de non cedendo*. The historical development can rather be said to be that of the *pactum de non aliendo*.

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[676] It is submitted that Blackwell J in *Du Plessis v Scott* 1950 (2) SA 462 (W) may have doubted whether the legal rules, as laid down by Sande and Voet, were applicable. This doubt was never express and the judge unfortunately did not pursue the matter. He probably believed that the Appellate Division in *Paiges* had conducted proper research and that the more likely situation was that it was he who was mistaken. See Chapter 3 where this view was first suggested.

As to the (true) historical development of the *pactum de non cedendo*, there is, to my knowledge, no historical record tracing this development. One can therefore only speculate. In my view, since cession was not recognised in Roman law, an agreement preventing cession (when it was finally seen as acceptable) was probably considered valid and a cession in contravention was probably ineffective, since it harked back to the traditional position.[677]

The lack of a historical development aside, the fact is simply that this prohibition exists and the pertinent issue is how our law is going to deal with it in the context of modern South African realities.

In chapter 6 some viable solutions are proposed.

4.5 Recent developments

Scott has recently published an article where she revisits her earlier ideas surrounding the *pactum de non cedendo* in light of developments in international financing law.[678]

Featuring strongly in her discussion is the significance of the commercial value of claims as assets. Realising that it is important for creditors (both private individuals and multinational companies) to freely dispose of their assets, she suggests that the traditional view of *pacta de non cedendo* should be relaxed to aid financial expediency, but at the same time without neglecting the interests of the debtor.[679]

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[677] Ineffective in the sense that ownership of the personal right did not pass to the cessionary.

[678] S Scott 'Once again: agreements prohibiting cession' 2008 *Stellenbosch Law Review* (vol 3) 483 (hereinafter referred to as 'Once again').

[679] Ibid.

Scott considers two international conventions seeking to unify assignment rules, since cross-border assignments can be confusing and very risky with different jurisdictions applying their own rules.[680]

The first is the UNIDROIT Factoring Convention of 1988 which covers the assignment of receivables in a factoring contract.[681] This Convention has a limited scope of application as it does not apply to all cross-border factoring assignments, but only to those where the receivables arise from the sale of goods and where the assignor's and assignee's places of business are in different states (or countries).[682]

Scott notes that article 6(1) of this Convention addresses *pacta de non cedendo* by declaring that any assignment in contravention of such a restriction is valid and effective despite the *pactum de non cedendo*. Article 6(3) bases this position on the principle that a *pactum de non cedendo* entered into by the creditor (assignor) and debtor operates *inter partes* and a breach thereof may lead only to a claim for damages for breach of contract.[683]

What further limits its scope of application is that only six countries have ratified it: France, Italy, Germany, Hungry, Latvia and Nigeria.

The second international convention is the UNCITRAL Convention on the Assignment of Receivables in International Trade of 2001, which covers assignments of international receivables where the assignor and debtor or the assignor and assignee are located in different states.

This Convention closely follows that of the UNIDROIT Factoring Convention in its governing of *pacta de non cedendo*. Article 9 provides

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[680] B Lurger 'Assignment' in *Elgar Encyclopedia of Comparative Law* (2006) 92.

[681] See Chapters 5 and 6 for a further discussion.

[682] Scott 'Once again' 488; Lurger op cit 92.

[683] Scott 'Once again'488-489; Lurger op cit 101.

that an assignment contrary to such a prohibition is valid and effective as the *pactum de non cedendo* operates *inter partes* only.[684]

The UNCITRAL Convention also has a limited scope of application since article 9 only applies to certain receivables,[685] and because a mere three countries have signed the convention (USA, Luxembourg and Madagascar) with only Liberia that has ratified it.[686]

Another international instrument mentioned by Scott is the UNIDROIT PICC (Principles of International Commercial Contracts) of 2004 and in Europe the PECL (Principles of European Contract Law) of 2003.

The purpose of the former instrument is to establish general rules for dealing with international commercial contracts and includes a section dealing with assignments and *pacta de non cedendo*.

The validity and effect of an assignment made contrary to a *pactum de non cedendo* is the same as the UNIDROIT Factoring Convention and the UNCITRAL Convention.[687] UNIDROIT PICC, however, is not a formal source of law and applies only if the parties have agreed that their contract shall be governed by it.[688]

The purpose of the latter instrument is to provide a comprehensive set of rules for contracts concluded in Europe. It covers the rules governing

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[684] Scott 'Once again' 489; Lurger op cit 101.

[685] That is, to the assignment of receivables: (a) Arising from an original contract that is a contract for the supply or lease of goods or services other than financial services, a construction contract or a contract for the sale or lease of real property; (b) Arising from an original contract for the sale, lease or licence of industrial or other intellectual property or of proprietary information; (c) Representing the payment obligation for a credit card transaction; or (d) Owed to the assignor upon net settlement of payments due pursuant to a netting agreement involving more than two parties. See article 9(3).

[686] Scott 'Once again' 489; Lurger op cit 101.

[687] Scott 'Once again' 489-499; Lurger 93-94.

[688] Scott 'Once again' 489-499; Lurger 93-94; F Mazza 'Assignment of rights' in *Commentary on the UNIDROIT Principles of International Commercial Contracts (PICC)* (2009) 995 *et seq*.

claims of any contractual performance and partially other transferable claims which are not sounding in money.

It addresses *pacta de non cedendo* in the same way as the other abovementioned instruments. Like the UNIDROIT PICC, it is not a formal source of law and applies only if the parties have agreed that their contract shall be governed by it.[689]

Despite not being formal sources of law, both the UNIDROIT PICC and the PECL serve as model rules for future attempts to unify the law of assignment at European and international levels.[690]

Scott's opinion of the abovementioned instruments is evident from the following passage:

> In all these instruments there is clearly a balancing of interests. Both the
> demands of commercial expediency and the interests of the debtor are considered. The principle of freedom of contract is upheld, but the effect of this freedom on third parties is curtailed to serve the needs of both the creditor and her debtors. All the above instruments favour the validity of agreements prohibiting cession, but restrict their effect to the contracting parties. Some of these instruments show a measure of sensitivity to the particular needs of the debtor.[691]

Bearing in mind the content of all the instruments, Scott's assertion for a solution in South Africa is that the entire law of cession is in 'dire need of reform and should therefore be codified'.[692]

[689] Scott 'Once again' 490; Lurger 93-94; GF Lubbe 'Assignment' in *European Contract Law: Scots and South African Perspectives* vol 2 (2006) 307 *et seq*.

[690] Scott 'Once again' 489 footnote 26 and 490; Lurger 94; Lubbe op cit 307 *et seq*; Mazza op cit 995 *et seq*.

[691] Scott 'Once again' 491. See also 492-493.

[692] Scott 'Once again' 494.

The proposed codification should approach the matter by declaring all *pacta de non cedendo* valid as this would be in line with the principle of freedom of contract. The effect of a cession made contrary to a *pactum de non cedendo* should give rise to a claim of damages for breach of contract, therefore operating *inter partes* only.[693]

Further, she adds that:

> Where the debtor has an interest in re-instating the personal nature of the obligation, she could do so in the agreement creating the claim. In this way both the interests of the creditor in the free disposal of her assets and the interests of the debtor would be protected.[694]

Scott's suggestion thus allows the parties to override the proposed legislation in an attempt to make the *pactum de non cedendo* non-transferable. This would have the result of rendering a cession in contravention of the *pactum de non cedendo* ineffective. Ownership would still vest in the creditor and the *pactum de non cedendo* would accordingly apply to third parties. The purported cessionary would presumably have a claim for damages against the creditor for breach of contract.

The logic and simplicity of this suggestion must be noted. I am, however, of the opinion that a more drastic change is needed to modernise our law and to bring South Africa in line with international commercial trends.[695]

Scott concludes that without legislation the codification of the law of cession and consequently the law governing *pacta de non cedendo* is not possible.[696] She is of the opinion that with all the mentioned international

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[693] Ibid.

[694] Ibid.

[695] My suggestions are to be found in Chapter 6.

[696] It is, however, submitted that the entire law of cession need not be codified in order to effect a re-evalution of the *pactum de non cedendo*. Further, codification of the law of cession would necessitate codification of related areas, like the law of contract and the

instruments dealing with the topic, South African legislators would have much to guide them.[697]

Judging from the attitude of the South African Law Commission in 1998, Scott is sceptical as to whether South African legislators will step up and codify the law of cession and *pacta de non cedendo*.[698]

The Law Commission deems it wise that our courts take on the task of reforming this area of the law. Scott is convinced that a successful reformation cannot occur within the walls of a courtroom. I tend to agree with her on this point, but only to a limited extent.[699]

law of delict. Moreover, my proposed solution suggests the enactment of legislation only where the *pactum de non cedendo* appears in a contract of a commercial nature, that is, where factoring is involved. I make this suggestion because a transformation of this magnitude cannot be made judicially. If Scott's proposed solution to the plight of the *pactum de non cedendo* is considered, the necessary adjustments can easily be made in a judicial decision.

[697] Ibid.

[698] Scott 'Once again' 485 and footnote 9.

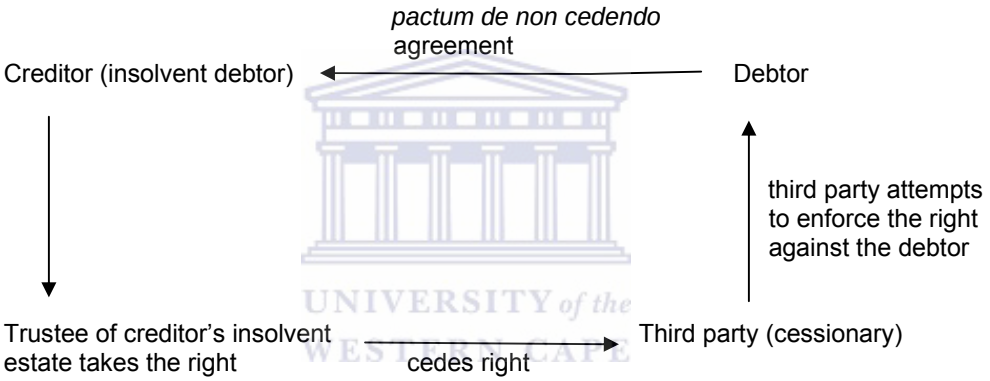
[699] That is, only in so far as the reform with regard to factoring (book debt financing) is concerned. See Chapters 5 and 6.

CHAPTER FIVE

AREAS OF APPLICATION

Chapter 4 reviewed the validity and effect of the *pactum de non cedendo* in general. This Chapter considers how the *pactum de non cedendo* manifests itself in specific contracts or in specific areas of the law and considers, in addition, American law. The reason for examining American law is for the purpose of comparison. Perhaps a viable solution can be uncovered.

5.1 Insolvency



5.1.1 South African law

In *Paiges v Van Ryn Gold Mine Estates,*[700] the Appeal Court held that:

> …the prohibition only contemplates a voluntary cession and does not prevent the right to the wages vesting in the Trustee in insolvency.[701]

This court thus laid down the principle that upon the insolvency of the creditor the trustee is not bound by the *pactum de non cedendo*. Since

[700] 1920 AD 600.

[701] Supra 616.

this right is an asset in the estate of the insolvent creditor, the trustee may consequently cede the right in administration of the indebted estate.[702]

In the case of *Estate Fitzpatrick v Estate Frankel and others; Denoon and another v Estate Frankel and others,*[703] the Appellate Division held that a clause in a lease which prohibited the lessee from, *inter alia*, ceding the lease without the consent of the lessor applied only to voluntary cessions and not cessions which had resulted from a 'forced sale'.[704]

The court further stated that a cession in execution was not in breach of the clause prohibiting cession because, according to the court's interpretation of the lease in this case, there was no clear intention that the clause should apply to a cession that was involuntary.[705]

The *Estate Fitzpatrick* case seems to have developed the principle laid down in *Paiges*, as the court opened the door to the possibility of binding the trustee to the *pactum de non cedendo* on insolvency. This possibility may be brought about if the contract specifically states that the *pactum de non cedendo* shall apply to involuntary cessions in the same way as it applies to voluntary cessions.

This case, however, dealt with a lease and the tendency of our courts was in any event that, depending on the wording of the lease, the trustee may or may not be bound.[706]

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[702] This principle was followed in other cases, *viz*, *Heimann v Klempman & Jaspan* 1922 WLD 115; *Stalson v Brook* 1922 WLD 143; *Moseley Buildings v Bioscope Cafés Ltd* 1923 WLD 189; *Himmelhoch v Liquidators, Fresh Milk & Butter Supply Co Ltd and others* 1925 TPD 958; *Govender v Tongaat Town Clerk and Others* 1986 (4) SA 187 (D). See also SM Luiz 'Review of recent cases' 1987 *De Rebus* (vol 3) 34.

[703] 1943 AD 207. See Chapter 3 for a summary of the case.

[704] Supra 218-219.

[705] Supra 219.

[706] See *Moseley Buildings v Bioscope Cafés Ltd* 1923 WLD 194; also *Lithins v Laeveldse Koöperasie Bpk and Another* 1989 (3) SA 891 (T) 894F-H where Olivier J states that the cases introducing the rule that a *pactum de non cedendo* in a lease does not bind the trustee were based on English decisions dealing only with leases. The English *ratio* seems to have, in the course of time, become a substantive rule in South African law.

In 1943 the Legislature inserted s37(5)[707] into the Insolvency Act[708] to create a statutory exception to the general principle that the trustee is not bound by a *pactum de non cedendo*. The section provides that a stipulation in a lease which restricts or prohibits the transfer of any right under the lease will bind the trustee of the insolvent estate as if he were the lessee. Section s37(5) is thus very limited in its application as it only applies to leases.[709]

Olivier J in *Lithins v Laeveldse Koöperasie*[710] held that the position of the *pactum de non cedendo* in insolvency is as follows:

> I think it can safely be deduced from these cases that there is a general principle in our law to the effect that the *pactum de non cedendo* does not bind the trustee or liquidator in insolvency, unless it appears in a lease, in which case s37(5) of the Insolvency Act applies, or unless it appears from the *pactum* that it would also be applicable in the case of insolvency. In the latter case, the question will then arise whether such a wide clause is valid.[711]

[707] Section 37(5) reads as follows: 'A stipulation in a lease that the lease shall terminate or be varied upon the sequestration of the estate of either party shall be null and void, but a stipulation in a lease which restricts or prohibits the transfer of any right under the lease or which provides for the termination or cancellation of the lease by reason of the death of the lessee or of his successor in title, shall bind the trustee of the insolvent estate of the lessee or of his successor in title, as if he were the lessee or the said successor, or the executor in the estate of the lessee or his said successor, as the case may be'.

[708] Act 24 of 1936.

[709] See *Durban City Council v Liquidators, Durban Icedromes Ltd and Another* 1965 (1) SA 600 (A) 613B-C; *Slims (Pty) Ltd and Another v Morris NO* 1988 (1) SA 715 (A) 734B-D and 742B-H; *Lithins v Laeveldse Koöperasie Bpk and Another* 1989 (3) SA 891 (T) 894B-C.

[710] *Lithins* Supra 895H. See Chapter 3 for a case summary.

[711] See RH Zulman 'Insolvency law' 1989 *Annual Survey* (vol 7) 251; S Scott *The Law of Cession* (2ed) 1991 206-207; AJ Kerr *The Principles of the Law of Contract* (6ed) 2002 500; PM Nienaber 'Cession' *LAWSA* (2ed) vol 2 2003 para 37; RH Christie *The Law of Contract in South Africa* (5ed) 2006 464; S Scott 'Sessieverbiedende ooreenkomste en die posisie van die curator of likwidateur by insolvensie' 2008 *Tydskrif vir die Suid-Afrikaanse Reg* (vol 4) 776 776-778 (hereinafter referred to as 'Sessieverbiedende').

Olivier J was therefore doubtful as to whether an express term would bind the trustee in cases other than that of a lease, but left the question open.[712]

Recently this issue came before the court in *Any Name 451 (Pty) Ltd v Capespan (Pty) Ltd*,[713] where Zondi AJ relied on the *ratio* in both *Paiges* and *Lithins*.[714] The outcome of the case was that on the interpretation of the wording of the *pactum de non cedendo*, it was not binding on any person other than the companies (the parties to the agreement) and it could thus not be construed as binding the liquidators on insolvency.[715]

Capespan appealed against this decision.[716] Thring J, who delivered the judgment, held that Zondi AJ had erred in reaching his conclusion in the court *a quo*.[717] According to the judge, Zondi AJ was correct in stating that a *pactum de non cedendo* will not always prevent an involuntary cession where a trustee or liquidator cedes the right in question to a third party.[718]

There would, however, be certain instances where the *pactum de non cedendo* would bind the trustee or liquidator on insolvency. Thring J notes that Zondi AJ mentioned two instances, *viz*: Where the *pactum de non cedendo* appears in a lease (being saved by s37(5) of the Insolvency Act) or where it appears from the *pactum de non cedendo* itself that the trustee

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[712] *Goodwin Stable Trust v Duohex (Pty) Ltd and Another* 1996 (2) All SA 558 (C) 563I-J. If it is uncertain as to whether an express term would bind the trustee, an implied or tacit term would definitely not bind the trustee. Although, on the other hand, the court in *Estate Fitzpatrick* did not seem to have a problem with this kind of term. Is it really such a wide term?

[713] 2007 JOL 19402 (C). See Chapter 3 for a case summary.

[714] Supra 26.

[715] Ibid.

[716] *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd* 2008 (4) SA 510 (C). See Chapter 3 for a case summary.

[717] Supra 512J.

[718] Supra 512J-513A.

should be bound.[719] Thring J is, however, of the opinion that a third instance exists.

In Chapter 4 the possibility was discussed that the *pactum de non cedendo* can manifest itself in two constructions.[720] Against the distinction between and acceptance of these two possible constructions, Thring J states that a third mechanism for binding the trustee to a *pactum de non cedendo* exists. According to the judge, when a personal right is created as a non-transferable right *ab initio*, thus falling within the first construction, the trustee is bound by the *pactum de non cedendo*.[721]

In such a case the trustee and liquidator on insolvency will be bound by the *pactum de non cedendo* as the personal right is 'inherently incapable' of being transferred.[722] Thus, a cession by the trustee in contravention of the *pactum de non cedendo* would be of no force or effect, even though the term 'involuntary cession' may be used.[723]

According to the judge, the principles of freedom of contract and that the trustee can acquire no greater right against the debtor than the insolvent creditor himself had, are persuasive arguments to overrule *Lithins* and other cases.[724]

Thring J also rejected *Paiges* as an authority that the *pactum de non cedendo* is unable to prevent an involuntary cession.[725] He explained that De Villiers JA in *Paiges* was merely referring to the fact that a *pactum de non cedendo* is powerless to prevent a '*vesting*' of a right in the trustee

[719] Supra 513A-C.

[720] See Chapter 4 140-143.

[721] Supra 518C-E.

[722] Supra 514G-515C; 515C-D; 519A.

[723] Supra 519B.

[724] Supra 518D-E. As well as the authority he quotes therein, which Thring J believes lends itself to such an interpretation.

[725] *Paiges* Supra 616: 'But the prohibition only contemplates a voluntary cession and does not prevent the right to the wages vesting in the Trustee in insolvency'.

upon insolvency. According to the judge, De Villiers JA was not stating that a *pactum de non cedendo* was powerless to prevent an *involuntary cession*.[726]

It is clear from the judgment that De Villiers JA used the word 'voluntary' cession, and never the word 'involuntary' cession, nor did he offer any explanation as to what the position would be once the right has vested in the trustee.

In my view, the answer lies in the principles of the law of insolvency: The *pactum de non cedendo* is powerless to prevent such a vesting as it is a natural and necessary consequence of insolvency,[727] but a *pactum de non cedendo* can (as it was so designed) prevent a cession, even in the hands of a trustee.

It is the function of the trustee to administer the insolvent estate in a manner that would best benefit the creditors of the insolvent estate.[728] The trustee, however, must take the insolvent estate as he finds it and better or greater rights for the creditors cannot be 'created' by allowing the trustee to be unbound by a *pactum de non cedendo*. Also, allowing the trustee (a third party) to interfere in a contract to which he was not a party, nor could ever be a party, is contractually unsound.

The question, however, arises that if the trustee is to be bound by the *pactum de non cedendo* and is consequently unable to cede the personal right, what is he to do with it? According to the prevailing legal principles, the trustee's only option would be to enforce the right against the debtor. If the debt is not yet due and enforceable, or if the debtor is unable to pay some or all of the debts for any reason, the insolvent estate may have to bear the loss.

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[726] See Chapter 3.

[727] Insolvency Act s20; R Sharrock et al *Hockly's Insolvency Law* 7ed (2002) 57.

[728] Sharrock et al op cit 110.

It stands to reason that if the earliest case relied upon as authority for allowing the trustee to ignore a *pactum de non cedendo* is incorrect, all the cases thereafter that rely on *Paiges* cannot be considered as authority on the issue either.

Scott has recently reviewed the *Capespan* case and the position of *pacta de non cedendo* in insolvency in general.[729] She questions why s37(5) of the Insolvency Act makes a statutory exception in the case of leases, whereas other personal rights are treated differently.[730] She makes a good point, one for which no plausible explanation can be found.

Scott also observes that after *Capespan*, the position is now somewhat uncertain.[731] She writes that, on the one hand, there is a judgment of a single judge in the Transvaal division (*Lithins*), which is based on a passage from the highest court of appeal in *Paiges*, although this was an *obiter dictum* and possibly misinterpreted. The judgement in *Lithins* has also been followed by single judge in the Cape division.[732]

On the other hand, there is a judgment of a full bench in the Cape division, *Capespan*, which deals with the issue differently and effectively overturns the earlier cases.[733] It is a concern that the possibility exists that the issue may be split on a geographical jurisdictional basis.

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[729] Scott 'Sessieverbiedende' in addition to offering criticism of both the *Lithins* and *Capespan* judgments.

[730] Scott 'Sessieverbiedende' 779 without any giving examples of other personal rights which are treated differently.

[731] Ibid.

[732] In *Goodwin Stable Trust v Duohex (Pty) Ltd and Another* 1996 (2) All SA 558 (C).

[733] Scott 'Sessieverbiedende' 779.

The current position is clearly unsatisfactory. The solution lies in the Appeal Court pronouncing on the issue expressly. Alternatively, this state of affairs can be disposed of if my proposed solution is adopted.[734]

5.1.2 American law

In America the law of bankruptcy is governed by the Bankruptcy Reform Act of 1978 and the 1994 Act, which served to update certain portions of the 1978 Act. This legislation can be found in Title 11 of the United States Code and is commonly referred to as the 'Bankruptcy Code'.[735]

Anti-assignment clauses appearing in the area of the law of bankruptcy are dealt with simply and logically.

In terms of the Bankruptcy Code s541(c)(1)(A), any property interest of the insolvent debtor (the creditor in the anti-assignment agreement) becomes the property interest of the trustee of the bankrupt estate, despite any kind of restriction that would hamper such interest being vested in the trustee.[736]

To this rule there is only one instance where a property interest would not automatically be transferred to the trustee, and that is in the case of a beneficial interest in a trust.[737]

Once the property interests are vested in the trustee, the general principle is the following:

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[734] See Chapter 6 were my suggestions are discussed in detail.

[735] TJ Salerno, JM Udall and B Sirower *Bankruptcy Litigation and Practice: A Practitioner's Guide* 2ed vol 1 (1995) 6.

[736] DE Ytreberg in *American Jurisprudence* 2ed vol 9A (1999) 412. Section 541(c)(1)(A) reads as follows: '…an interest of the debtor in property becomes property of the estate…notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law that restricts or conditions transfer of such interests by the debtor…'. See also TH Jackson *The Logic and Limits of Bankruptcy Law* (1986) 104.

[737] Ytreberg op cit 412.

> [T]o the extent that an interest in property is limited in the hands of the debtor, it is equally limited in the hands of the bankruptcy estate.[738]

Thus, the debtor's assets become the property of the trustee of the insolvent estate, but are still fully subject to their 'nonbankruptcy attributes'.[739] Thus, if an insolvent debtor was prohibited from assigning a personal right due to an anti-assignment clause, then upon the vesting of the right in the trustee, he too, will be prohibited from assigning the personal right.

The rationale for this is that the trustee does not obtain a greater right against third parties than the debtor himself had as at the day of commencement of the bankruptcy case.[740] Accordingly, the trustee of the bankrupt estate is subject to the same claims and defences that a third party may have asserted against the insolvent debtor, as if the bankruptcy estate had never been created.[741]

This means that if the trustee assigns the personal right in contravention of an anti-assignment clause, he will be subject to a claim for damages for breach of contract by the third party (the debtor in the anti-assignment agreement).

The trustee, it seems, only has two options when faced with an anti-assignment clause, with his choice dependant on which option would best serve the bankrupt estate: Either he can enforce the personal right against the debtor of the anti-assignment agreement and transfer the proceeds to the bankrupt estate to be distributed among the creditors; or he can assign the personal right contrary to the anti-assignment clause, while expecting a claim for damages to be lodged against the bankrupt estate, but while knowing that such a claim would be ranked together with

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[738] Ibid.

[739] Jackson op cit 104.

[740] Ytreberg op cit 412.

[741] Ibid.

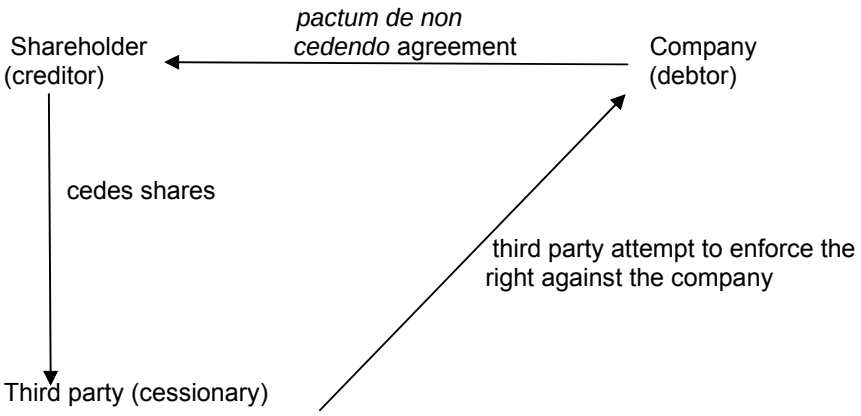
the other claims of the concurrent creditors and would not affect the general indebtedness of the estate. [742]

The American law approach seems to make more legal sense in that it does not allow the creditors of the insolvent estate to benefit from something that the insolvent debtor would not have been able to benefit from had he not become insolvent. Further, it upholds the principle of *pacta sunt servanda* by honouring the agreement entered into by the debtor and creditor (of the *pactum de non cedendo* agreement).[743]

[742] For the sake of completeness it must be added that, in terms of s365(f)(1) of the Bankruptcy Code, the trustee has the choice to take up an 'executory' contract or to assign it, regardless of any prohibition or restriction against assignment. What is under discussion here, is assumption or assignment of the performance of a duty or obligation by the insolvent debtor (that is – the executory contract) and not assumption or assignment of the insolvent debtor's right to claim performance.

[743] Had the Appellate Division in *Paiges* decided not to render the personal right of a valid *pactum de non cedendo* non-transferable, the position would be the same in South African law, as the Trustee could elect to honour the agreement or not on the pains of damages.

5.2 Company law



5.2.1 South African law

A share in a company with a share capital is an incorporeal asset in the estate of the shareholder, not only because of its monetary value when a company declares dividends, but, *inter alia*, also because of the voting rights that accompany it.[744]

Shares are generally issued to a shareholder in terms of a company's articles of association,[745] and the articles of association is, ultimately, governed by the Companies Act.[746]

A private company may, in terms of s59(2) of the Companies Act, adopt the model articles in Schedule 1, Table B of the Act or it may draft an original set of articles.[747] Regardless of which set of articles the company

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[744] HS Cilliers and ML Benade et al *Corporate Law* 3ed (2000) 224-225. See also s91 of the Companies Act 61 of 1973.

[745] The articles of association is a document determining the manner in which the company will function (hereinafter referred to as the 'articles'). Shares may also be issued in terms of a shareholder's agreement. See Cilliers and Benade op cit 74.

[746] Act 61 of 1973; Cilliers and Benade op cit 225.

[747] Cilliers and Benade op cit 74.

uses, its articles will still be subject to the restrictions in s20 of the Companies Act.[748]

In order for a company to qualify as a private company it must comply with s20 of the Companies Act. Besides requiring a private company to have a share capital, s20 compels the company to include in its articles three restrictions.[749] One of these restrictions, which appears in s20(a), is that a private company must restrict the free transferability of its shares.[750]

Cilliers and Benade discuss how the restriction on the transfer of shares can manifest itself:

> Forms which the restriction can assume are that the shares may only be transferred subject to the approval of the board or directors, or only to existing members of the company, or only if they have first been offered to the other members, or only to persons approved of by all the members or by a particular person and so forth.[751]

Thus, the issuing of shares is subject to a company's articles, which is, in turn, subject to the restrictions in s20 and upon purchasing shares the shareholder agrees to the restrictions. The restrictions which a private company is compelled to insert into its articles effectively amount to a *pactum de non cedendo*.[752]

In addition to the provisions of s20 of the Companies Act, s65(2) of the Act also elevates the articles to the status of a contract between the company and its members. Since it is impossible to be a member of a private company without also being a shareholder at the same time, the articles

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[748] The restrictions on the transfer of shares may also be written into the articles of a public company, although public companies are not statutorily required to do this.

[749] Cilliers and Benade op cit 40.

[750] Ibid.

[751] Ibid.

[752] See MS Mphalele 'Cession of the rights of a member in a close corporation' 1998 *Journal for Juridical Science* (vol 21) 244 256. Although the article discusses *pacta de non cedendo* in close corporations, the general idea is the same as in private companies.

(which contain the *pacta de non cedendo*) constitutes an agreement between the company and its shareholder.[753]

Should a private company elect to adopt the model articles, such a restriction can be found in article 11 of the model articles. This article states that the directors of a company have the power to refuse to register the transfer[754] of any shares without giving reasons therefor.

This restriction was illustrated in *Richter N.O v Riverside Estates (Pty) Ltd*[755] where, although the company had drafted its own articles, the articles contained a provision almost the same as that of article 11.

The court held that if *pacta de non cedendo* are valid, then the restriction on the transfer of shares in the company's articles, to which the shareholder had agreed (by virtue of purchasing the shares subject to the articles) was also valid, as such a restriction amounts to a *pactum de non cedendo*.[756]

Another restriction is to be found in articles 21-24 of the model articles. These articles state that if a shareholder desires to sell his shares he must give written notice thereof to the directors of the company. The directors subsequently have one month in which to first offer the shares for purchase to the other shareholders.[757] Should the other shareholders not purchase the shares within that time, the shareholder may only then offer it to a person outside of the company.[758]

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[753] *De Villiers v Jacobsdal Saltworks (Pty) Ltd* 1959 (3) SA 873 (O).

[754] The word 'transfer' (of shares) in the Companies Act encompasses the cession of the shares, the completion of the transfer document in terms of s133 and the placement of the shareholder's name in the register of members. See *Smuts v Booyens*; *Markplaas (Edms) Bpk en 'n ander v Booyens* 2001 (4) SA 15 (SCA) 21H.

[755] 1946 OPD 209. See Chapter 3 for a case summary.

[756] Supra 226.

[757] As stated in article 22.

[758] As stated in article 24.

These two restrictions (that is, in terms of articles 11 and 21-24) appeared in the articles of a company under consideration in *Van der Berg v Transkei Development Corporation,*[759] where the court confirmed that the restrictions indeed amounted to *pacta de non cedendo*. The court further added that the prohibitions would bind a deputy-sheriff of the court who sells the shares in execution of a debt.[760]

The case of *Britz NO v Sniegocki and others* [761] illustrated that a provision in a company's articles first requiring the company's consent before a share is transferred, also amounts to a *pactum de non cedendo*. A transfer of shares in contravention of a *pactum de non cedendo* is accordingly 'incomplete' or 'ineffective'.[762]

The court's reasoning can be summed up by the following passage:

> It seems to me that the rights constituting the shares were created with conditional restrictions against alienation. These restrictions are contained in the document recording it and the right itself is limited by the conditional stipulation against alienation.[763]

This passage is founded on the words in *Paiges,*[764] and the effect of a cession subject to a *pactum de non cedendo* with regard to shares seems to be the same as that of a *pactum de non cedendo* concluded in general

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[759] 1991 (4) SA 78 (Tk) 80C. See Chapter 3 for a case summary.

[760] Supra 81G-H.

[761] 1989 (4) SA 372 (D). It must be pointed out that the company under discussion in this case was not a private company, but a public company. This means that it was not required by statute to restrict the transfer of its shares, but it elected to do so by choice, with such a restriction amounting to a *pactum de non cedendo*. See Chapter 3 for a case summary. See also JM Otto 'Oorsig van regspraak: sessie' 1990 *De Rebus* (vol 19) 101.

[762] Supra 383D-E.

[763] Supra 383B.

[764] *Paiges v Van Ryn Gold Mine Estates* 1920 AD 600 617: 'The stipulation against cession is part and parcel of the agreement creating the right, and the right is limited by the stipulation'.

contracts as discussed in *Paiges*: Ineffective to vest ownership in the cessionary.[765]

The most authoritative case on the issue is that of *Smuts v Booyens*; *Markplaas (Edms) Bpk en 'n ander v Booyens*.[766] In this case the Appeal Court confirmed the existing case law by stating that if a private company adopts the model articles and the procedure in articles 21 – 24 is not complied with before the shares are offered to a person who is not a shareholder, the rights to the shares cannot be transferred at all.[767] The court added that the right would 'from its inception, lack the attribute of transmissibility' as the restriction would be in the form of an absolute prohibition.[768]

It is interesting to note that a *pactum de non cedendo* does not bind the trustee in insolvency, yet it does bind the deputy-sheriff when attaching shares in execution of a debt. Surely both are instances of involuntary cessions? Yet different rules apply.

Another noteworthy observation is that none of the cases dealing with *pacta de non cedendo* with relation to shares make reference to the interest requirement – that is – that the prohibition must be in the interest of the company (the debtor). Nor do the courts refer to *Trust Bank* as an authority for having departed from the interest requirement when the *pactum de non cedendo* appears in the articles or the shareholder's agreement creating the personal right from its inception (as is usually the case with shares).

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[765] *Van der Berg v Transkei Development Corporation* 1991 (4) SA 78 (Tk) 81G: non-transferable until the articles have been complied with. *Smuts v Booyens*; *Markplaas (Edms) Bpk en 'n ander v Booyens* 2001 (4) SA 15 (SCA) 24G: intransmissible *ab initio*.

[766] 2001 (4) SA 15 (SCA). See Chapter 3 for a case summary. The *ratio* in the *Smuts v Booyens* case has been followed in the recent case of *Sindler NO and others v Gees and others and six other cases* 2006 (5) SA 501 (C) 506G-H.

[767] Supra 22D read with 24F.

[768] Supra 24G read with 24H-25A.

It appears that these courts have abandoned the interest requirement and in doing so have ignored the *ratio* in *Paiges*. Perhaps the interest requirement has been abandoned in company law because a private company is required by statute to place restrictions on the transfer of its shares.

A situation which has not been addressed by the courts is where a shareholder in breach of a *pactum de non cedendo* cedes his shares to a third party, for example a bank, as security for a loan. If the restriction in the articles is an absolute one, it appears that a security cession would not be possible since the courts have made it very clear that the personal right would 'lack the attribute of transmissibility' and 'cannot be transferred at all'. The third party-cessionary of shares ceded *in securitatem debiti* in such a case would effectively receive nothing.

The situation would be different if the restriction on transfer is not absolute, for example, if the articles only restricts registration and consequently membership, but does not restrict the cession of the shares. In such a case it seems as though a cession *in securitatem debiti* with the pledge construction may take place, because if this construction is carefully considered, the shares are not ceded, but only pledged as security.[769] It appears as though a cession *in securitatem debiti* with the *pactum fiduciae* construction would result in a valid transfer of ownership of the shares since this construction effects an out-and-out cession.[770] The company (the debtor), however, would be fully entitled to refuse to register and recognise the third party-cessionary as a member of the company. This would result in ownership vesting in a third party, being the beneficial owner of the shares and membership and shareholding vesting in the cedent being the nominee shareholder.

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[769] See below for a more detailed explanation of the pledge construction.

[770] See below for a more detailed explanation of the *pactum fiduciae* construction.

The third party may decide to sue the company on the basis that it was unaware of the *pactum de non cedendo* in order that its name can be entered into the register of members and consequently be recognised as a shareholder. The question was raised in the court *a quo* of *Smuts v Booyens* whether a company can argue constructive notice against a third party. A company may raise this as a defence against those dealing directly with it, but can a company raise constructive notice against a third party in such an instance? The question was not dealt with in the Appeal Court because, on the facts, Cameron JA found it unnecessary to consider.[771]

5.2.2 American law

In America the Model Business Corporation Act[772] is a model piece of company law legislation upon which the different states in America may base their company law legislation.[773]

According to the Model Business Corporation Act, restrictions on share transfers are valid and enforceable provided that the restriction is conspicuously noted on the front or back of the share certificate. If no share certificate was presented, the proviso is that the company sends the

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[771] *Smuts v Booyens* supra 25 E-F.

[772] Http://www.abanet.org/buslaw/committees/CL270000pub/nosearch/mbca/assembled/20051201000001.pdf (accessed on 30 April 2009). This Act is revised every year. About 35 American states have company law legislation based on the Model Business Corporation Act. The state of Delaware has drafted its own company laws in a statute called the Delaware General Corporation Law, which is completely different from the Model Business Corporation Act, yet it, too, has very similar provisions to the Model Business Corporation Act regarding the restrictions on share transfers [s202(a)-(e)]. Further, other states, where many large companies are located, have legislation that combines the Model Business Corporation Act and the Delaware General Corporation Law and thus also apply the same principles governing share transfer restrictions, for example New York, California, Texas and Illinois.

[773] See generally AC Harberle et al in *American Jurisprudence* 2ed vol 18A (1985) 557-569; RW Hamilton *Corporations* 4ed (1997) 288-293; FH O'Neal 'Restrictions on transfer of stock in closely held corporations: Planning and drafting' 1952 *Harvard Law Review* (vol 65) 773; CA Platt 'The right of first refusal in involuntary sales and transfers by operation of law' 1996 *Baylor Law Review* (vol 48) 1197; MB Gershanik 'Legislature provides for certificateless shares; amends law on transfer restrictions' 2005 *Louisiana Bar Journal* (vol 53) 237; SR Carpenter 'Net operating losses: Preserving what you never wanted in the first place' 2007 *Utah Bar Journal* (vol 20) 16.

new shareholder an information statement containing (amongst other things) the restrictions attached to the shares.[774]

The Model Business Corporation Act also states that, should the transfer restrictions not be conspicuously noted on the share certificate, or if an information statement is not sent to the shareholder, then the restriction on transfer is not enforceable against a person not having knowledge thereof.[775]

The Act includes two of the restrictions contained in the South African model articles. The first is the transfer restriction subject to approval by the directors, although the Model Business Corporation Act goes a step further by permitting the approval to come from any person provided the approval or disapproval is not manifestly unreasonable.[776]

The second is the restriction that the shareholder first offer the shares to the company or to other shareholders or to any other person before offering it to a person outside the company.[777]

A prohibition not included in the South African Companies Act, but which is contained in the Model Business Corporation Act, is the ability of a company to prohibit the transfer of shares to designated persons or classes of persons, provided however, that the prohibition is not manifestly unreasonable.[778]

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[774] Model Business Corporation Act s6.27(a)-(b). The Uniform Commercial Code article 8-204 has a similar provision regarding restrictions on the transfer of securities (shares sold on the stock exchange) as such transfers are ineffective against a person without knowledge of the restriction, unless the restriction appears conspicuously on the security certificate or the registered owner has been notified of the restriction.

[775] Model Business Corporation Act s6.27(b).

[776] Model Business Corporation Act s6.27(d)(3). See also O'Neal op cit 776 – a 'closely held corporation' is akin to a private company in South African law.

[777] Model Business Corporation Act s6.27(d)(1). See also O'Neal op cit 776.

[778] Model Business Corporation Act s6.27(d)(4).

Another difference between the South African model articles and the Model Business Corporation Act is that in South Africa share transfer restrictions are generally found in the articles or in shareholder's agreements, although restrictions may validly be found elsewhere. According to the Model Business Corporation Act, however, share transfer restrictions are commonly found in various locations. The articles of incorporation[779] may contain a restriction, or it may be contained in a by-law[780] of the company, or it may be included in an agreement amongst the shareholders, or in an agreement between the shareholders and the company.[781]

Lastly, it seems as though the restriction requiring a shareholder to first offer the shares to certain people (like shareholders) before others, would not apply to an involuntary transfer or to a transfer by operation of law.[782]

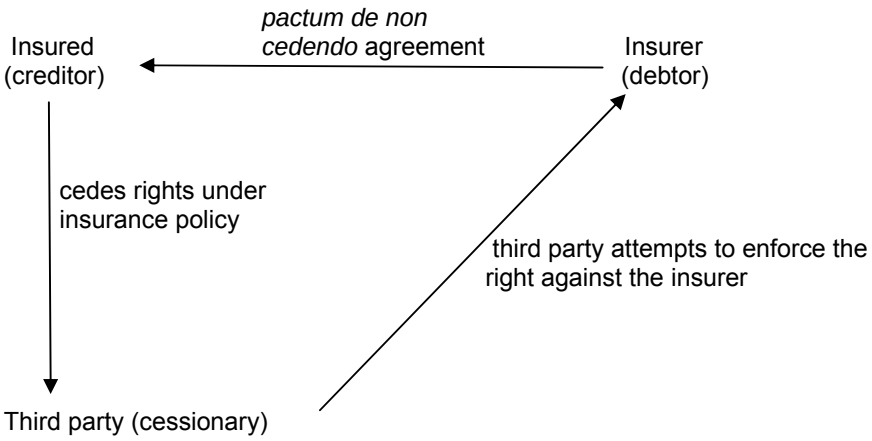
[779] In American law the 'articles of incorporation' is not equivalent to our articles of association, but rather to our memorandum of association.

[780] A 'by-law' is akin to a regulation made by the company.

[781] Model Business Corporation Act s6.27(a). See also O'Neal op cit 785-786.

[782] Harberle et al op cit 571 and 573. See also Platt op cit 1209-1210 where she discusses that this can only be seen as a general principle as there seems to be controversy in some states, for example, Texas where there is authority for the view that an involuntary transfer would also be bound by such a restriction. In her conclusion (1211) she states that the courts may be moving toward a tendency of enforcing these restrictions upon involuntary transfers.

5.3 Insurance law



5.3.1 South African law

In South African law an insured can freely cede his rights under an insurance policy without the consent, and even without the knowledge of the insurer (usually an insurance company).[783] The right which is transferred is the insured's conditional right to be indemnified if he suffers a loss when the risk insured against materialises.[784] The effect of a cession of rights under an insurance policy is illustrated by the following quotation:

> The effect of a cession is that the claim vests in the cessionary and nothing remains with the cedent. The cessionary is creditor and as such is the only person who can sue for or receive payment. Thus, if the insured has ceded his conditional right to indemnification, it is the cessionary who can claim and receive payment if the insured should subsequently suffer a loss.[785]

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[783] MFB Reinecke et al 'Insurance' in *LAWSA* first re-issue vol 12 (2002) para 435. The cession of the rights under an insurance policy must be distinguished from the assignment of the policy (otherwise known as subrogation), which in insurance law has acquired a specific meaning. Assignment of the insurance policy denotes the substitution of the original insured with another person and a different set of legal principles applies. See Reinecke et al op cit para 439. See also DM Davis *Gordon and Getz on the South African Law of Insurance* 4ed (1993) 267 footnote 1.

[784] Reinecke et al op cit para 435. It further seems perfectly valid for the insured to cede his rights under the insurance policy regardless of whether or not the risk insured against has occurred and regardless of whether the policy is one of indemnity insurance or non-indemnity insurance (life insurance).

[785] Reinecke et al op cit para 437.

It often happens, however, that insurance policies contain clauses which restrict or absolutely prohibit the cession of rights under the policy. Obviously echoing the *Paiges* case, the applicable legal principle for a *pactum de non cedendo* to be valid and enforceable in an insurance policy, is proof that it serves a useful purpose.[786] It has been held that, for an insurer, this requirement is easy to prove.[787]

Once the insurer has proved that the *pactum de non cedendo* serves a useful purpose, it stands to reason that a cession in contravention is void and cannot vest ownership in the cessionary.[788] In this manner *pacta de non cedendo* in insurance contracts are treated in the same way as *pacta de non cedendo* that feature in general contracts.

Controversy only arises when the insurance policy contains a *pactum de non cedendo* and the insured cedes his rights under the policy in contravention thereof as security for a debt – a so-called cession *in securitatem debiti*.[789]

If a right is ceded *in securitatem debiti*, it is largely unsettled as to which legal construction is intended, unless of course it is clear from the agreement between the parties.[790] The construction can either be one of pledge or of *pactum fiduciae*.

The pledge construction is well known for being imprecise and 'obscure'.[791]

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[786] Davis op cit 267; Reinecke et al op cit para 436.

[787] *Northern Assurance Co Ltd v Methuen* 1937 SR 103 111. See Chapter 3 for a case summary. See also Davis op cit 267; Reinecke et al op cit para 436.

[788] The cessionary would presumably have an action for damages for breach of contract against the insured (the purported cedent).

[789] See PM Nienaber 'Cession' in *LAWSA* 2ed vol 2 (2003) para 52-56; S Van der Merwe et al *Contract General Principles* 2ed (2003) 463 *et seq*; Badenhorst et al *Silberberg and Schoeman's The Law of Property* 4ed (2003) 377-379.

[790] Davis op cit 274.

[791] Van der Merwe et al op cit 467.

The court in *Muller v Trust Bank*[792] stated that this construction is based on the principles governing the pledge of a corporeal movable where the right of action is pledged to the cessionary.

The cedent, notwithstanding the cession, still retains ownership or a 'bare dominium'[793] despite the fact that while the cession is operative the cedent is precluded from exercising his rights against the debtor.[794]

The courts in *Cohen's Trustee,*[795] *Muller*[796] and *Millman v Twiggs,*[797] stressed that the cessionary does not obtain ownership, but only obtains a *jus in re aliena* which allows him to realise the right should the cedent default.

The cedent also has a reversionary interest in that once the debt has been discharged the right of action must be reverted to him, thus he need only demand the return of his property and a re-cession is not necessary to complete his title.[798]

This construction has been heavily criticised as being unsound for a number of theoretically based reasons,[799] yet the courts still prefer this construction to that of the *pactum fiduciae* construction.[800]

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[792] *Muller v Trust Bank of Africa Ltd* 1981 (2) SA 117 (N) 123G and 124E-F. See also *Trust Bank of Africa Ltd v Standard Bank of South Africa Ltd* 1968 (3) 166 (A) 186.

[793] *Italtrafo SpA v Electricy Supply Commission* 1978 (2) SA 705 (WLD) 712.

[794] *National Bank of South Africa Ltd v Cohen's Trustee* 1911 AD 235 256; Davis op cit 272-273.

[795] Supra 242.

[796] Supra 123H-124A.

[797] *Millman NO v Twiggs and another* 1995 (3) SA 674 (A) 676G-H.

[798] *Cohen's Trustee* supra 246-247.

[799] Van der Merwe et al op cit 467. The reasons can be listed as follows: (1) There is no historical basis for using this construction when dealing with incorporeals. (2) The notion that a cessionary can obtain a real right of security in an incorporeal asset is unsound as one cannot have a real right over a personal right. (3) The fact that the cedent can retain the *dominium* in the personal right which has been ceded as security defies the essence of a cession. (4) The idea that a right of pledge (which requires delivery) can exist in respect of an asset which is incapable of being possessed is flawed.

A question that may be rightfully asked is why the cedent's rights are returned to him on demand without the need for a cession to restore his title? If the cedent ceded the rights under the insurance policy as security for a debt, when the debt has been discharged, how else can he possibly retrieve the rights other than by a re-cession? If the cedent can simply demand the rights back, then he never ceded them in the first place. If the parties' intentions are to effect a security cession, then the existence and use of the pledge construction is totally inappropriate. Further, a security cession by way of pledge is clearly a misnomer as cession does not actually take place. Should our courts insist on using this construction it should be termed something which reflects more accurately the transaction it describes.

According to the *pactum fiduciae* construction, the right of action is completely ceded to the cessionary, together with an undertaking (the *pactum fiduciae*) that the cessionary will re-cede the right of action to the cedent upon discharge of the debt.[801] The right of action thus vests completely in the cessionary and the cedent is left with a personal right to enforce the re-cession once the debt has been discharged.[802]

If the parties' intentions are unclear and the pledge construction is preferred, then the *pactum de non cedendo* has not *actually* been breached, as ownership of the right still vests in the insured (the cedent). During the course of the security cession, however, the cedent cannot

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[800] Innes CJ in the *Cohen's Trustee* case 251-252 stated that although judicial recognition has been given to the *pactum fiduciae* construction (using *Sutherland v Elliot Bros* 2 Menzies 349 as an example), he and the other judges still preferred the pledge construction; the court in *Muller* 123G held that the right of parties under a cession *in securitatem debiti* must be determined according to the law of pledge; the Appellate Division in *Millman v Twiggs* 671G authoritatively stated that 'when a right is ceded with the avowed object of securing a debt, the cession is regarded as a pledge of the right'. Notable cases that have showed a preference for the *pactum fiduciae* construction are *Lief v Dettmann* 1964 (2) SA 252 (A) and *Trust Bank of Africa Ltd v Standard Bank of South Africa Ltd* 1968 (3) 166 (A).

[801] Davis op cit 271-272; Nienaber op cit para 53; Van der Merwe et al op cit 465-466.

[802] Ibid.

claim performance from the insurer, nor can the insurer validly perform to the cedent as the rights under the policy have been ceded.[803]

This effect is surely something the insurer wished to guard against by inserting the *pactum de non cedendo* into the insurance policy in the first place. The insurer cannot sue for damages as the contract has not, strictly speaking, been breached. Perhaps a cession in this manner could be a ground upon which to cancel the policy.[804]

If the *pactum fiduciae* construction is preferred, then it seems that the *pactum de non cedendo* has been breached, as ownership would then vest in the cessionary. The insurer would be fully within its rights to claim damages therefor. My only reservation is that the insured (the cedent) is not left empty-handed. The insured is left with a personal right to re-cession, which is obviously not ownership, but neither is he left with nothing as is the usual outcome after a cession.

Cessions *in securitatem debiti* are first and foremost cessions, regardless of the fact that they are cessions in security. There should be, therefore, only one construction of cessions *in securitatem debiti*.[805] Accordingly, cessions *in securitatem debiti* of insurance policies containing a *pactum de non cedendo* should be considered as ordinary cessions and should be treated as such.

5.3.2 American law

In this legal system a distinction is drawn between life insurance policies and indemnity (or property insurance) policies. The validity and effect of

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[803] Reinecke et al op cit para 438.

[804] Cancellation would depend on the terms of the policy. This is most certainly still largely undeveloped.

[805] See my criticism of the pledge construction above.

an anti-assignment clause appearing in these policies is correspondingly different.[806]

In the absence of a provision to the contrary, life insurance policies may be freely assigned as they are deemed to be investments.[807] Should an anti-assignment clause be present in a life insurance policy, it would, however, be valid and binding.[808]

An indemnity insurance policy, on the other hand, is considered to be a personal undertaking, as it is not so much the property itself that is insured, but rather the interest of a particular person in that property.[809] In fact, indemnity insurance policies usually contain anti-assignment clauses, subject to the consent of the insurer first being obtained.[810] If such a policy is assigned without the consent of the insurer the assignment is ineffective.[811]

The situation is different once the risk materialises or the loss occurs, as then the insured is free to assign the policy without the consent of the insurer.[812] The reason for this is because:

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[806] See generally PF Hofer 'Corporate succession and insurance rights after Henkel: A return to common sense' 2007 *Tort Trial and Insurance Practice Law Journal* (vol 42) 763; ER Anderson and J Gold 'Assignment of insurance claims by policyholders to underlying claimants' 1997 *Practising Law Institute* (vol 557) 687.

[807] SL Johnson et al 'Insurance' in *American Jurisprudence* 2ed vol 43 (1982) 851; RA Lord *Williston on Contracts* 4ed vol 17 (2000) 105-107; NN Bernstein *International Encyclopaedia of Laws* vol 3 (2002) 61.

[808] RA Anderson *Couch on Insurance Law* 2ed vol 16 (1983) 756-757. The anti-assignment clause would only be valid and binding before the loss occurs. Once the loss has occurred the policy may be freely assigned. See Johnson et al op cit 854.

[809] Johnson et al op cit 852; Bernstein op cit 61.

[810] Ibid. Or they prohibit assignment absolutely before loss.

[811] Johnson et al op cit 852; Anderson and Gold op cit 696; Hofer op cit 771.

[812] Lord op cit 124-125; Anderson op cit 763-765. Further, a provision prohibiting assignment is only effective before the loss or death has occurred. A provision prohibiting assignment absolutely after loss or death is accordingly null and void on the basis of public policy. See Johnson et al op cit 854; Anderson op cit 758-759, 766; Bernstein op cit 61. See also Anderson and Gold op cit 697 *et seq*; Hofer op cit 771.

> [Once the loss has occurred]… it is not the personal contract which is being assigned, but a claim under or a right of action on the policy.[813]

Insurance contacts indemnifying against the risk of fire are singled out and treated slightly differently. Fire insurance policies may not be assigned before loss as they are also regarded as personal contracts.[814] Further, sometimes the insurer does not have a discretion on whether to include an anti-assignment clause in a fire insurance policy – legislation may, in certain states, oblige an insurer to include such a prohibition.[815]

Cessions *in securitatem debiti*, or assignments as collateral or security as they are termed in America, are generally permitted on the premise that an insurance policy is 'a species of property which may be pledged'.[816]

If, however, the insurance policy is subject to an anti-assignment clause and the insured assigns the policy as collateral for a debt before loss has occurred, the assignment would generally be valid even without consent.

The reason for this is because an assignment as collateral would not fall within the meaning and scope of a general provision preventing

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[813] Johnson et al op cit 854.

[814] Johnson et al op cit 852. See also KH York, JW Whelan and LP Martinez *Cases, Materials and Problems on General Practice Insurance Law* 3ed (1994) 224. The authors discuss the case of *Christ Gospel Temple v Liberty Mutual Insurance Co* 417 A.2d 660 (1979) where the judge held that: 'It is well settled that a fire insurance policy is a *personal* contract of indemnity, and is on the insured's *interest* in the property, *not the property itself*'. [Judge's emphasis]

[815] Anderson op cit 757; York et al op cit discuss the case of *Christ Gospel Temple v Liberty Mutual Insurance Co* supra and include the following passage from the case: 'Although the Appellants argue on several grounds, that we must ignore the clear prohibition against assignments without Liberty's consent, we can find no legal basis for doing so. The provision in question [*viz* the provision prohibiting assignment] is not simply a self-protective clause inserted the whim of the Appellee, but rather a legislatively mandated provision, *specifically required* to be included in fire insurance policies such as the one in issue in the instant case'. [Judge's emphasis]

[816] Johnson et al op cit 859. See also MC Dransfield 'Transfer or pledge of fire insurance policy as collateral security for debt within policy provisions prohibiting or restricting assignment of policy' 1953 *American Law Reports* 2d (vol 31) 1199. This article, however, only focuses on the assignment of a fire insurance policy as collateral for a debt, but considers the issue from the perspective of many of the individual states of America and provides a comprehensive overview of the case law.

assignment. The policy must expressly prohibit the assignment of *any* interest *whatsoever* under the policy in order to prevent an assignment as collateral in addition to an ordinary assignment.[817]

In the absence of a specific anti-assignment clause, American law permits a security assignment of the rights under insurance policies (even before loss has occurred) because when a security assignment is made, the insured is not divested of his legal interest in the policy.[818] The assignee acquires only 'an equity' under the policy by the creation of a lien in his favour to the extent of the debt owed.[819]

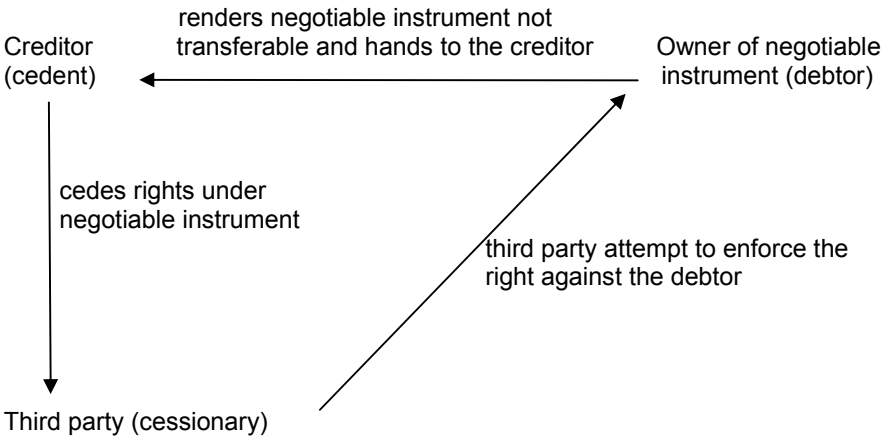
In terms of the American law approach, 'assignment' of an insurance policy as collateral for a debt would actually be a misnomer since nothing would be transferred to the 'assignee'. The 'assignee' merely acquires an equity in the policy to the amount of the debt that manifests itself in a lien. Apart from the misleading name, security cessions in America are definitely more theoretically acceptable than security cessions in South African law.

[817] Johnson et al op cit 859-860. See also Dransfield op cit 1199 *et seq*, in so far as fire insurance policies which are assigned as collateral are concerned.

[818] Ibid.

[819] Johnson et al op cit 859-860; Bernstein op cit 61. In American law a lien describes a 'non-possessory' security interest, unlike in South African law where a lien describes the right to retain (or possess) something until a debt has been paid. An equitable lien is 'a right enforceable only in equity to have a demand satisfied out of a particular fund or specific property without having possession of the fund or property.' See http://en.wikipedia.org/wiki/Lien (accessed on 22 July 2009). See also PJ Badenhorst et al *Silberberg and Schoeman's The Law of Property* 4ed (2003) 389 *et seq*.

5.4 Negotiable instruments



5.4.1 South African law

A negotiable instrument, such as a bill of exchange, cheque or promissory note, has been described as:

> … a legal document entitling the holder thereof to a specified sum of money…the right to the sum of money is transferable with the ease with which a cash payment is made. It is obvious that the handing over of an instrument presents a safer and more convenient method of transferring money or the right to a sum of money from one person to another.[820]

A fundamental characteristic of a negotiable instrument is its ability to be transferred from person to person.[821] This transfer usually takes place through negotiation,[822] and if the bill is taken in good faith and for value (*inter alia*), the transferee becomes the holder in due course.[823] The

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[820] MA Fouché et al *Legal Principles of Contracts and Negotiable Instruments* 5ed (2003) 270.

[821] It must be stated at the outset that this discussion focuses only on a negotiable instrument which is an order document and not a bearer document.

[822] The word 'negotiation' merely means a transfer that complies with s29 of the Bills of Exchange Act 34 of 1964. See FR Malan and JT Pretorius *Malan on Bills of Exchange, Cheques and Promissory Notes* 4ed (2002) 129; Fouché et al op cit 276.

[823] Malan and Pretorius op cit 129; Fouché et al op cit 270, 276.

position of the holder in due course is a secure one since it remedies an absence of title or any defect in title of the transferor.[824]

A negotiable instrument (or rather the rights thereunder) may also be transferred through an ordinary cession, where the transferee does not become the holder or holder in due course, but the cessionary.[825] In such a case the cessionary-transferee takes the instrument subject to a lack of title or any defects in the title of the cedent-transferor and is not afforded the secure position of a holder in due course.[826]

It often happens that a party[827] wishes to make the instrument non-transferable – that is – that the instrument goes no further than the named payee or an indorsee. In terms of s6(5) of the Bills of Exchange Act a party can make a bill of exchange non-transferable by inserting words prohibiting transfer, or indicating an intention that the bill should not be transferable.[828] In terms of s75A of the Bills of Exchange Act a party can render a cheque non-transferable by, *inter alia*, writing the words 'not transferable' boldly on the face of the cheque usually between transverse

[824] Fouché et al op cit 270. The title of holder in due course is thus an exception to the general rule contained in the maxim *nemo plus iuris ad alium transferre potest quam ipse haberet*.

[825] DV Cowen and L Gering *Cowen on the Law of Negotiable Instruments in South Africa* 4ed (1966) 6-7, 271-272; Malan and Pretorius 164; A Govindjee 'Negotiable Instruments' in *LAWSA* 2ed vol 19 (2006) para 65. See also *Factory Investments (Pty) Ltd v Ismail* 1960 (2) SA 10 (T) 13.

[826] Cowen and Gering op cit 6-7, 271-272; Malan and Pretorius op cit 132; Govindjee op cit para 65.

[827] Usually the drawer, the person who gives the order to the drawee (usually a bank in the case of cheques), to pay a sum of money to the named payee (or his indorsee). Fouché et al op cit 270.

[828] See also *Standard Bank of South Africa Ltd v Sham Magazine Centre* 1977 (1) SA 484 (A).

parallel lines.[829] A promissory note with the word 'only' written clearly and legibly after the name of the payee will render it non-transferable.[830]

The question that now arises is whether such transfer prohibitions would have the effect of *pacta de non cedendo* on negotiable instruments that are transferred through cession.

The court in *Trust Bank v Standard Bank*[831] touched indirectly on this issue. The topic of discussion in this case was deposit vouchers that were subject to a condition stating that they were neither transferable nor negotiable.

While all the judges in this case agreed that deposit vouchers were not negotiable instruments, there was some dispute as to whether the condition upon which they were issued amounted to a *pactum de non cedendo*.

In the minority judgment of Ogilvie Thompson JA, the opinion was expressed that the prohibition on transfer concerned the document itself (the piece of paper) and not the rights embodied therein. A transfer of the rights was thus possible as the prohibition did not constitute a *pactum de non cedendo*.[832]

The majority were of the view that, although the deposit vouchers only evidence the rights recorded therein, on an ordinary interpretation, the words prohibiting transfer were an attribute of those rights and not the

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[829] See generally *Standard Bank of South Africa Ltd v Sham Magazine Centre* 1977 (1) SA 484 (A); *Eskom v First National Bank of Southern Africa Ltd* 1995 (2) SA 386 (A).

[830] L Gering and DG Tobias *Handbook on the Law of Negotiable Instruments* 3ed (2007) 154; *Standard Bank of South Africa Ltd v Sham Magazine Centre* 1977 (1) SA 484 (A) 503-504.

[831] *Trust Bank of Africa Ltd v Standard Bank of SA Ltd* 1968 3 SA 166 (A). See Chapter 3 for a case summary.

[832] Supra 182C.

document itself. The prohibition was accordingly held to amount to a valid *pactum de non cedendo*.[833]

Would the judges' opinions have been different if the instrument under discussion was a negotiable instrument that had been ceded contrary to a prohibition on the face of it?

Malan and Pretorius submit that words prohibiting transfer do not necessarily prevent a cession of the rights, as these prohibiting words would usually refer to the document itself and not to the rights embodied therein. [834]

On the other hand, according to Govindjee,[835] who relies on *Trust Bank* as authority, if the rights under a negotiable instrument are ceded despite words prohibiting transfer, for example, payable 'to X only' or marked 'not transferable', such a cession would be invalid. It seems as though this author has applied the majority *ratio* in *Trust Bank*, a case not concerning negotiable instruments, to a situation dealing with negotiable instruments.

Govindjee is not alone in his view. Oelofse is also of the opinion that rights under a document marked 'not transferable', or that is payable to a specific person only, can in no manner be transferred.[836]

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[833] Supra 190C, 191B-C.

[834] Malan and Pretorius op cit 429-430. See also FR Malan 'Die nie-oordraagbare tjek' 1980 *De Jure* 391 393 where he states that because personal rights arising from bills of exchange can be transferred by cession (as illustrated by *Factory Investments (Pty) Ltd v Ismail* supra) it stands to reason that the *ratio* in the *Trust Bank* case cannot be directly applied to negotiable instruments like bills of exchange, cheques and promissory notes. Malan also associates himself with the minority judgment of Ogilvie Thompson JA (as explained above) and described this judgment as insightful ('insiggewend'). See also FR Malan 'The liberation of the cheque' 1978 *Tydskrif vir die Suid-Afrikaanse Reg* 107 116.

[835] Govindjee op cit para 65.

[836] AN Oelofse 'Rektawissel en rektajtek, verhandeling en sessie in die Duitse en Suid-Afrikaanse reg' 1987 *Modern Business* (vol 9) 129 135 where he uses the cases of *Volkskas Bpk v Johnson* 1979 (4) SA 775 (K) and *Gishen v Nedbank Ltd* 1984 (2) SA 378 (W) in support of his view. Neither of these cases deal with the issue directly, but proceed on the assumption that a cession of a non-transferable instrument is not possible.

Oelofse points out that words excluding negotiation of an instrument, for example, 'not negotiable' or 'not indorsable', may rule out a negotiation of the instrument, but not a cession as the instrument is still susceptible to be transferred by any other mode.[837] In his view, where transfer in general is prohibited, then even a cession is not possible. He notes that it is ultimately the construction of the prohibitory words that will determine whether the instrument can be ceded or not.[838]

A convincing argument can be made in support of the authors who hold the view that a negotiable instrument which is not transferable precludes a transfer through cession. Were it otherwise, the presence of a *pactum de non cedendo* on the instrument would make little sense. More compellingly, however, it must be remembered that a negotiable instrument (the piece of paper itself) and the rights thereunder are inextricably linked. If prohibitory words appear on the face of the document, the prohibition pertains not only to the document itself, but also to the rights it embodies.

Thus, in my opinion, the minority judgment of Ogilvie Thompson JA and the view of Malan are flawed, since the document itself is worthless without the rights which attach thereto.

5.4.2 American law

In America the law of negotiable instruments is governed by article 3 of the Uniform Commercial Code (hereinafter referred to as the 'UCC'). As in South African law, negotiation is the usual manner in which a negotiable instrument is transferred. The UCC dictates whether a transfer amounts to

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[837] Oelofse op cit 136.

[838] Ibid.

a negotiation or whether a transferee has the right to compel a negotiation.[839]

As in South African law, an assignment of a negotiable instrument will not confer on the assignee a better title than that of the assignor, and he takes subject to equities.[840]

Although the UCC recognises that a negotiable instrument may be transferred by way of assignment,[841] article 3 of the UCC states that transfers of negotiable instruments are generally regarded as negotiations. These two methods of transfer are therefore deemed to be clearly separate from each other and are accordingly treated differently.[842]

The general law of contract and assignment seems to be the applicable governing law when a negotiable instrument is assigned, and not article 3 of the UCC.[843]

If, therefore, a negotiable instrument is negotiated in accordance with the UCC, the rules therein are applicable. If a negotiable instrument is assigned, then the general principles governing assignment are applicable.

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[839] UCC 3-203 (post 1990 version). FM Hart and WF Willier *Negotiable Instruments Under the Uniform Commercial Code* vol 2 (2007) part 1B-23.

[840] Hart and Willier op cit 1B-23; AMH Foley et al 'Bills and Notes' in *American Jurisprudence* 2ed vol 11 (1997) 397, 544.

[841] This possibility is found in the words 'unless otherwise agreed' in UCC 3-203(c). See Hart and Willier op cit part 3-9 – 3-10.

[842] Hart and Willier op cit part 1B-23; Foley et al op cit 397 and 544: 'Negotiability is limited to the special class of contracts known as negotiable instruments, while assignability applies to contractual rights and chooses [*sic*] in action in general, as well as to any right of property or interest therein'.

[843] Hart and Willier op cit part 3-6 – 3-8: 'The rights of the assignee against the assignor are primarily governed by the contract between the two parties…'. See also part 3-8: 'If a negotiable instrument is assigned, Article 3 of the Code generally has little application to the transfer'.

It thus stands to reason that if a negotiable instrument contains an anti-assignment clause or any words prohibiting its transfer, the law as discussed in Chapter 2 would find application.

In Chapter 2 it was explained that there are two types of assignment in American law to which different rules apply: Assignments of a general nature and assignments of a commercial nature.

The Restatement of Contracts is the law governing assignments of a general nature, although the validity and effect would depend upon the interpretation of the Restatements by the courts of a particular state.[844] If a negotiable instrument contains an anti-assignment clause the Restatements and the judicial interpretation thereof would be the applicable law.

Article 9 of the UCC governs contracts of a commercial nature.[845] Article 9, however, functions primarily to regulate the assignment of accounts receivable (book debts) in the context of factoring agreements.[846] Article 9-406(d) renders any prohibition on the assignment of an account receivable as invalid and ineffective if it falls within the definition of 'account'.

Article 9-102(2) defines 'account' as a right to payment of a monetary obligation. A few examples include: Property that has been leased or disposed of, services rendered or to be rendered and an insurance policy issued or to be issued. Article 9-102(2) goes further to state that the definition of 'account' does not include, amongst other things, 'rights to payment evidenced by chattel paper or an instrument'.

[844] For example the 'magic words' or Illinois interpretative approach etc. See Chapter 2.

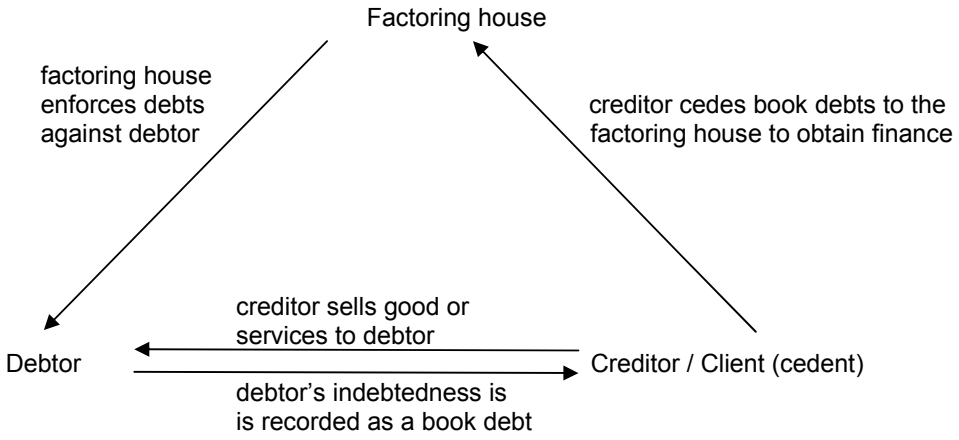
[845] See Chapter 2.

[846] See below as well as Chapter 2 for a further explanation.

In case it was not clear whether the article was referring to a negotiable instrument, article 9-102(47) contains a definition of the word ‘instrument’. This article confirms that the word ‘instrument’ indeed means negotiable instrument.

Accordingly, a negotiable instrument is excluded from the definition of the word ‘account’ and can therefore not find application under article 9 of the UCC. Thus, if a negotiable instrument contains an anti-assignment clause, it can only be dealt with as an assignment of a general nature where the Restatements would be applicable.

5.5 Factoring (book debt financing)



'Book debt financing' or 'accounts receivable financing'[847] as it is also called, is one of the main components of 'factoring'.[848] It has been said that to describe or explain what factoring is in brief is not an easy task due to the lack of agreement regarding its very characterisation.[849]

The basics of a factoring agreement are very similar across most legal systems. What follows is thus a non-legal-system-specific background to factoring agreements before the South African and American legal systems are discussed.[850]

[847] It seems as though 'accounts receivable financing' is the preferred term in America, whereas 'book debt financing' or 'boekskuldfinansiering' appears to be more widely used in South Africa.

[848] The term 'factoring' is often used in a generic sense to refer to the book debt financing component of factoring. See N Joubert 'The legality of continuity clauses in factoring contracts' 1994 *South African Law Journal* (vol 111) 604 (hereinafter referred to as 'continuity clauses').

[849] R Noel, S Mills and N Davidson *Salinger on Factoring* 4ed (2006) 1.

[850] For South African materials dealing with factoring generally see N Joubert *Die Regsbetrekking by Kredietfaktorering* (1985) LLD Thesis Randse Afrikaanse Universiteit (hereinafter referred to as '*Kredietfaktorering*'); N Joubert 'Boekskuldfinansiering en pacta de non cedendo' 1986 *Modern Business* 109 (hereinafter referred to as 'Boekskuldfinansiering') ; N Joubert 'The legal nature of the factoring contract' 1987 *South African Law Journal* 88 (hereinafter referred to as 'The factoring contract'); S Scott 'Sessie en factoring in die Suid-Afrikaanse reg' 1987 *De Jure* (vol 20) 15 (hereinafter referred to as 'Sessie'); S Scott *The Law of Cession* 2ed (1991) 259 *et seq* (hereinafter referred to as '*Cession*'; S Scott 'Claim enforcement (debt collection)' 2002 *SA Mercantile*

I would describe factoring as the business conducted by a 'factoring house' or a 'factor'.[851] It is a dual-faceted system providing credit facilities as well as financial services to clients (predominately small to medium sized businesses) who, in return, sell their book debts or accounts receivable to the said factoring houses.

I classify the factoring system as a dual-faceted one since two main functions can be broadly distinguished:

First, factoring provides immediate cash flow to a business requiring cash for various reasons, for example, to expand the business, to pay off pressing debt, to re-finance credit extended to its customers and to purchase goods or services.[852] Often book debt financing is the only form of financing that a small to medium business can acquire.[853] Further, this type of finance is quick and easy to obtain when compared to a bank loan as the solvency (or insolvency) of the business (the client) is not considered.[854]

Law Journal (vol 14) 491 (hereinafter referred to as 'Claim enforcement'); *Sasfin (Pty) Ltd v Beukes* 1989 (1) SA 1 (A).

[851] There has been much variation in the use of terms describing the factor to the factoring agreement (especially terms in Afrikaans, see Scott 'Sessie' 15 *et seq*. The terms 'finance house' and 'finance company' have also been used. My view is that although any of the listed terms would suffice, I prefer the term 'factoring house' because the factor is usually a large company (or bank) and this term therefore seems more appropriate.

[852] Http://en.wikipedia.org/wiki/Factoring_(finance) (accessed on 17 April 2009); WD Malcolm 'Accounts receivable financing under the uniform commercial code' 1966 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* (vol 30) 434 435; Joubert 'Boekskuldfinansiering' 110.

[853] Joubert *Kredietfaktorering* 467; Joubert 'Boekskuldfinansiering' 109; Noel et al op cit 35-36.

[854] Http://en.wikipedia.org/wiki/Factoring_(finance) (accessed on 17 April 2009). It is rather the strength of the book debts or the creditworthiness of the debtors that will determine whether the factoring house will do business with a potential client.

All the client need do is cede its book debts to the factoring house. Book debts are the monies owing to the client by its debtors.[855] The factoring house would consequently own the book debts and would be legally entitled to enforce them.[856] In return, the factoring house pays the client the monetary value of the book debts minus certain fees, for example, its collecting fee, interest, and sometimes a fee covering the possibility of non-payment.[857]

Secondly, a factoring house provides a range of financial services.[858] These services include notifying the debtor of the change in creditor and most importantly, collecting the debt. Collecting the debt may prove to be a great benefit or advantage to the client since it takes the responsibility of this task out of the client's hands.[859]

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[855] In South Africa book debts may be current or future book debts. See Joubert 'continuity clauses' 604 *et seq*.

[856] It must, however, be added that the specific factoring agreement between the factoring house and the client may stipulate that although the factoring house is legally entitled to enforce the claim, the client must collect the debt and hand over the proceeds. This arrangement is not the usual *modus operandi* of a factoring agreement, but because the parties are free to draw up the contract as they see fit, it is perfectly valid. This, of course, makes it very difficult to describe a typical factoring agreement. See also Malcolm op cit 436.

[857] Http://en.wikipedia.org/wiki/Factoring_(finance) (accessed on 17 April 2009). In America the factoring house usually pays the client a sum of money which is a percentage of the face value of the book debts. The remainder is kept in reserve and held until payment by the client's debtors has been made. The cost associated with the transaction is the factoring house's fee and it is deducted from the reserve and the balance is paid to the client. Sometimes the factoring house may charge the client an additional service charge, as well as interest determined by the period of the debtors' delayed payment. An amount that might not be collected due to non-payment may also be taken into account.

[858] The range of financial services depends upon the specific agreement between the client and the factoring house or on which factoring package the client selects. It is possible that in a specific agreement none of these services may be offered by the factoring house in a certain package, or required by the client. Since a factoring agreement can be so client-specific it is easy to see how the term is so difficult to define.

[859] Http://en.wikipedia.org/wiki/Factoring_(finance) (accessed on 17 April 2009); Scott 'Claim enforcement' 491, 493-494. The task of collecting debt is a specialised service requiring skills and manpower that a small to medium (business) client may not posses. Thus, it eliminates the need for and cost of employing permanent skilled staff to perform this function. It also eliminates the need to outsource the service. As part of the debt collecting service, most factoring houses also provide reports on the creditworthiness of the debtors, keep a detailed history of their payments and provide periodical reports to the client on payments received.

It has been recorded that in 1983 the world factoring turnover was 66 994 million US dollars.[860] The factoring turnover for the same year in South Africa was 725 million US dollars.[861] To illustrate how the factoring industry has grown, in 2004 the total world factoring turnover was 1 161 290 million US dollars.[862] In South Africa in 2004, the total factoring turnover was 9 585 million US dollars.[863] Despite the fact that factoring has been on the rise in South Africa since 1983, when these statistics are considered against those in other countries,[864] it provokes justifiable concern as to why South Africa is lagging behind.[865]

5.5.1 South African law

The factoring house will require some kind of interest in the book debts if it is to extend credit to its client. Book debts are therefore ceded to the factoring house either by an out-and-out cession or as a cession *in securitatem debiti*.[866]

It makes sense that anything that would prevent the factoring house from acquiring such an interest, like *pacta de non cedendo* for instance, poses a grave threat to the smooth functioning of this powerhouse industry.[867] It is perhaps the presence of *pacta de non cedendo* applicable to factoring

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[860] Joubert 'The factoring contract' 88, 89 footnote 4.

[861] Ibid.

[862] Noel et al op cit 360

[863] Noel et al op cit 359.

[864] See Noel et al op cit 359. For example, the total factoring turnover in the United States of America in 2004 was 110 511 million US dollars.

[865] All totals have been expressed as a number in US dollars for the purpose of comparison.

[866] Joubert 'Boekskuldfinansiering' 109. Thus in South African law it seems possible that a factoring contract can come into existence in a situation where, once the credit extended by the factoring house has been repaid by the client, the book debts will once again find themselves in the hands of the client. This is not a typical factoring arrangement.

[867] Joubert 'Boekskuldfinansiering' 109.

contracts that has restrained the growth of the factoring industry in South Africa, whereas this industry is a thriving one in other countries.

One of the main reasons why a debtor would insist that a *pactum de non cedendo* be included in a factoring contract is to prevent a situation where he has to account for the debt twice: Once to the cedent in the false but genuine belief that he is still the creditor and again to the cessionary upon the presentation of proof of cession. If the cedent absconds or is insolvent, the debtor may never recover this undue payment.[868]

Besides the risk of double payment, debtors apparently also seek to avoid the cost, complication and inconvenience of changing the creditor in their books, especially when their bookkeeping is managed by computer programs, as is so often the case.[869] Hence, for the debtor's all-round protection, the *pactum de non cedendo* is frequently seen as a standard clause in contracts, especially for the purchase of goods on credit.[870]

The creditor may have no scope to negotiate if the debtor places a large order of goods while insisting upon a contract containing a *pactum de non cedendo*. This, as a result, leaves the creditor in the lurch if the situation arises where immediate finance is needed.[871]

In South Africa the position of *pacta de non cedendo* applicable to factoring agreements is just as uncertain as that of *pacta de non cedendo* appearing in ordinary contracts: The judicial decisions are somewhat divided on the issue and the correctness of the historical basis as illustrated in the *locus classicus*[872] is doubtful.[873]

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[868] Even if notice of cession was sent to the debtor, such notice can be easily missed. Joubert 'Boekskuldfinansiering' 109; Scott 'Sessie' 33.

[869] Joubert 'Boekskuldfinansiering' 109-110; Scott 'Sessie' 33. Surely nowadays with modern computer programs and technology this would not be a problem?

[870] Joubert 'Boekskuldfinansiering' 110.

[871] Ibid.

[872] *Paiges v Van Ryn Gold Mine Estates Ltd* 1920 AD 600.

Joubert is of the opinion that *pacta de non cedendo* applicable to factoring contracts should be invalid on the basis that they are against public policy. Public policy places a high premium on economic growth and the optimal utilisation of capital. *Pacta de non cedendo* may stifle this if allowed to neutralise book debt financing.[874]

Scott criticises Joubert's straightforward approach as giving almost no attention to the principle of freedom of contract, the interest of the debtor and the reasonableness or not of the *pactum de non cedendo*.[875]

Scott is of the opinion that when the *pactum de non cedendo* appears in the contract creating the right, then according to the principle of freedom of contract, the right to cede the book debts becomes non-transferable regardless of whether or not the restriction is in the interest of the debtor.[876]

If the *pactum de non cedendo* was super-imposed on an already existing right, Scott is of the opinion that the right to cede the book debts is only transferable if the debtor has an interest.[877] Should such an interest exist and should the book debts be ceded contrary to the prohibition, the debtor has an action for damages for breach of contract.[878]

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[873] See Chapters 3 and 4 for a more detailed discussion.

[874] Joubert 'Boekskuldfinansiering' 110-112; Joubert *Kredietfaktorering* 68. For a further discussion of Joubert's views see Chapter 4.

[875] Scott 'Sessie' 36. She also questions the importance of the role that factoring plays in South Africa, since Joubert had previously mentioned that factoring is not that well known in South Africa. It must be borne in mind that Joubert's statement and Scott's comment were made 24 years and 22 years ago, respectively. As illustrated by the factoring turnover statistics mentioned above, factoring has developed in leaps and bounds in South Africa and such statements no longer hold true.

[876] Scott 'Sessie' 32, 37; Scott *Cession* op cit 265. See also Chapter 4 for a more detailed discussion of Scott's views.

[877] Scott 'Sessie' 32.

[878] Scott 'Sessie' 32 and footnote 134, 36-37.

The fact that *pacta de non cedendo* in general, and *pacta de non cedendo* appearing in book debts, find themselves in a precarious position, places a huge strain on the future growth potential of factoring as a powerhouse industry. Is a factoring house expected to scrutinise each and every contract related to each and every book debt to determine if some book debts are subject to a *pactum de non cedendo*?

Notwithstanding the fact that the search for *pacta de non cedendo* would be a cumbersome task, it could be accomplished, but at what cost?

It can be argued that the factoring house could employ a team of permanent staff whose only job would be to inspect the contracts concluded between its clients and its clients' debtors to determine which book debts were able to be ceded and which were not. In my opinion, this extra step in the procedure would be time consuming and would result in a delay in the speedy obtaining of finance. Book debt financing may eventually lose its lustre of being a quick fix.

Not only would this proposed inspection result in a delay in obtaining finance, but the client would ultimately have to carry the cost of the factoring house employing extra staff to do a job that may be seen as unnecessary. The charges and fees of factoring would increase and consequently, factoring would become a more expensive method of obtaining finance.

Two suggestions of note to remedy this problem are either for the factoring house to obtain the debtors' consent to the cessions which are hindered by *pacta de non cedendo*; or for the factoring house to indemnify the debtors against the risk of making double payments and to offer indemnification in the case of additional bookkeeping expenses.[879]

[879] Scott *Cession* op cit 267.

These suggestions, however, are not practical since they also translate into extra time and costs for the factoring houses, and that will eventually have a negative impact on its clients, who depend on this industry to function as quickly as possible and as inexpensively as possible. Obtaining a debtor's consent would take just as long as an inspection if not longer, and the factoring house would still have to inspect each contract. Indemnification would be the more time effective option, but would obviously not be cost effective and the client would ultimately have to bear the extra expense.

5.5.2 American law

The problems that *pacta de non cedendo* create in South Africa law are not a concern in America due to the introduction of the Uniform Commercial Code (UCC) which deals with commercial law in general. Article 9 of the UCC governs the legal principles concerning security interests in personal property.

A book debt or an 'account receivable', being the more popular term in America, is personal property as it is an asset in the estate of the creditor. It is also a security interest as it can be used as collateral or security should the creditor be required to offer collateral in any kind of transaction.

In its application article 9 also includes outright sales of accounts receivable (the typical factoring contract) and sales of contractual rights as though they were transfers of security interests.[880]

Article 9, therefore, regulates the assignment of accounts receivable, provided that the transaction falls within the definition of 'account' in article 9-102(2).[881]

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[880] Malcolm op cit 453 where even though the different transactions embody different legal concepts, the functions of the transactions are of primary importance. Since security transfers and outright transfers are similar, they are treated exactly the same.

If the assignment falls within this definition, then article 9-406(d) renders any prohibition on the assignment of an account receivable invalid and ineffective.

Accordingly, no matter how clearly an anti-assignment clause is phrased in a factoring contract falling within the ambit of article 9, it will be rendered ineffective. It has been said that the American legislators have drafted article 9 in this manner as a 'modern credit economy' requires contractual rights to be freely assignable in order to function properly.[882]

Article 9 was considered in great detail in Chapter 2. My opinion that article 9 serves its purpose well will, however, be re-iterated. If factoring houses are to be in existence to offer needy businesses quick finance, accounts receivable have to be freely assignable, and it would be ludicrous to impede or to refuse to improve the very mechanism that drives this industry.

[881] See Chapter 2 for a more detailed discussion.

[882] JE Murray *Corbin on Contracts* revised ed vol 9 (2007) 491.

5.6 Conclusion

This Chapter has compared the law governing a *pactum de non cedendo* appearing in specific contracts in South Africa with the law governing an anti-assignment clause appearing in specific contracts in America.

The purpose of this comparison, as already mentioned, was to determine if a possible solution could be found to alleviate the problems experienced in the South African law of *pacta de non cedendo*.

This comparative examination revealed two points of interest. First, in both American law and South African law slightly different legal principles apply when a prohibition on cession is contained in a specific contract to when such a prohibition is contained in a general contract.

Secondly, and more significantly, the difference in the legal principles between *pacta de non cedendo* contained in general contracts and the legal principles of *pacta de non cedendo* contained in specific contracts, is plainly obvious in South African law. American law, in contrast, has a more consistent approach, albeit not entirely uniform.

It is these two points, but especially the second, that have motivated the proposed solution discussed in the next Chapter.

CHAPTER SIX

PROPOSED SOLUTION

American law is not perfect in every respect – no legal system is, but I am of the opinion that South African law can look to American law for inspiration. My proposed solution is to take the general manner in which American law approaches *pacta de non cedendo* and to apply it to South African law in a manner that would be sensible in a South African context, considering at all times current trends and future commercial realities.

I propose to divide the law of *pacta de non cedendo* into two broad categories as it is done in America: Contracts of a general nature and contracts of a commercial nature.

6.1 General contracts

Both anti-assignment clauses in America and *pacta de non cedendo* in South Africa experience inconsistencies and uncertainties when they appear in a contract of a general nature. These grey areas are undoubtedly more prevalent in South African law.

Further, as can be seen from the comparative examination in the previous Chapter, slightly different principles are applied when prohibitions on cession appear in specific contracts or in specific areas of the law, for example, in company law or in the law of insolvency. In American law, the approach to anti-assignment clauses contained in specific contracts is more consistent with the approach to anti-assignment clauses contained in general contracts. In South African law the difference in applicable legal principles is much more distinct.

This creates unnecessary complications. Is one set of legal principles that experiences inconsistencies and uncertainties not challenging enough?

Why should a slightly different set of rules (with its own shortcomings) apply when a *pactum de non cedendo* appears in a contract of specific application?

Some of these shortcomings were considered in Chapter 5, for example, whether or not a particular party, who is acting *nomino officio*, like a trustee of an insolvent estate or a deputy-sheriff of the court, is bound by a *pactum de non cedendo*. Why should the rules afford a party more or less rights depending upon the capacity in which he acts? Another shortcoming can be seen in insurance law when an insurance policy is ceded *in securitatem debiti,* as it is still largely unclear whether the pledge construction or the *pactum fiduciae* construction is to apply. Also, in negotiable instruments it is uncertain whether the rights under a negotiable instrument marked 'not transferable' can still be ceded. Further, in company law, it seems as though the interest requirement has been abandoned altogether.

Would it not be simpler and more logical if the rules were all the same? Judging from the comparative examination of anti-assignment clauses in Chapter 5, it appears that an attempt is made in America to apply a uniform approach to all prohibitions on assignment whether contained in general or specific contracts.

This attempt has been successful in some areas, for example, in the law of negotiable instruments, where article 3 of the Uniform Commercial Code finds application if a negotiable instrument is negotiated. If a negotiable instrument is assigned, the Restatement of Contracts applies.[883] Also, in the law of bankruptcy the trustee is considered to be in the same position as that of the creditor (the debtor of the bankrupt estate) as the creditor's

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[883] FM Hart and WF Willier *Negotiable Instruments Under the Uniform Commercial Code* vol 2 (2007) part 3-8: 'If a negotiable instrument is assigned, Article 3 of the Code generally has little application to the transfer'. See also Chapter 5.

assets are still fully subject to their 'nonbankruptcy attributes'.[884] Thus, the Restatement of Contracts would find application. I, therefore, suggest that in South Africa the law governing the areas of general and specific application should be standardised.

It should not make a fundamental difference if the subject-matter of the prohibited cession varies. If the rights under an insurance policy, for example, are prohibited from being ceded, or if shares are prohibited from being ceded, why should different rules apply? All *pacta de non cedendo*, whether appearing in general or specific contracts, should be dealt with in the same manner – as *pacta de non cedendo* of a general nature.

As will be discussed below, the only exception to the standardisation of *pacta de non cedendo* should be when they appear in commercial contracts, that is, factoring contracts. Allowance has been made for this exception for the purpose of enabling South African law to keep abreast with current trends and commercial realities.[885]

6.1.1 Validity

I propose that *pacta de non cedendo* be valid and binding automatically, without an interest first being proven to exist.[886] My reasons are as follows:

First, the interest requirement serves no purpose in light of my proposed solution as a whole. Under the current position, if the *pactum de non cedendo* is valid, the right to claim performance from the debtor, which is an asset in the creditor's estate, is rendered non-transferable. Thus, the debtor must show that he has a clear interest in the prohibition before the

[884] TH Jackson *The Logic and Limits of Bankruptcy law* (1986) 104. See also Chapter 5.

[885] See Chapter 5 where the benefits and the annual financial turnover of this powerhouse industry were mentioned.

[886] See Chapter 4 for a general discussion of the interest requirement.

creditor is deprived of the freedom to administer his estate as he sees fit (which is a rather drastic consequence for any creditor to bear). If, however, the *pactum de non cedendo* does not render the right non-transferable, as is my suggestion, the effect is not so far-reaching and the need for the interest requirement can fall away.

Secondly, the interest requirement is not a requirement for the validity of other contractual terms. Why is the *pactum de non cedendo* so significant as to warrant the extra requirement? Other contractual terms depriving contractants of more than merely the right to cede are valid without an interest requirement first having been met, for example, agreeing to cede the right to inheritance[887] or a legacy,[888] ceding the right to prospect[889] and ceding a right of pre-emption.[890]

Thirdly, in keeping with the principle of freedom of contract, if the parties agree to prohibit cession, why should the debtor have the extra encumbrance of showing that the prohibition is in his interest?

Fourthly, there is no historical basis upon which the interest requirement can be founded. The court in *Paiges v Van Ryn Gold Mine Estates Ltd*[891] relied on Sande and Voet as authority, but as discussed in Chapter 4, these two old authorities were in all likelihood not writing about *pacta de non cedendo*, but rather *pacta de non aliendo*.

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[887] S Scott *The law of Cession* 2ed (1991) 169; *Moodley v Moodley* 1953 (3) SA 860 (N); *Weiner NO v The Master* 1976 (2) SA 830 (T); *Rein NO v Fleischer NO* 1984 (4) SA 863 (A).

[888] Scott op cit 169; *Nel v Nel* 1912 EDL 435.

[889] Scott op cit 168; *Cullinan v Pistorius* 1903 ORC 33; *Henderson v Hanekom* 1903 20 SC 513.

[890] Scott op cit 169; *Van der Hoven v Cutting* 1903 TS 299; *Hersch v Nel* 1948 (3) SA 686 (A).

[891] 1920 AD 600.

Fifthly, since I base my proposed solution on the general manner in which American law deals with agreements prohibiting cession, where no such requirement exists,[892] it is consequently out of place.

Lastly, it should not make a difference if the *pactum de non cedendo* was inserted into the agreement creating the right or whether it was super-imposed onto an already existing agreement. Although I acknowledge that the *pactum de non cedendo* can take either of these constructions, it should have no impact on the validity or effect.

6.1.2 Effect

In Chapter 2 it was discussed that American law follows what they call the 'modern approach'. If the power to assign has been extinguished, the personal right is rendered non-transferable. If only the right to assign has been prohibited then it is still possible for the personal right to be transferred, but an action for damages arises in favour of the debtor for breach of contract. In American law, the debate surrounds the interpretation of the modern approach. Three different judicial interpretative approaches exist. Could the modern approach and one of these interpretations perhaps be a viable solution in South Africa?

- The *Allhusen* or *Rumbin v Utica* minority interpretative approach[893] requires only general terms to extinguish the power to assign, provided the general terms are plain, clear and unambiguous.

  This approach has the benefit of being flexible and giving effect to freedom of contract as parties are given the scope to use their own language to express their intentions. Thus, the main advantage of this approach is that it does not scrutinise the specific words used by the parties (like the magic words approach).

[892] The interest requirement also does not feature in the English law for that matter.

[893] See Chapter 2.

The fatal flaw, as pointed out in Chapter 2, is that if the parties only employ general language to extinguish the power to assign, how much more general should their language be, or how should their intentions be couched only to restrict the right to assign?

In my opinion, to differentiate between a general intention where the power to assign is extinguished and an even-more-general intention where only the right to assign is prohibited, the contract language will inevitably be scrutinised.

From a South African law perspective, objection can be raised to the somewhat confusing distinction between a general and even-more-general intention. Further, it places a wide discretion in the hands of the court in deciding the parties' intentions. This interpretative approach is certainly not ideal.

- The so-called 'magic words' approach requires certain words (the magic words), for example, 'void', 'invalid' or 'ineffective', to render the personal right non-transferable, otherwise an assignment in contravention results only in damages for breach of contract.[894]

  As a solution in South Africa, this interpretative approach would practically result in compelling contractants to use certain words, almost like Roman lawyers did with their *stipulatio*. It is, however, much simpler than the *Allhusen* or *Rumbin v Utica* minority approach and basic to use, for example, 'an assignment in contravention of the anti-assignment clause shall be void'. Another benefit is that it limits the amount of discretion that a court may exercise.

[894] See Chapter 2.

Whether it will be successful in South Africa is debatable. Ignorant parties may not only be unable to use the magic words to their advantage, but may actually be in a worse position by using them incorrectly.

The South African law of contract requires consensus *ad idem* for a contract to be valid and enforceable. If it can be shown that the written contract does not reflect the consensus reached by the parties, then a court will generally not give effect to the written contract.[895] In such a situation what would our courts do? It may be difficult, if not impossible, to determine if (oral) consensus was reached with or without magic words.

It would also be impossible for a court to determine the existence of magic words if the agreement was an oral one *ab initio* and not reduced to writing. In our law an orally concluded contract is perfectly valid. If the magic words approach were to be adopted it would force contractants to conclude written agreements, since without a document evidencing the use of magic words, or a stipulation of whether a duty is created or a power is relinquished, the intentions of the parties would be difficult to ascertain.

- The Illinois approach[896] improves on the above two approaches in the sense that it is not so heavily reliant on words. According to this

[895] *Khan v African Life Assurance Society Ltd* 1932 (WLD) 160 167: 'In contracts regard must be rather to the truth of the matter (*rei veritas*) than to what has been written…for there may be mistake in the writing… the Romans did not allow the true agreement between the parties to be prejudiced by a slip of the pen or other inaccurate expression.' See S Van der Merwe et al *Contract General Principles* 2ed (2003) where it is explained that this general principle must, however, be read against the possibility that a contract in South African law may be upheld on the ground of reasonable reliance. This can occur when, although the contractants were not *ad idem*, a contractant can show that he reasonably relied on the belief that consensus had been reached (35-36). This general principle must also be read against the possibility that, although consensus was not reached, the contract may still be upheld if a contractant can prove that the contract contains an *iniustus error* or inexcusable mistake (38 *et seq*). South African courts will also generally uphold a written contract where the parties agree to rectify the document to express their true intentions (162-163 *et seq*).

[896] See Chapter 2.

approach, all the surrounding circumstances and factors need to be taken into account when determining whether or not the power to assign has been extinguished.

From a South African law perspective, this interpretative approach is the best of the three approaches, but is not quite the ideal solution as it still contains the uncertainty of a court-finding: A court may decide that the effect of a contravention lies either in damages for breach of contract or that the right is non-transferable.

The reason that a court has the option to make either of these decisions is because this approach (and the *Allhusen* or *Rumbin v Utica* minority approach) gives the contractants the freedom to deviate from the default position, being that of damages for breach of contract.[897]

In my opinion there should be no scope for deviation. The effect of contravention should be the same in every case with the only question before the court being whether the anti-assignment clause or *pactum de non cedendo* was indeed contravened in light of the specific facts of a particular case.

My view, therefore, is that inspiration can be sought from the default position of the modern approach applied in American law in so far as the effect of a cession in spite of a *pactum de non cedendo* is concerned – that is – it should give rise to damages for breach of contract in every case. This, however, necessitates a rejection of the modern approach as whole, along with the three possible interpretative alternatives.

The debtor may argue that damages is not a satisfactory remedy and that the right should rather be rendered non-transferable. If one, however,

[897] As set out in the Restatement of Contracts where s332(2)(b) states that if a contract prohibits the assignment of rights and a contracting party assigns the rights regardless of the prohibition, then, unless a different intention is manifested, the debtor is entitled to damages for breach of the contract, but the breach does not render the assignment ineffective.

considers the debtor's reasons for insisting on including a *pactum de non cedendo* in a contract, it makes no logical sense why a prohibition on cession should be treated differently to any other ordinary contractual term where an action for damages would suffice in the case of a breach. Why *must* the right be rendered non-transferable?

As already mentioned, the possible reasons that a debtor may insist on a *pactum de non cedendo* are:

g) he fears double payment of the debt (if notice is missed);
h) he may be prevented from using set-off against the creditor;
i) he is familiar with the creditor;
j) he is of the belief that the creditor may be more willing to grant time extensions;
k) he is of the belief that the creditor may be more willing to overlook some indebtedness;
l) a change in creditor may be generally inconvenient.

None of these reasons are so severe that the debtor would be unconscionably prejudiced should the effect of a cession in contravention of a *pactum de non cedendo* result in damages for breach of contract as opposed to non-transferability of the right.

Damages as the effect of a cession in contravention of the *pactum de non cedendo* do, however, raise one red flag: Quantification. If one considers the list above, what patrimonial harm or loss could the debtor possibly suffer by the creditor ceding the right contrary to a *pactum de non cedendo*? In South African law the general rule is that damages cannot be recovered for loss which is non-patrimonial.[898]

[898] Van der Merwe et al op cit 389; RH Christie *The Law of Contract in South Africa* 5ed 2006 546-547 where Christie states that the plaintiff must prove his damages and if none can be proven, damages will not be awarded. It is also stated that contractual damages are strictly confined to patrimonial loss and are not extended to any form of intangible loss.; AJ Kerr *The Principles of The Law of Contract* 5ed (1998) 646, 679 where the author explains that it is insufficient for the plaintiff to show that the contract has been

Of course, it is not being suggested that the debtor be left with a right to claim damages, while being pointed out that this right is practically empty. The 'damages' that I am referring to are 'damages' that can be attained through the use of a penalty clause.

If a debtor can insist on a *pactum de non cedendo* for his protection, he can similarly insist on a penalty clause, which would function in his favour should the *pactum de non cedendo* be contravened.

A penalty clause is a clause or stipulation in a contract stating that in the event of the contract being breached, the offending contractant will pay a sum of money or render a certain performance to the other contractant.[899] The advantages of the penalty clause to the debtor are that he may claim the penalty (a sum of money) without proving that he has suffered damages and the penalty clause is wide enough to include non-patrimonial damages.[900] If the right is ceded contrary to the *pactum de non cedendo*, the debtor will have to perform to the cessionary, but at least he will have a sum of money to ease the inconvenience he may suffer, if any.

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breached, and that to merit an award of damages, loss of a patrimonial nature must also have been suffered. This loss cannot be one of inconvenience or the like, but must be of an economic nature.

[899] Van der Merwe et al 412. Penalty clauses are governed by the Conventional Penalties Act 15 of 1962. The definition of a penalty clause in s1 reads as follows: 'Any person shall, in respect of an act or omission in conflict with a contractual obligation, be liable to pay a sum of money or to deliver or to perform anything for the benefit of any other person…either by way of penalty or as liquidated damages'. I am hard pressed to think of a situation where the debtor would not prefer monetary compensation, but something else instead, yet it is quite possible for the parties to agree to any other type of performance (for example the rendering of a service). This performance also need not be made to the debtor himself, but can be made to any person. See also Christie op cit 560: 'At the time of contracting it is not uncommon for the parties to include a term in their contract binding the one party to pay a fixed sum of money or return the property and forfeit all instalments paid or due, or something similar, in the event of committing a specified breach or perhaps any breach of the contract'. See also Kerr op cit 685-690.

[900] Van der Merwe et al 412.

The advantage of the penalty clause to the creditor is that the clause provides certainty as to the monetary amount to which he would be held liable should he breach the contract. This, I am sure, will cause the creditor to ponder a little longer before ceding at a whim. The creditor will have to weigh up breaching the contract and paying the penalty to the debtor against the possible gains of ceding the right to the cessionary. This may dissuade him from breaching the contract. Alternatively, the creditor may breach the contract, but be quite content to pay the penalty if the gain from ceding the right outweighs the consequences of breaching the contract (also an advantage to the debtor).

Not only do penalty clauses provide the abovementioned advantages, but they also operate in a fair manner (another advantage for both parties):

Section 3 of the Conventional Penalties Act, the legislation governing penalty clauses, states that a court may reduce the penalty if it seems to be out of proportion to the prejudice suffered by the debtor due to the breach of the contract.[901]

Section 1 of the Act does not restrict the penalty to one sounding in money, but allows the parties to agree to any other type of performance as a penalty if this is what they would rather prefer. This alternative performance may also be rendered to a party other than the debtor himself.

I am of the opinion that, should this suggestion be applied to *pacta de non cedendo* in South African law, it would not only be in keeping with

[901] Van der Merwe et al 416-417. The court will reduce the penalty to that which is reasonable in the circumstance considering every interest which may be affected by the breach, for example, proprietary interests, sentimental interests, convenience and reputation. The onus, however, rests on the creditor to prove that the penalty is *prima facie* out of proportion to the prejudice suffered by the debtor. Should the creditor succeed in proving this, the debtor has the opportunity to rebut the allegations. See also Christie op cit 563-564 and Kerr op cit 690-694.

international trends, but it would bring about a much needed balance in this area of the law of cession:

- Creditors could now dispose of their rights (which are assets in their estates), whereas the current position renders rights subject to *pacta de non cedendo* non-transferable.

  Of course, if a creditor has agreed that he will not cede a right and breaches this agreement, he should not be allowed to escape liability just because the right is an asset in his estate. Agreements must be honoured and a breach must bring about some consequence for him to bear and a penalty clause would achieve this. Albeit the creditor cedes on pain of monetary compensation arising from a penalty clause, he must be able to cede his rights should he wish to do so.

- The debtor could now rely on the *pactum de non cedendo* as being automatically valid and binding, whereas under the current position he must have an interest in the prohibition for it to be valid. Although the right in the creditor's estate would not be rendered non-transferable, the debtor would still be protected in the case of a cession in contravention of a *pactum de non cedendo* by monetary compensation arising from a penalty clause which would function as damages.

I think that it is possible for these improvements to be made within a judicial decision. The meeting of a suitable set of facts with a willing and capable judge may, on the other hand, be wishful thinking.[902]

6.2 Commercial contracts

[902] I say this because South African judges are so reluctant to depart from previously decided cases, although Thring J delivered a surprisingly bold judgment in *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd* 2008 (4) SA 510 (C), see Chapters 3 and 5.

The following suggestion will certainly bring about a drastic change in South African law, but a change that I believe is long overdue. It is also a suggestion that will bring our highly outdated legal principles up to date with modern worldwide commercial trends.

I propose that South African law take a lesson from American law and render *pacta de non cedendo* invalid and unenforceable when appearing in book debts for the purpose of book debt financing or factoring as illustrated by article 9 of the Uniform Commercial Code (UCC).

I think that many small to medium businesses in South Africa are missing out on huge growth and finance opportunities which could, in turn, boost the general economy. If we changed our laws to implement this new system, we could also influence and encourage our neighbouring countries to do the same, thereby uplifting the businesses and economies in Africa as a whole.

In Chapter 4 three international instruments were briefly discussed: The UNIDROIT Factoring Convention of 1988, which covers the assignment of receivables in a factoring contract; the UNCITRAL Convention on the Assignment of Receivables in International Trade of 2001, which covers assignments of international receivables; and the UNIDROIT Principles of International Commercial Contracts of 2004 (PICC). The instrument applying only in Europe, Principles of European Contract Law (PECL) of 2003, was also discussed.

Although none of these instruments support the solution that I propose, they all consider the cession of receivables or book debts in general and suggest ways to unify the principles across nations to allow for international factoring. These general principles can be used as a guide for South African law to implement its own set of rules so that they may be in line with international tendencies.

To be in accordance with my suggestion, however, preference should be given to article 9 of the UCC, as the Code renders *pacta de non cedendo* appearing applicable to factoring contracts automatically invalid, notwithstanding any provision in the contract between the debtor and the creditor which may indicate otherwise. The instruments mentioned above, however, regard *pacta de non cedendo* as valid and deem a cession in contravention thereof as giving the debtor a claim for damages for breach of contract.

I make this suggestion for all the reasons and benefits as discussed in Chapter 5. It appears that English academics, whose law on the issue is more similar to the South African position than to the American approach, also share my view.

While complaining bitterly about the approach in the English law, but without suggesting any kind of radical revamp, Goode[903] and Munday[904] both enviously examine the liberal approach in America.[905]

A more outspoken Allcock also favours the idea that book debts should be freely transferable. He is of the opinion that the difficulties (if any) that it would cause the debtor would not outweigh the commercial desirability of freely assignable debts.[906] He concludes his article with an expression of anticipation for the legislature in England to enact legislation similar to that in America 'making all debts assignable regardless of any restriction'.[907]

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[903] RM Goode 'Inalienable rights?' 1979 *Modern Law Review* (vol 42) 553.

[904] RJC Munday 'Prohibition against assignment of choses in action' 1979 *Cambridge Law Journal* (vol 38) 50.

[905] See Chapter 2 for a more detailed discussion.

[906] B Allcock 'Restrictions on the assignment of contractual rights' 1983 *Cambridge Law Journal* (vol 42) 328 345. See Chapter 2

[907] Allcock op cit 346.

Salinger is another English academic who shares the view that the economy in the United Kingdom would be much better served if the legislature implemented a system similar to that in America.[908]

Joubert, a South African authority on the issue, states that it was not surprising that article 9 of the UCC renders *pacta de non cedendo* invalid when applicable to factoring contracts.[909] He went on to recommend that the position be the same in South Africa.[910]

This suggestion was made in 1985 and was very insightful since factoring was not yet that well known in South Africa. How much more relevant and necessary is this suggestion 24 years later, when factoring has become a powerhouse industry in South Africa generating thousands of millions of US dollars?

Malcolm, an American academic, writing about book debt financing under the UCC, has only praise for article 9 and remarks that:

> …the UCC provides maximum simplicity and effectiveness for accounts receivable financing in the United States but at the same time is basically fair to all interested parties. It is excellent legislation.[911]

Further, as Murray (an American academic) points out, article 9 has stirred little, if any, litigation, considering that it limits a debtor's freedom of contract. Disputes rather involve matters of interpretation, that is, whether

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[908] FR Salinger 'Factoring: Are the true benefits still to come?' *The Company Lawyer* 1981 (vol 2) 243 247.

[909] N Joubert *Die Regsbetrekking by Kredietfaktorering* (1985) LLD Thesis Randse Afrikaanse Universiteit 468. Joubert is without a doubt the leading authority on factoring in South Africa and has written much on the topic. See Chapter 5.

[910] Joubert op cit 468. His reason was that if it were not so it would be against public policy. See Chapter 5. His reasoning is not exactly the same as mine, but the end result nonetheless is – although perhaps today, 24 years later, he may agree with me.

[911] WD Malcolm 'Accounts receivable financing under the uniform commercial code' 1966 *Rabels Zeitschrift für ausländisches und internationales Privatrecht* (vol 30) 434 458.

an assignment of a debt falls under the definition of 'account' as stipulated in article 9 of the UCC.[912]

If such an approach were to apply in South African law, when a dispute arises, a court need only apply the definition of 'account', while keeping the overall purpose and function of book debt financing in mind at all times, and it should readily be clear whether a certain cession of a debt falls under the definition or not. Should the court encounter an unusually complicated case, nothing would prevent it from looking to American case law for assistance.

For this solution to find practical application, legislation must be enacted. Radical reform of this nature is not a task that our courts have the power to carry out. Hopefully, the legislature will have the wisdom to codify this area of the law of cession.

[912] JE Murray *Corbin on Contracts* revised ed vol 9 (2007) 219. See Chapter 2.

CONCLUSION

After an examination of the relevant case law, it becomes clear that many of the principles governing *pacta de non cedendo* are uncertain. Rather than clarifying and improving the position, some judgments have had the opposite effect.[913]

The leading case, *Paiges*, is open to criticism on the ground that the historical foundation upon which it was based is incorrect. It was pointed out in an earlier Chapter that Sande and Voet, the old authorities heavily relied on by the court in *Paiges*, were in all likelihood referring in their writings to restraints on the alienation of corporeal things and not restraints on the alienation of incorporeal things.

It therefore follows that the historical development of the *pactum de non cedendo* as recounted in Chapter 1 is not entirely correct, as part of what was discussed in Chapter 1 is actually the historical development of the *pactum de non aliendo* or restraints on the alienation of corporeal things. Since there is no record (to my knowledge) documenting the historical development of the *pactum de non cedendo*, the historical development would be open to speculation.

Further, not only did the court in *Paiges* apply the incorrect legal principles, but the court did not apply them consistently. The court followed Sande and Voet in determining the validity of *pacta de non cedendo*, but followed German jurists when determining the effect.

[913] For example, *Italtrafo SpA v Electricity Supply Commission* 1978 (2) SA 705 (W) and *Vawda v Vawda and others* 1980 (2) SA (TPD) 341 where the courts cast doubt on the interest requirement by potentially creating a new standard being that of a 'material and reasonable' interest. Another example can be found in *MTK Saagmeule (Pty) Ltd v Killyman Estates (Pty) Ltd* 1980 (3) SA 1 (A) where the Appellate Division appears to have laid down another ground for invalidity on the basis of non-compliance with a contractual formality.

From the discussion of the cases, it can be seen that no court has expressly identified these mistakes or attempted to correct them, albeit the Appeal Court has had the opportunity to do so on many occasions.

This state of affairs is certainly unsatisfactory and academics have accordingly developed their own views of the rules governing *pacta de non cedendo*, which are not necessarily in line with the courts' views.

The court in *Paiges* mentioned only a *pactum de non cedendo* that is inserted at the time when the agreement creating the personal right is concluded. If the *pactum de non cedendo* is formed in this manner, most academics are of the opinion that since the personal right is intransmissible *ab initio*, the debtor need not show that he has an interest in the prohibition, thus deviating from the interest requirement laid down in *Paiges*.[914]

Further, most academics also recognise a second form of *pactum de non cedendo*. This form occurs when the *pactum de non cedendo* is super-imposed on an already existing contract. For this form of *pactum de non cedendo* to be valid, the debtor must show that he has an interest in the prohibition. Although the interest requirement still survives the second construction, this construction was unknown to the court *Paiges*.

Notwithstanding the fact that the interest requirement has survived the second construction, it has been vehemently criticised from two opposing points of view. On the one hand some academics argue that the interest requirement deprives parties of their freedom of contract as the debtor has to show that he has an interest in the prohibition for it to be valid, even

[914] This view may be supported by *Trust Bank of Africa v Standard Bank of South Africa Ltd* 1968 (3) SA 166 (A) which was confirmed in *Italtrafo SpA v Electricity Supply Commission* 1978 (2) SA 705 (W) and in the recent case of *Capespan (Pty) Ltd v Any Name 451 (Pty) Ltd* 2008 (4) SA 510 (C).

though the parties intend to bring a *pactum de non cedendo* into existence.[915]

On the other hand, other academics are of the opinion that the interest requirement does not go far to limit freedom of contract because the concept is vague and has no real meaning, and seen from that perspective, the debtor would always be able to show that he has an interest.[916] I have agreed with this school of thought.

Yet other academics have approached the issue by attempting to judge the *pactum de non cedendo* against the idea of unlawfulness and public policy by using a restraint of trade clause as an analogy;[917] or by judging *pacta de non cedendo* against public policy in general.[918] Both of these alternative arguments were, however, found to be unworkable.

Considering that the legal principles governing *pacta de non cedendo* were based on an incorrect historical foundation, does it follow that all the legal principles that have developed from *Paiges*, like the interest requirement, the two possible constructions of the *pactum de non cedendo*, the supposed limitation on the freedom of contract, and the alternative arguments, as well as the various submissions by other academics, are of no relevance and applicability to the *pactum de non cedendo*?

Unfortunately, the principles laid down in *Paiges* and all that has developed thereafter is relevant as it is the applicable law as it presently

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[915] See GF Lubbe and CM Murray *Farlam & Hathaway: Contract Cases, Material and Commentary* 3ed (1988) 655; SR Roussouw 'Pacta de non cedendo' 1991 *Responsa Meridiana* 54-55.

[916] Welsh 'General principles of contract' 1950 *Annual Survey* 81 82; JC De Wet and AH Van Wyk *Kontraktereg* 4ed (1993) 254 footnote 16; S Scott 'Italtrafo SpA v Electricity Supply Commission 1978 (2) SA 705 (W)' 1978 *Tydskrif vir Hendendaagse Romeins-Hollandse Reg* 334; S Scott *The Law of Cession* 2ed (1991) 206.

[917] N Joubert *Die Regsbetrekking by Kredietfaktorering* (1985) LLD Thesis Randse Afrikaanse Universiteit 464 *et seq*; N Joubert 1986 'Boekskuldfinansiering en pacta de non cedendo' *Modern Business* 110.

[918] Roussouw op cit 54.

stands. Despite being based on a flawed foundation, the *Paiges* judgment was nonetheless handed down by the Appellate Division and the Appeal Court has not since made any amendment.

I was of the opinion that a solution is not to be found in any of the submissions made by our academics. The approach adopted by *Paiges* and the courts that follow is equally unsatisfactory. The whole concept of agreements prohibiting cession has been re-evaluated and I have made a suggestion in this regard preferring a law of property approach.

I proposed to divide the law of *pacta de non cedendo* into two broad categories as done in America: Contracts of a general nature and contracts of a commercial nature.

- As to contracts of a general nature: Whether appearing in a general or a specific contract, the *pactum de non cedendo* should be standardised and governed by the same principles. I proposed that these principles should deem *pacta de non cedendo* valid with the interest requirement being done away with. The construction that the *pactum de non cedendo* takes should have no impact on its validity or effect. Further, if the personal right is ceded contrary to the *pactum de non cedendo*, the debtor should be able to claim monetary compensation through a penalty clause that should be attached as a standard clause to all *pacta de non cedendo* agreements, as quantification would cause difficulties if damages were to be claimed.

  This change, to be brought about in a judicial decision, would not only be in keeping with international trends, but it would bring about a much needed balance in this area of the law of cession.

- As to contracts of a commercial nature: I proposed that when a *pactum de non cedendo* is contained in a commercial contract –

that is – a factoring contract (book debt financing), the *pactum de non cedendo* should be automatically invalid despite any agreement between the debtor and the creditor to the contrary. This follows the general approach of article 9 of the Uniform Commercial Code in America.

The purpose for this suggestion was because factoring has grown into a powerhouse industry generating thousands of millions of US dollars. The factoring industry not only boosts the general economy, but comes to the financial aid of small to medium business as well as providing debt collecting and other services.[919] *Pacta de non cedendo* are thus hindrances to the smooth functioning of the factoring industry. For this radical change to be effected I was of the opinion that legislation is called for.

Hopefully this re-evaluation of the *pactum de non cedendo* will re-capture the attention of academics and judges alike, so that those in the position to do so, will carefully re-consider its validity and effect.

[919] Http://en.wikipedia.org/wiki/Factoring_(finance) (accessed on 17 April 2009); S Scott 'Claim enforcement (debt collection)' 2002 *SA Mercantile Law Journal* (vol 14) 491.

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