

# The balance between the principle of pacta sunt servanda and section 22 of the Constitution in a restraint of trade agreement

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## ABSTRACT AND KEY WORDS/PHRASES

### 1. Abstract

The focus of this discussion is whether there is still the need to enforce the restraint of trade agreements in their pre-Constitutional form. The dawn of the constitutional era has necessitated a re-examination of common law with a view to establishing whether the balance created by the latter (regarding this field) still exists.

The Bill of Rights has obviously raised some doubts regarding the equilibrium desired between employer and employee interests. Section 22 of the Constitution is to the effect that everyone must be free to secure employment (as a fundamental right), whereas the common law restraint of trade agreements impose some bars to the operation of the said right.

It is common course that the Constitution is more superior to common law, what remains a debateable issue is whether there are any reasonable limits that must be considered to justify the disregard of the Constitution. Serious arguments around the direct and indirect application of the Bill of Rights still persist and failure to resolve them would have the effect of excluding or weakening the application of the Bill to disputes arising in this field.

In common law the enforcement of restraint agreements is *sine qua non* for the greater good of protecting the sanctity of contracts. Contractual obligations must be fulfilled unless it would be unreasonable to enforce same.

The question of the *onus* to prove unreasonableness, which lies with the employee, turns to place an onerous burden on the employee. This coupled with the employee's weaker bargaining power raises doubts as to whether the employee is in a better position to conclude a restraint of trade agreement. Common law does not consider or accommodate this concern in that its main object is the fulfilment of the agreement.

It is believed that the Constitution has ushered in a new approach which focuses mainly on the fairness of the agreement itself. The enforcement of the agreement must pass the constitutional muster built in section 22 in order to ensure

that there is equilibrium between the employer (the *restrainer*) and employee (the *restraineed*) interests.

In the end this discussion explores whether it is justifiable to subject the Right to work (as provided by the Constitution) to the common law restraint which is opposed to the constitutional right. The circumstances under which the exclusion of section 22 is condonable are interrogated within the framework of conflicting case law.

## 2. Key words/phrases

- a. *Pacta sunt servanda*
- b. Restraint of trade agreements
- c. Section 22 of the Constitution of South Africa
- d. Direct and indirect application of the Bill of Rights
- e. Unequal bargaining power of the parties
- f. The role of public policy in dispute resolution
- g. Horizontal and vertical application
- h. Limitation of the Bill of Rights
- i. Payment of consideration *in lieu* of restraint
- j. Supremacy of the Constitution to common law

## 1 Introduction

In adjudicating disputes regarding the restraints of trade agreements, the South African courts have departed to an extent from the principle *pacta sunt servanda*, which elevates the sanctity of contracts above any other consideration. In short, our courts' point of departure is that contracts are enforceable. The party that wants to show that a particular contract should not be enforceable must demonstrate why that position should be held against the established common law position.

The courts apply a reasonableness test to determine whether the enforcement of the restraint is in accordance with public policy or contrary thereto. It goes without saying that under the South African approach the onus lies with the employee to convince the court to declare the restraint unreasonable and therefore unenforceable. The employer is left with a lighter burden to prove the existence of the contract and that it is in accordance with public policy that the said contract be enforced.

This position in reality means that the employee's constitutional right to freedom of trade, occupation and profession (section 22), is relegated to the background until the employee proves that this right outweighs the employer's right to the restraint. In the case of *Esquire System Technology v Cronje*<sup>1</sup> it is stated that "it is against public policy to enforce a covenant which is unreasonable, one which

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1 (2011) 32 ILJ 601 (LC).

unreasonably restricts the covenantor's freedom to trade or work". As seen in the *Esquire* case the employer need only prove that it has a protectable interest which is under threat by the employment of the employee with the competitors. The court will consider if the restraint is not against public policy and if so convinced it will be satisfied that the employee's constitutional right is not jeopardised.

Case law will show that there are many restraint of trade agreements which are not meant to serve the purpose for which they were entered into. Some of the restraints were abandoned when the employer faced reciprocal duties to pay the considerations guaranteed in return. In some instances the restraints were found to be used to destroy competition unfairly.<sup>2</sup>

The question is whether the employee attaches any significance to his constitutional right to freedom of trade, occupation and profession when he signs to accept the restraining agreement. The desperate situation of the employee would make him accept the unacceptable hoping that things will change for the better with the progress of time. The danger posed by hanging the restraint on his neck, like the sword of Damocles, is not immediately visible to him. At that stage the employee is excited that his prayer has just been answered by finding the job. As such, at the conclusion of the agreement, the employer faces no challenge from the employee about the freedom of trade, occupation and profession which is eventually at stake.

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2 *Henred Freuhof v Davel* (2011) 32 ILJ 618 (LC).

Carl Mischke<sup>3</sup> summarises the problem, from the employee's point of view, in the following terms:

The real issues, disputes and disagreement only arise on termination of employment, when an employee suddenly finds his further employment opportunities restricted by a contractual provision he or she did not pay much attention to in the beginning. Another employer may make a very attractive offer, an offer that the employee is contractually precluded from accepting.<sup>4</sup>

It should be understood that at the time when the restraint agreement is being concluded the position of the employee is that of a beggar who cannot choose. It is an agreement by two parties who are far from being equal; the employee being the less equal by virtue of his inferior economic power. The problem arises when the beggar wants to join the opposition, which is normally an agreement where the employer's competitor wishes to infringe on the rights protected by the restraint.

Weighing the sanctity of contracts against the employee's constitutional right is a challenge which merits attention. However, the opposite also needs consideration: To what extent is a breach of the restraint agreement affecting the employer's rights in terms of section 22 of the Constitution?<sup>5</sup> As a result we have to deal with two competing parties vying for protection under the same section of the Constitution. Most importantly there is the question whether there is still balance between the employer and employee parties after the restraint has been effected.

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3 IR Network Weekly Comments August 2008.

4 IR Network Weekly Comments August 2008.

5 *Constitution of the Republic of South Africa*, 1996 (hereafter referred to the *Constitution*).

## 2 Enforcement of restraint agreements in common law

The discussion that follows focuses on the main important factors in the enforcement of restraint of trade agreements. The rules relating to *pacta sunt servanda*, public policy, onus, bargaining power of the parties, as well as the equalising strategy, are dealt with in detail hereunder.

### 2.1 The rule relating to *pacta sunt servanda*

*Pacta sunt servanda* is a common law principle which demands that contracts entered into freely and voluntarily should be fulfilled. Agreements so entered should be respected and obligations thereto should be fulfilled. It is about achieving □simple justice between man and man□.<sup>6</sup>

According to the decision in *Magna Alloys & Research (SA) v Ellis*<sup>7</sup> the restraint agreement was a sacred contract not subject to treatment that other contracts are subjected to. The restraint agreement received special treatment by virtue of its special nature. As a token of veneration for the sanctity of contracts the Appellate Division rejected the English law position which states that restraint of trade agreements are *prima facie* unenforceable and that the party that wished to enforce such must show the reasonableness thereof.<sup>8</sup> The current position in South Africa is that restraint agreements are *prima facie* enforceable and that the

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6 *Sasfin v Beukes* 1989 1 SA 1.

7 1984 4 SA 874 (A).

8 *Magna Alloys & Research (SA) v Ellis* 1984 4 SA 874 (A).

onus lies with the party that wishes to escape enforcement to prove that it is unreasonable and therefore unenforceable.

The position of this principle in common law is best explained by the statements that follow. In *Den Braven v Pillay*<sup>9</sup> Judge Wallis confirms this point:

I know of no developed system of jurisprudence that does not recognise the need ... to enforce contractual obligations. Problems that may arise from the disparate power relationships of the parties are dealt with in a variety of ways and particularly by legislation. However as a general proposition, most societies regard the enforcement of contractual obligations as having a value itself. This is hardly surprising, as recent studies in the field of economics have recognised that economic development is closely linked to the rule of law....<sup>10</sup>

The Court in this case emphasises that the sanctity of contracts is part and parcel of the rule of law. It is further shown that economic development is at the core of strengthening the principle of the sanctity of contractual obligations. The logic here is very simple: Economic development will suffer if there is no certainty regarding fulfilment of contractual obligations. To prevent such the rule of law must prevail by strengthening *pacta sunt servanda*. Respect to the sanctity of contracts (which is respect to the rule of law) will ensure that the economy is not subjected to the whims of court decisions that might favour parties that argue against enforcement of contractual obligations.

The negative implication of this is that individuals who command less economic power, like individual employees, might find themselves being sacrificed for the good of the economy. They will just become cogs in the machinery of production

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9 2008 6 SA 229 (D).

10 2008 6 SA 299 (D) at 33.

and profits. Their human dignity<sup>11</sup> is swallowed up in the quest by big businesses to accumulate as much wealth as possible.

It goes without saying that the courts are expected to play a substantial role to protect small parties against blatantly unfair bargains. Reasonableness must accompany contractual obligations that parties are committed to. The rule of law is also manifested in the balancing acts, normally done to satisfaction by the courts.

## **2.2 The role of public policy**

This is the criterion against which the reasonableness of a restraint agreement or any other contractual term is measured. It is, as case law has demonstrated, a fluid concept which does not lend itself to mathematical precision. In *Reddy v Siemens*<sup>12</sup> the Court held that if the facts show that the restraint is reasonable the employer must succeed, if the facts show that the restraint is unreasonable, the employee will succeed. It concluded that this calls for a value judgment.

Public policy is the sum total of the views of society on a particular aspect. It is not the views of legal scientists or specialists that determine public policy. It is the views or perceptions of ordinary society comprising ordinary people. It reflects the □general sense of justice of the community, the *boni mores*□.

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11 S 10 of the *Constitution*.

12 *Reddy v Siemens Telecommunications* (2007) 28 ILJ 317 (SCA).

It must be noted that by its very nature, public policy changes with the progress of time. Reliance on public policy must therefore be realistically matched with the new developments that necessitate adjustments in the thinking of society and public policy. Failure to adjust with time might bring about a situation where modern times are subjected to the rule of outdated public policy.

It is a sad story that there is resistance to change which is carried on under the pretext of judicial precedent. Court judgments cannot be fashioned to address modern situations based on "the shibboleths of the past".<sup>13</sup> Paradigm shifts must be accommodated so that justice can be achieved without any doubts as to the appropriateness of the tools applied.

It is argued that due to these discrepancies the disputes between employer and employee regarding the restraints agreements cannot be adjudicated to the satisfaction of society. The Magna Alloys decision which happened a decade before the Constitution cannot hold true for the new era. The constitutional values that are so important today, section 39(2) which forces every judge to apply the Constitution, were not there when this decision took place. Therefore there is without a doubt a serious lacuna in this regard and until the Constitutional Court is presented an opportunity to rule on this point, the problem of uncertainty will persist. The discrepancy of public policy in this instance must be fixed to bring about real justice between man and man.

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13 *Mozart Ice Cream Classic Franchises v Davidoff* (2009) 30 ILJ (C) at C.

### **2.3 Onus of proof**

The case of *Magna Alloys*<sup>14</sup> ruled that onus to prove that the restraint agreement is unreasonable and therefore unenforceable lies with the party that wants to escape enforceability. Before then the party that wanted to enforce the restraint agreement bore the onus to prove reasonableness, which position was in line with English law.<sup>15</sup>

The courts have so far not experienced any problems with this position. In *Advtech Resourcing v Kuhn*<sup>16</sup> the court held that the onus lies with the party who wishes to enforce the contract. Some courts begrudgingly refrained from following suit due to the question of *stare decisis* following the *Magna Alloys* decision. Other courts contended that the question of onus does not matter due to the fact that the other party must also adduce the facts that prove its case.

It is submitted that the employer party in a restraint agreement must bear the onus since he seeks to limit a constitutionally guaranteed right (section 22 of the Constitution). For now the employee party's constitutional right does not enjoy priority since *pacta sunt servanda* occupies this position.

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14 *Magna Alloys & Research (SA) v Ellis* 1984 4 SA 874 (A).

15 *Mitchell v Reynolds* (1711) 1 P 181.

16 2008 2 SA 375 (C).

## **2.4 The unequal bargaining power of the parties**

Contracts are required to be concluded by parties with equal power. The parties must be free to negotiate terms without fear. It is still debatable whether in a restraint of trade agreement the employee as a party voluntarily and freely agrees to the terms. As Davis J puts it in *Mozart Ice Cream v Davidoff*:

The fundamental dispute concerns the balance between the bargain, as it is phrased in the contract, and the demands of public policy that give content to the idea of a constitutional community.<sup>17</sup>

The fact that so many cases are referred to court means that the employee was never *ad idem* with the employer at the point of concluding the contract which the employee voluntarily signed.

The question that needs to be addressed is whether it can be assumed that there was consensus between employer and employee at the point of concluding the contract. Since the restraint agreement is *prima facie* enforceable it can be assumed that there was consensus as well because assuming otherwise would mean that there was no contract.<sup>18</sup>

If it is assumed that the agreement was concluded between parties whose bargaining power was not equal, the courts must come to the protection of the weaker party. To understand the position of the weaker party at the conclusion of the contract, the purpose of concluding the contract must be explored. The

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17 *Mozart Ice Cream Classic Franchise v Davidoff* (2009) 30 ILJ 1750 (C) H.

18 Law of Contract: Consensus is one of the requirements for concluding contracts.

question is why would a party commit to a contract which terms are not favourable thereto. It is obvious that employee parties would sacrifice their future freedom in order to secure an employment position at stake. Taking the employer to task so that he can adjust the terms to accommodate the employee's interests is not an option at the point of concluding the contract.

The employee party is faced with a take-it-or-leave-it situation. A standard form contract prepared a long time ago is presented for ratification by the job seeker. The job seeker signs the contract and secures the job whilst at the same time committing to the restraint accompanying the job.

In the *Barkhuizen* case<sup>19</sup> the Supreme Court of Appeal accepted that the constitutional values of equality and dignity may prove to be decisive when the parties' relative bargaining power is an issue.

It is submitted that it is not enough that the values of equality and dignity may be decisive. These constitutional values must be decisive for the balance to be maintained. The court in *Barkhuizen*<sup>20</sup> stresses the point that "these considerations express the constitutional values which must now inform all laws, including the common law principles of contract".

The court continues to state as follows:

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19 *Barkhuizen v Napier* 2007 5 SA 323 (CC) 13.

20 *Barkhuizen v Napier* 2007 5 SA 323 (CC) 57.

In *Afrox*, the Supreme Court of Appeal recognised that unequal bargaining power is indeed a factor which together with other factors, play a role in the consideration of public policy. This is recognition of the potential injustice that may be caused by inequality of bargaining power...<sup>21</sup>

The court went on to endorse this principle as an important principle in a society as unequal as ours.

Contrary to the belief by some that the parties must suffer the consequences of their folly<sup>22</sup> in committing themselves to terms that are harmful, it is imperative that wherever there was an imbalance in the bargaining process preceding the conclusion of the contract the courts must take that into consideration. It is contended that the purpose of our constitution does not accommodate the perpetuation of incidents of imbalance done in the name of freedom to contract. An injustice cannot be allowed by accepting that simply because the party entered into the contract voluntarily it is then fair that he suffers the injustice occasioned thereby silently.

It is indeed correct that an individual's right to human dignity includes freedom to conclude contracts. It is however not appropriate to ignore the plight of individuals who were obligated into concluding covenants that are to their disadvantage. The position of the small man concluding an employment contract can never be said to be equal to the bigger man, the employer. The economic muscle of the employer is strong enough to endure the wait until the weaker party gives in to the imbalanced employment terms. The Constitution acts as the bigger brother to

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21 *Afrox* 15.

22 *Knox D'Arcy v Shaw* 1996 2 SA 651 (W) 7 where it is stated that the constitution does not take such a meddlesome interest in the private affairs of individuals that it would seek, as a matter of policy, to protect them against their own foolhardy or rash decisions.

maintain the balance between the parties. The imbalance would most probably result from the excess of power waged by the employer in relation to the employee's weaker bargaining position.

It must be emphasised that should the constitutional values be swept under the carpet, the weaker party will be left vulnerable. The restraint agreement is allowed freedom of its own in the sense that it is not subject to the robust arena of unions versus employers. One employee who exits the workplace faces the consequences of the restraint agreement whilst others who remain do not face the same predicament. This isolates the outgoing employee for the restraint agreement to operate in peace as no strike action will take place in sympathy with the ex-employee. This is where the Constitution must come to the rescue of the lone ex-employee who intended to join a competitor employer by guaranteeing against undue interference with his section 22 rights.<sup>23</sup>

Recognising that the bargaining position of parties can tip the scales in favour of the stronger party necessitates that the courts come alive to the reality of the existence of the constitutional dispensation which respects the individual's right to work. The existence of the constitutional right to trade, occupation or profession should be the point of departure when deciding disputes in this regard. In other words protecting the individual's right to go and secure another job should be the priority as it is specifically provided for in the Bill of Rights.<sup>24</sup>

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23 Right to freely choose trade, occupation or profession which is entrenched in the *Constitution*.

24 Chap 2 of the *Constitution*, 1996

*Pacta sunt servanda*, important as it is, should not hinder the ex-employee's chances of securing the next job opportunity unless it is extremely necessary to deny him that right. The court should not allow the hindrance if it is only that the ex-employee signed the contract and therefore he must be held to it. Limiting a constitutional right entrenched in the Bill of Rights should take more than this due to the quest by society to avoid and prevent the imbalances that existed in the past under circumstances where bigger parties took advantage of the weaker parties.<sup>25</sup>

The tug of war between common law and constitutional rights is far from over. In the meantime the employee is denied full advantage of the fundamental rights that operate in his favour. Common law principles rule the roost due to reluctance by judicial powers to engage the protection afforded by the Constitution.

The restraint of trade is by its very nature similar to detention without trial which enjoyed wide practice during the dark days of Apartheid. The employee is being punished for no wrong committed. Therefore utmost care must be exercised when resorting to this extreme measure to limit the employee's constitutional right.

Having realised that even with a reasonable restraint agreement the employee stands to lose, in Germany payment of a consideration equivalent to 50% of salary for 50% of the restraint period is paid to the employee as part of the deal.<sup>26</sup>

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25 See s 36 of the *Constitution*, the limitation clause.

26 Weiss "Lecture".

This means that the employee carries 75% burden of the restraint to the employer's 25%. The imbalance is not fully addressed.

In this country the equalising strategy is non-existent. The adjudication process tends to be winner-takes-all as the employee is not given or paid any amount to offset the restraint period. No balance is struck.

### **3 The constitutional values relating to restraint of trade agreements**

The constitutional values have come to colour every dispute due to the fact that most of the legislation applicable was made before the dawn of the constitutional era. Most of the values that are now held in high esteem were not even considered in the past. Discrimination, for instance, dictated the better part of legislation and application and there was found to be nothing wrong.

The discussion hereunder focuses on the values and topical issues that dictate the manner of approaching dispute resolution in the constitutional regime. This section covers the debate about vertical/horizontal application, direct/indirect application, as well as sections from the Bill of Rights, which are the cornerstones of this discussion.

#### ***3.1 The horizontal and vertical application debate***

Vertical application refers to the application of the Bill of Rights to disputes between individuals and the state. An individual can invoke the violation of a right contained in the Bill of Rights to bring litigation against the state.

Horizontal application refers to application of the Bill of Rights between private parties. This seldom happens due to the fact that common law still covers most of the disputes arising between private individuals. It is still a big debate whether the Bill of Rights should apply to private disputes or not.

This question was raised In Re: Certification of the Constitution of the Republic of South Africa<sup>27</sup> that was heard in 1996.

The following objections were raised regarding section NT 8(2) which provides that:

A provision of the Bill of Rights binds natural and juristic persons if, and to the extent that, it is applicable, taking into account the nature of the right and of any duty imposed by the right.

It was objected that this would impose obligations upon persons other than organs of the state; it permitted horizontal application.

It violated the principle of separation of powers between the legislature, the executive and the judiciary. This, it was objected, was due to the fact that the courts would be empowered to alter legislation, particularly, common law. It was further objected that the courts would be bestowed with the improper duty of balancing competing rights including instances where private persons are involved.

If horizontal application is allowed obligations upon individuals would make them suffer a diminution of their rights in a manner that is contrary to Constitutional Principle II (CP II).

The court successfully addressed all objections, save for the fact that horizontal application is not universally accepted. It argued however that the requirement of

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27 (1996) 17 ILJ 821 (CC).

universal acceptance does not preclude the inclusion of provisions which are not universally accepted.

It is also important that the court emphasised the duty of the courts to invalidate legislative provisions which are inimical to the Constitution as provided for in section 2 thereof. The duty to develop common law dates back and it is further confirmed by the constitution.

The courts have grappled with this debate for a long time and so far no certainty has been established. Today one court will rule that horizontal application of Chapter 2 is the way to go and tomorrow another court rules differently. This is the state of things so far and people have to make do with that.

*In Du Plessis v De Klerk*<sup>28</sup> Judge Madala laments the situation as follows:

Because of these conflicting decisions, clarity on the issue is needed and the ruling of the Constitutional Court is eagerly awaited. The question involves a consideration of whether or not a private individual can institute action or sustain a defence against another private individual on the basis of a violation of a right contained in Chapter 3. There is no simple answer to the question whether an alleged breach of a fundamental right contained in Chapter 3 could found an action between private individuals, but the answer to this question must be sought in the provisions of the constitution itself, having regard to the underlying values and objects of the Constitution.<sup>29</sup>

The question that remains to be answered is whether the courts are able to do justice to private litigants when this kind of uncertainty is still experienced. This effectively means that until the Constitutional Court is presented with the

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28 1996 3 SA 850 (CC) 156.

29 *Du Plessis v De Klerk* 1996 3 SA 850 (CC) 156.

opportunity to decide this debate, uncertainty will continue to characterise decisions based on this controversy.

Judge Kriegler in the same case adds a dimension to this argument which will keep the fire burning until then. He argues that it does not matter if the Bill of Rights has or does not have horizontal application. He states that the debate is not one of "verticality" versus "horizontality".<sup>30</sup> According to his interpretation the Chapter 2 applies to all law and this includes common law. The judge is convinced that "all means all".<sup>31</sup> The judge is satisfied that putting the interpretation clause at the end of Chapter 2 (Chapter 3 in interim constitution) means that even in the cases whereon provisions of the chapter do not apply directly, the spirit, purport and objects of the Bill of Rights must inform the rules of applicable law.<sup>32</sup>

It is submitted that the argument by Judge Kriegler, being informed by the preamble of the Constitution and the historical background of the Constitution as well as the object of the new order sought to be created, is in accord with the purpose of the Constitution. Vertical application of Chapter 2, in isolation from horizontal application, is definitely not the intention of the drafters of the Constitution.

Even if it may be called vertical application the practical imperatives emanating from the Constitution are such that horizontal application cannot be ruled out

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30 *Du Plessis v De Klerk* 1996 3 SA 850 (CC) 119.

31 *Du Plessis v De Klerk* 1996 3 SA 850 (CC) 130.

32 *Du Plessis v De Klerk* 1996 3 SA 850 (CC) 137.

completely. The extent to which the chapter will be involved will depend on the situation of the case looking at the provisions of the enabling law in application. The judge's argument that the plight and imbalances of the past did not come from the government alone but they came from private individuals as well makes much sense for horizontality. To argue that private parties are not governed by Chapter 2 would undermine the objects of the constitution by discouraging direct litigation based on violation of the fundamental rights. In echoing this sentiment Judge Madala in the case of *Du Plessis v De Klerk* writes as follows:

Ours is a multi-racial, multi-cultural, multi-legal society in which the ravages of apartheid, disadvantage and inequality are just immeasurable. The extent of the oppressive measures in South Africa was not confined to government/individual relations, but equally to individual/individual relations. In its effort to create a new order, our Constitution must have been intended to address these oppressive and undemocratic practices at all levels. In my view our Constitution starts at the lowest level and attempts to reach the furthest in its endeavours to restructure the dynamics in a previously racist society.<sup>33</sup>

In *Barkhuizen v Napier*<sup>34</sup> the court was called upon to decide on a contractual term that the Applicant alleged to violate section 34 of the Constitution. The term was to the effect that after repudiation of the claim the claimant must approach the court within 90 days. The Applicant argued that the 90 day period is inconsistent with his right to seek the assistance of the courts because it was too short.

Judge Moseneke argued against verticality as follows:

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33 *Du Plessis v De Klerk* 1996 3 SA 850 (CC).

34 2007 5 SA 323 (CC).

Public policy cannot be determined at the behest of the idiosyncrasies of individual contracting parties. If it were so, the determination of public policy would be held ransom by the infinite variations to be found in any set of contracting parties.<sup>35</sup>

This was a matter between private parties and the judge was just emphasising that the courts cannot sit back and allow the fundamental rights contained in the Constitution<sup>36</sup> to be violated under the pretext of contractual autonomy. *Pacta sunt servanda* does not preclude the courts from adjudicating on the contractual terms that violate the fundamental rights.

This should serve to confirm that the right to freedom of trade, occupation or profession should be treated with the same dignity afforded *pacta sunt servanda*, if not more.<sup>37</sup> The reasonableness of the restraint agreement should be examined with vigour to guarantee protection from undue interference with the employee's right to work.

The problem of horizontality and verticality haunts not only one country but many that have similar constitutional models. In Germany they have settled for indirect horizontal application. In some other countries such as the USA indirect horizontal application which accommodates horizontal application for some rights, has become the norm. In Germany the same model is followed by identifying direct areas and indirect ones.<sup>38</sup>

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35 *Barkhuizen v Napier* 2007 5 SA 323 (CC) 38.

36 Right to approach the courts (s 34) was at stake.

37 The right is entrenched whereas *pacta sunt servanda* is not.

38 Weiss "Lecture" 2005.

The courts in this country have adopted, through practice, indirect horizontal application through the vehicle of public policy.<sup>39</sup> The effect of indirect horizontal application is that the Bill of Rights is not directly applicable to the disputes in question. The rights contained in the Bill of Rights only find expression through the vehicle of public policy. The constitutional imperatives as exemplified by the values such as equality, freedom, fairness and human dignity are □a must apply□, but they only seep through or radiate through the requirement of public policy.<sup>40</sup> The importation or incorporation of these values will therefore differ from court to court depending on the understanding of the particular court.

The challenge with this model is that some courts are likely to continue to exclude the Constitution under the pretext that it does not apply to private disputes. This would be sad news for the country considering the past where the imbalances were the order of the day under the regime of common law and relevant statutes.

## **3.2 *Direct and indirect application***

### *3.2.1 Direct application*

Direct application refers to disputes where the Bill of Rights is the applicable law and forms the basis of the cause of action. In these instances the Bill of Rights overrides any other law that applied before the Bill came into existence. Any conduct or law inconsistent therewith will not concurrently apply due to the fact

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39 See *Barkhuizen v Napier* 2007 5 SA 323 (CC); *Du Plessis v De Klerk* 1996 3 SA 850 (CC).

40 *Du Plessis v De Klerk* 1996 3 SA 850 (CC) 110.

that it cannot be allowed to contradict the provisions of the Bill of Rights. The Bill will moreover generate its own remedies where ordinary law does not have remedies congruent thereto.<sup>41</sup>

### 3.2.2 *Indirect application*

In indirect application the Bill of Rights does not override the ordinary law that applies in the circumstances. It however serves to establish a normative value system through a set of values that must be respected in the interpretation of the ordinary law applicable. These values will radiate into interpretation of the applicable and thereby reflect indirectly the spirit, purport and objects of the Constitution.<sup>42</sup>

The Bill of Rights would not be directly applicable to the disputes about restraint of trade agreements because this is the area covered by ordinary common law. The constitutional values would only radiate through by the process of being □read into□.

The danger of reading into or radiation of the constitutional values is that the courts might easily decide to skim on top or gloss over for the sake of compliance. The interpretation accommodating the constitutional values might not enjoy favour over the established common law rules. The employee's section 22 right might not be satisfactorily considered when deciding on the verdict due to the scant reverence for the Constitution under the circumstances.

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41 Currie and De Waal *Bill of Rights Handbook* 32

42 See Currie and De Waal *Bill of Rights Handbook*.

### **3.3 The application of section 22**

The section reads as follows:

Every citizen has the right to choose their trade, occupation or profession freely. The practice of a trade, occupation or profession may be regulated by law.

Currie and De Waal argue as follows regarding the constitutional era and the enforcement of restraint agreements:

Arguably however, the 1996 Bill of Rights requires review of the common law in this area, particularly in relation to the question of onus. The principles of restraint of trade law are based on public policy. Public policy is not constant and unchanging and must be considered against the background of the Constitution. As we have seen, the 1996 Constitution brought about an important change in the focus of the freedom of trade right. The broad right to commercial freedom entrenched in s 26 protected both freedom of contract and freedom of trade. But the more narrow freedom of occupational choice and practice guaranteed by s 22 seems to favour freedom of trade. In *Magna Alloys*, the Appellate Division held that the onus of proving the unreasonableness of a restraint was on the party who wished to escape the restraint. The reason, according to the court, was that the common law favoured sanctity of contract over freedom of trade. The effect of the clear preference for freedom of trade in the 1996 Constitution is that the issue of the onus must therefore be reconsidered.<sup>43</sup>

This statement is a clear indication that the dawn of the constitutional era requires new approaches in interpreting restraint agreements. Old precedent must be followed with caution especially where matters of constitutional importance are dealt with. The *Magna Alloys* case is constitutionally speaking neither here nor there; it has run its course and is out of time.

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43 Currie and De Waal *Bill of Rights Handbook* 497.

### **3.4 *The element of dignity***

Section 10 reads as follows:

Everyone has inherent dignity and the right to have their dignity respected and protected.

This section finds real expression where a person's welfare is jeopardised by the threat of poverty and having to live not knowing where the next meal will come from. The damage caused to a person's dignity by disengaging them from the employment world, or by closing down their only source of income, cannot be explained. The indignity of unemployment has caused untold suffering to many people who were working initially and lost their jobs.

*Currie and De Waal* remark as follows concerning the right to human dignity:

Recognising a right to dignity is an acknowledgement of intrinsic worth of human beings. Human beings are entitled to be treated as worthy of respect and concern. This right therefore is the foundation of many of the other rights that are specifically entrenched in the Bill of Rights.<sup>44</sup>

It follows that the restraint of trade agreement will definitely have the effect of dealing a hard blow to the dignity of the ex-employee if not administered properly. The balancing act must be performed to leave the losing party with the means of the dignity of work. The restraint that has the effect of preventing the employee to look for work at places of his choice and convenience will definitely affect his right to dignity negatively.

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44 *Bill of Rights Handbook* 274.

### **3.5 *The equality clause***

Section 9 provides that everyone must receive equal treatment, protection and benefit of the law. The unequal position of the employer and employee must be considered as one of the factors militating against enforceability of the restraint. It has been shown by Mokgoro, J in the *Barkhuizen v Napier*<sup>45</sup> case that standard contractual terms are drawn virtually without the other party present to make an input or to object. This demonstrates the inequality that characterises the proceedings at the point of concluding of contracts.

### **3.6 *The limitation clause***

Section 36 prescribes the procedure that must be followed to justify the limitation of a right contained in the Bill Of Rights (Chapter 2 of the Constitution). The cases that have so far been considered do not use this procedure in full due to the fact that they still follow the precedent of cases decided before the Constitution came into operation. In terms of the provisions of this section the employer would have had to justify the limitation of section 22 in respect of the employee. It is submitted that if the dispute is subjected to the procedure prescribed by this section the outcome would be more convincing than currently is the case.

The debate about verticality and horizontality has proved to be just a storm in a teacup. The same goes for direct and indirect application because in the final

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45 2007 5 SA 323 (CC) at 15-19.

analysis the courts are stretched to ignore these barriers when in serious search for justice.

The limitation clause in the restraint agreements disputes must find a way of being applied so that justice can be fostered by adducing evidence justifying the limitation of section 22.

#### 4 Enforcing restraint of trade under the Constitution

The constitutional era has brought with it a new approach to adjudication of disputes. The Constitution empowers the courts to develop common law in its model to an extent that where the latter fails to agree with it, it will be accordingly declared invalid.

The courts are instructed to interpret legal provisions in such a manner that they will be consistent with the spirit, purport and the objects of the Constitution. The discussion hereunder deals with case law delivered after the Constitution has come into operation in 1996. The purpose here is to establish how far the courts go to foster balance between common law of contract and the Bill of Rights as well as to check whether the limitation clause is followed when limiting the constitutional rights.

There are normally three elements to a restraint of trade clause. First we find a description of the activities or kind of work which the employee is restrained from doing, and this is then secondly linked to a time period. In most cases limits are placed on the geographical area in which the employee may not work during the term of the agreement.<sup>46</sup> The above clause was included in Mr. Reddy's

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46 *Reddy v Siemens Telecommunications* 2007 28 ILJ 317 (SCA). The relevant clause in the contract read as follows: "The employee agrees and undertakes that, in order to protect the proprietary interest of the employer in the employer's trade secrets, he or she shall not throughout the period of his employment by the employer and for a period of twelve months after the termination date, either directly or indirectly within the prescribed area

employment contract with Siemens and when it appeared that he was contemplating taking up employment with Ericsson, Siemens approached the High Court for an interdict preventing him from accepting employment with Ericsson. The employer was successful and the High Court held that the restraint of trade was aimed at preventing a person with knowledge of the employer's technologies as a result of his employment from utilising them to the detriment of his employer.

The Supreme Court of Appeal concurred with the finding of the High Court. The court held that the main questions that arise in the context of restraints of trade relate to contracts and whether and when they should be enforced. The court accepted that Reddy had willingly concluded a contract which included the restraint of trade provisions. The Supreme Court of Appeal took into account the constitutional values when applying the law of contract as the Constitution enjoins it to do.

On behalf of the employee, it was argued that the applicable contractual rules stating that contracts should be enforced and the rule that the onus is on the employee to show that the restraint is unreasonable was in contravention of section 22 of the Constitution.

The court held that it was not necessary to decide the Constitutional challenge to the rules of onus. It stated that if the facts show that the restraint is reasonable

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[Gauteng] be interested, engaged or concerned as an employee in any concern which carries on the same business as the employer's business or a business allied or similar to the employer's business.”

the employer must succeed; if the facts show that the restraint is unreasonable, the employee will succeed. The court concluded that this calls for a value judgment.

The court summarised the principles when making a value judgment in the case of restraint of trade: The first principle is that the public interest requires that parties should comply with their contractual obligations. The second principle is that all persons should be permitted to engage in trade or commerce or a profession. The court concluded that both these principles reflect not only the common law, but also constitutional values:

Contractual autonomy is part of freedom informing the constitutional value of dignity, and it is by entering into contracts that an individual takes part in economic life. In this sense freedom of contract is an integral part of the fundamental right referred to in section 22. Section 22 of the Constitution guarantees '[e]very citizen ... the right to choose their trade, occupation and profession freely' reflecting the closeness of the relationship between the freedom to choose a vocation and the nature of a society based on human dignity as contemplated by the Constitution. It is also an incident of the right to property to the extent that section 25 protects the acquisition, use, enjoyment and exploitation of property, and of the fundamental rights in respect of freedom of association (section 18), labour relations (section 23) and cultural religious and linguistic communities (section 31).

The Supreme Court of Appeal referred to and approved earlier decisions in which the Court formulated four questions that had to be taken into account when considering the reasonableness of a restraint of trade:

1. Does the one party have an interest that deserves protection after termination of the agreement?
2. If so, is that interest threatened by the other party?

3. In that case, does such an interest weight qualitatively and quantitatively against the interests of the other party not to be economically inactive and unproductive?
4. Is there an aspect of public policy having nothing to do with the relationship between the parties that requires that the restraint be maintained or rejected?

If the interest of the party sought to be restrained (the employee) weighs more than the interest to be protected, the restraint is unreasonable and consequently unenforceable. At the time of enforcement of the restraint of trade, the enquiry includes the nature, extent and duration of the restraint of trade and specific considerations relating to the parties and their respective bargaining powers and interests.

On the facts the Supreme Court of Appeal found that the employee was in possession of confidential information in respect of which there was an obvious risk that he would disclose this information during the course of his employment with a competitor. His loyalty would be to the new employer and there is a real possibility that he would disclose the information he obtained while employed by Siemens. The court reiterated that public policy requires contracts to be enforced and that that is consistent with the constitutional values of dignity and autonomy. In this case the restraint of trade agreement was not against public policy and it should be enforced. The Supreme Court of Appeal agreed with the High Court that a final interdict preventing Mr. Reddy from working for the competition was the acceptable remedy.

In *Dickinson Holdings Group v Du Plessis*<sup>47</sup> the Court looked in detail at the kind of knowledge the employee obtained, by virtue of his employment, and whether this constitutes proprietary information that amounts to a protectable interest. Here the court again rejected the argument of the employee that he is prevented from working since the employee did not present any evidence on what he did to obtain work.

In respect of the question of protectable interest, the High Court looks at a number of cases to see what this means. Some of these earlier cases had held that customer lists, could be included, as would information about business opportunities, trade connections, pricing strategies and manufacturing processes, methods of operation, business conditions and customer relationships. The type of information itself does not, however, establish whether it is confidential – all the relevant facts must be taken into account. Naturally, information must be useful to a competitor in order to be regarded as confidential as between an ex-employer and ex-employee. The seniority of the employee is also an important consideration; after all, senior employees obtain more knowledge that may be of considerable value to a competitor.

From the author's point of view it should be taken into account that the employee resigned voluntarily with full knowledge that he was subject to a restraint clause in his contract of employment. Can this be a matter of *volenti non fit injuria* (if it can apply)?

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47 2008 4 SA 214 (N); (2008) 29 ILJ 1665.

In balancing the rights of the parties the court again in *Den Braven SA v Pillay*<sup>48</sup> looked not only at the information that the employee had available from his former employer but also to the relationship that the employee, who was a sales person in the specific area had with customers. The court found on the facts that the employee presented no evidence that the client would not follow him should he be allowed to work for the new employer. The court stated the principle that the connection between the former employee and the customers must be of such a nature that it will be possible for the employee to persuade the customers to follow him or her to a new business.

The principles laid down by the Supreme Court of Appeal in the Reddy case was applied in *Continuous Oxygen Suppliers t/a Vital Aire v Meintjes*.<sup>49</sup> Turning to the law pertaining to restraints of trade, the court confirmed that covenants in restraint of trade are generally enforceable and valid. Like all other contractual stipulations, however, they are unenforceable when, and to the extent that, their enforcement will be contrary to public policy. Where a restraint unreasonably restricts an employee's right to work or freedom to trade, such restraint will not be enforced. Whether a restraint is in fact unreasonable is determined on the facts of the case. In making its assessment the court has regard to the circumstances that existed when the parties entered into the restraint agreement, as well as what has happened since and what prevails at the time enforcement is sought. The court is required to make a value judgment bearing in mind two principal policy considerations, namely that the public interest requires that parties should comply with their contractual obligations, and that it is in the interests of society

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48 2008 6 SA 229 (D).

49 (2012) 33 ILJ 629 (LC).

for all persons to be productive and permitted to engage in trade.<sup>50</sup> The court was however concerned about the two year duration of the restraint and reduced the term to 12 months in order to balance the rights between the parties.

On the balance it seems that the courts had consideration for the constitutional values but also used the principles and practicalities to find whether the employer had a protectable interest. The question is whether this is sufficient to give effect to the constitutional values.

It is good that the courts have regard for the constitutional values when deciding on disputes on restraint agreements. As indicated above the court's attitude to the reach of the Constitution into this kind of disputes, will determine how far it goes to incorporate the constitutional values in its decision. Some courts will only cursorily and without effect refer to the constitutional values whereas others will really work in the said values to make a difference in the decision.

The courts that have indicated that the Constitution has no place in these disputes imply that the existence of section 22 and the Bill of Rights itself have no impact. This obviously raises questions that the creation of the Bill of Rights was meant for no useful purpose and that the Constitution is as good as not there. The reality is that the Bill of Rights must be implemented as intended by the creators thereof.<sup>51</sup> There is fear that the question of the restraint agreements in post-constitution era will never be confronted head-on with section 22 as the point of reference. All the decisions that have been made only touch the

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50 In the headnote at G and H.

51 Redressing injustices of the past is one of the objects of the Constitution. See preamble.

periphery of this right and no reference to its limitation is ever made. The problem is that the SCA for instance still adheres to the decision made in 1984 in the *Magna Alloys* case.<sup>52</sup> This shows reluctance on the part of the courts to deal with the controversy. A post-constitution precedent must be set which deals satisfactorily with the hard-core issues of *pacta sunt servanda* versus the right entrenched by the Constitution (section 22).

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52 See *Reddy v Siemens Telecommunications* 2007 2 SA 486 (SCA).

## 5 Conclusion and recommendations

Section 22 does not receive full attention in dispute resolution concerning restraint agreements. Common law still reigns supreme as the courts are satisfied that this area is best served by applying common law principles of *pacta sunt servanda*.

The constitutional rights contained in the Bill of Rights do not receive first preference as the general approach is that where common law is applicable, the constitutional rights must be applied indirectly. The High Courts are still grappling with old precedents that no longer address the demands of new developments arising from the constitutional regime. It becomes apparent that the courts did not find it necessary to develop the common law any further but to consider the constitutional rights as one of the factors to consider in answering the question as to whether the contract is against the public policy or *boni mores*. The debate therefore remains open as to whether this approach provides sufficient protection of the rights enshrined in the Constitution.

The debate about vertical / horizontal application of the Bill of Rights will remain hanging until the Constitutional Court makes a decisive ruling in this regard. Currently the indirect application model is the one favoured by most courts. The problem is that some courts totally exclude the constitutional values when determining reasonableness of the restraint agreements.

The concept of public policy means different things to different people and courts. From a common law point of view public policy means that contractual obligations

such as the restraint agreements must be fulfilled and the party that wants to escape such must show the reason why. The employee's interests are subject to the employer's protectable interest as outlined in the agreement.

The new era interpretation of public policy is to the effect that constitutional values must characterise public policy. The protagonists of this view stop short of shifting the onus to the employer to show why the employee's right of occupation should be interfered with. The constitutional right to freedom of trade, occupation or profession is held higher than *pacta sunt servanda* meaning that the employer party must do more to prove the need to deny the employee party to enjoy the right.

The belief by some courts that common law has all along been catering sufficiently for the interest of the employee parties, coupled with the notion that the employee party exercise his constitutional right to human dignity and freedom by concluding contracts, and the argument that the employee party does not therefore deserve any further protection, does not help matters when it comes to the balancing act. The employee party's interests are best articulated by section 22 (the right to freely choose trade, occupation or profession) whereas in common law this interest enjoys only the status of a mere consideration.

It is recommended that Section 22 to be considered as one of the rights that apply directly to the sphere of contract law. Furthermore restraint agreements should be subjected to section 36 of the Constitution with the employer showing cause why alternative means should not be applied to protect employer interest. The third proposal is that the courts should vigorously shape the common law of

contract in line with the constitutional framework comprising the values of freedom, democracy, equality, and human dignity.

And finally that a consideration be payable to the employee in the event the restraint agreement has been found reasonable and enforceable. Payment should be made for 50% of the restraint period.

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## Certificate of language editor



### VERKLARING TEN OPSIGTE VAN TAALVERSORGING

Hiermee verklaar ek, Wilna Myburgh, dat die onderstaande skripsie, wat deur Mapiti Piet Ramaphoko aan die Noordwes-Universiteit ingedien word, deur my taalversorg is en dat dit in lyn met die nuutste taalgebruikriglyne en algemeen aanvaarde standaardde is.

Geteken op 14 November 2013

A handwritten signature in black ink, appearing to be 'Wilna Myburgh', is written over a faint rectangular box.

W MYBURGH