

Privy Council Appeal No. 93 of 1933.

The Pearl Assurance Company, Limited - - - - *Appellants*

v.

The Government of the Union of South Africa - - - *Respondents*

FROM

THE SUPREME COURT OF SOUTH AFRICA (APPELLATE DIVISION).

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE
PRIVY COUNCIL, DELIVERED THE 10TH JULY, 1934.

Present at the Hearing :

THE LORD CHANCELLOR (VISCOUNT SANKEY).

LORD TOMLIN.

LORD RUSSELL OF KILLOWEN.

LORD MACMILLAN.

SIR LANCELOT SANDERSON.

[*Delivered by* LORD TOMLIN.]

This is an appeal by special leave from an order of the Supreme Court of South Africa (Appellate Division) dated the 25th April, 1933. The Appellate Division dismissed with costs the appeal of the appellants against that part of an order of the Supreme Court of South Africa (Transvaal Provincial Division), dated the 24th December, 1932, which had disallowed one branch of an exception taken by the appellants to the respondents' declaration in an action by the respondents, against the appellants.

The facts are as follows : On the 28th May, 1928, acting under the provisions of the Diamond Cutting Act of 1919, the respondents by the Under Secretary for Mines and Industries entered into an agreement with Rosenstrauch Bros. and Jacques Korb (hereinafter called the cutters), whereby in effect the cutters undertook to set up a diamond cutting industry in the Union and within a period of six months, to erect and complete a diamond cutting factory or factories, to provide the necessary machinery therefor, and to conduct all necessary operations in connection therewith. The contract was one for five years. The respondents were to pay substantial subsidies : £15,000 for the first ; £10,000 for the second ; and £5,000 for the third year, and also to provide free second-class steamship accommodation from London or Southampton to a Union port and free railway passages to the

place where the factory was to be erected, for expert workmen, not exceeding fifty, to be introduced by the Cutters from overseas. Further, the Cutters bound themselves to import from overseas expert workmen, to provide the necessary machinery, including forty polishing mills, to train in their factory one hundred apprentices, who should be Union nationals, for the first year, an additional hundred for the second year, one hundred and fifty for the third year and one hundred and fifty for the fourth year, that is 500 in all of such apprentices in four years, and to pay them wages as set out in the agreement. By clause 14 of the agreement the Cutters undertook upon the signing of the agreement to deposit with the respondents a guarantee of £5,000 (five thousand pounds) and, if called upon by the Minister of Mines and Industries to lodge within six weeks after ratification of the agreement a further guarantee to his satisfaction in a further sum not exceeding £5,000 (five thousand pounds) which guaranteed sums were to be considered as liquidated damages and to be paid to the respondents in the event of the Cutters' failure to carry out all and several the obligations imposed upon them under the agreement.

The agreement was ratified by Parliament on the 1st June, 1928, and the full guarantee up to £10,000 was called for by the Minister under clause 14 of the agreement.

The Cutters, in order to fulfil their obligations under clause 14 of the agreement, arranged with the appellants for the latter to give to the respondents the guarantee next hereinafter mentioned.

On the 6th November, 1929, the appellants gave to the respondents a guarantee for £10,000 to satisfy clause 14 of the agreement. It was in the form of a letter by the appellants addressed to the Secretary for Mines and Industries and reads as follows :—

"Referring to the Agreement dated 28th May, 1928, between the Government of the Union of South Africa and Rosenstrauch Bros. and Jacques Korb, for the establishment of a diamond cutting industry in the Union we beg to state that we, Pearl Assurance Company, Limited, hereby bind ourselves as sureties in solidum for the sum of £10,000 (ten thousand pounds sterling) for the due fulfilment of the said Agreement.

The said sum or portion thereof is payable upon our receiving written demand from you, that such sum or portion thereof is due and payable in terms of our Guarantee.

This surety bond shall continue and be binding on us for a period of four years from this date. It is not negotiable nor transferable and should be returned as soon as the terms of the said Agreement have been fulfilled."

After the execution of the agreement, the Cutters proceeded to erect a factory, but on the 31st December, 1931, they repudiated the agreement and closed down the factory.

In March, 1932, the business of the Cutters was sequestrated as insolvent by the Supreme Court of South Africa.

On the 2nd June, 1932, the respondents commenced an action against the appellants, and in the declaration claimed against the appellants as guarantors :—

- (i) the stipulated sum of £10,000 as and for liquidated damages,
- (ii) alternatively, damages up to £10,000, particulars of damages amounting in all to £27,559 3s. 11d., being set out in para. 10 of the declaration.

On the 21st June, 1932, the appellants filed an exception to the declaration on the ground that it was vague, embarrassing and bad in law and disclosed no cause of action.

The exception was heard in the Transvaal Provincial Division of the Supreme Court of South Africa, by De Waal, J.P., and De Wet J., on the 25th and 26th October, 1932, and on the 24th December, 1932, the Court, for reasons which will presently be stated, dismissed with costs the exception in so far as it related to the first claim for the stipulated sum of £10,000 as and for liquidated damages, but upheld with costs the exception in so far as it related to the alternative claim for particular damages.

As to the alternative claim the respondents subsequently entered a cross-appeal against the judgment of the Court of first instance, but thereafter withdrew such cross-appeal. The declaration therefore stands as though the particulars and the alternative claim were struck out.

The appellants appealed to the Supreme Court of South Africa (Appellate Division) against the order in so far as it related to the first claim for the stipulated sum of £10,000, and this appeal was dismissed. Against that dismissal the appellants have appealed to His Majesty in Council.

Before dealing with the problems with which this case is concerned, their Lordships think it well to call attention to certain considerations which in their view should be borne in mind in dealing with such a matter as this.

In the first place, the questions to be resolved are questions of Roman Dutch law. That law is a virile living system of law, ever seeking, as every such system must, to adapt itself consistently with its inherent basic principles to deal effectively with the increasing complexities of modern organised society.

That those principles are capable of such adaptation cannot be doubted, and, while it would be idle to assert that the development of the Roman Dutch law in the territories now constituting the Union has not been affected appreciably by the English law, yet in their Lordships' judgment, approach should be made to any question governed by Roman Dutch law without any fetter imposed by recollections of other systems, and through the principles of Roman Dutch law alone.

The fact that the solution of a particular problem reached by the Roman Dutch law bears a similarity to the solution provided by another system does not necessarily indicate any imposition of the rules of one system upon the other, but may be cogent evidence of a resemblance between the relevant basic principles of the two systems.

In the next place their Lordships would observe that on procedural questions their Lordships would always be reluctant to differ from the conclusions arrived at by the Courts on the spot.

Now the questions which have been debated before their Lordships' Board are three in number, namely :—

(1) Whether the stipulated sum sought to be recovered by the respondents from the appellants as the guarantors thereof in the name of liquidated damages and described as liquidated damages in the principal contract between the respondents and the Cutters is an agreed pre-estimate of damage, or a penalty.

(2) Whether if it is a penalty the declaration which as matters now stand contains no allegation of damage is demurrable in the absence of any plea of damage, and

(3) If the declaration is not demurrable whether the onus is on the appellants to prove that the respondents' damages are nothing or less than the penalty or whether it is for the respondents to prove what damage has in fact been suffered.

The Supreme Court of South Africa (Transvaal Provincial Division) upon the exception so far as it failed held that the sum was an agreed pre-estimate of the damage recoverable and that therefore upon proof of breach by the Cutters the respondents were entitled to succeed.

Upon appeal to the Appellate Division the Court unanimously held that the stipulated sum was a penalty, but that the exception failed because the claim for the stipulated sum without a plea of damage was sufficient even if the sum was a penalty. The majority of the Court, however (Wessels, C.J. and de Villiers, J.A.) also adopted the view that it was for the appellants to plead and prove that the respondents had suffered no damage or damage less than the penalty before any onus came to lie upon the respondents at all, while the third judge, Stratford J.A., held that though it was enough for the respondents to claim the sum without alleging damage, it was for the respondents to prove the damage actually suffered and that the damage so proved not exceeding the agreed sum could be recovered.

Upon the first question the Appellate Division were in their Lordships' judgment clearly right. Indeed the contrary was but faintly argued.

The second of the above questions appears to their Lordships to be in the main a question of local procedure and their Lordships are not prepared to differ from the view taken below which attributes to such a pleading as this by implication an allegation of damage. The third question is of general importance and involves a broad consideration of the way in which "pœna" has been from time to time regarded and dealt with under the Roman Dutch law.

Among the writers of authority there were marked differences of opinion upon this topic—Dumoulin adhered to the view that a "pœna" stipulated in case of non-performance of an obligation

might when excessive, be reduced and moderated by the judge differing in this respect from the doctrine which had long before been expressed by Azo to the effect that a conventional penalty is not subject to moderation.

The view of Dumoulin was approved by Pothier (Evans Translation, 1806, Vol 1, pp. 209 *et seq.*) and Voet (45.1.13) says "sed & si non voluntaria verum necessaria pœnæ stipulatio sit," then the proctor has power to reduce the penalty.

Van Bynkershoek (*Quæstiones Juris Privati*, c.14) states the position in what is perhaps the most logical form. After a somewhat contemptuous reference to Dumoulin and others, he says: "it is safer and better to follow the Roman law and to hold that penalties in contracts for doing or not doing something were invented for no other purpose than to provide that the measure of damages should not be uncertain and that provided we observe the qualifications laid down in Justinian's decree (*Cod. de Sentent. quæ pro eo quod interest prof.*) there is nothing to fear from such pacts. He adds later, however, that if a penalty clause in a contract is vastly in excess (*longe et late excedat*) of any real loss which the stipulator may suffer, then the decree referred to must be strictly observed, that is to say, the assessment of damages must be left to the judgment of the Court, but subject to this limitation, that if the matter is of a fixed and definite value the damages shall not exceed another similar sum, but if the matter is of uncertain and doubtful value, the damages shall not exceed the actual value to the stipulator, that is, they shall be limited to the loss sustained, but shall not include the profits which have been lost."

These differing and not always consistent opinions arise no doubt from a common desire to reconcile the application of two conflicting principles recognised by the Roman Dutch law, namely, the principle that a man should be held to his bargain and the principle that one man should not be allowed oppressively to enrich himself at the expense of another.

Now, it is to be observed that all the writers who favour the Court's power of reducing the "pœna" make the test of its reducibility, that is the test whether it is "ingens" or not, the amount of the damages actually resulting from the breach. By none is it suggested that in the intention of the parties as exhibited by the contract is there to be found any guide as to the reducibility of the pœna.

The view of Van Bynkershoek seems to have been adopted and applied by the Supreme Court of the Cape of Good Hope in the early part of the last century in such cases as *Steytler v. Smuts* (1833), 1 M.40, and *Borradaile & Co. v. Muller* (1832), 1 M.55, and it is not until much later that there is found to be a change of usage and the intention of the parties as expressed in the contract is taken into account. In *Cape Town Town Council v. Linder*, 6 Cape of Good Hope L.R. 410, at p. 412, De Villiers, C.J., says:

"Now there is a strong disinclination in our law to allow one person to be enriched at the expense of another and where a stipulation of this kind [i.e., a penalty clause] is inserted in a contract the Court will enquire carefully in each case whether it has been inserted as a penal stipulation or as compensation for damages. In the present case there is no doubt whatever that the sum was to be paid as a penalty. The words are: 'Shall forfeit the penalty of £500.' . . . Well then if this clause was intended as a penal stipulation, I am of opinion that the plaintiffs cannot recover without proof of damage."

This change was perhaps due in part at any rate to the necessity of stressing the principle of the sanctity of contracts as the conditions of society become more highly organised and complex.

In the Transvaal, the cases of *Peach & Co. v. Jewish Congregation of Johannesburg* (1894) 1 O.R. 345 and *Davey Pazman & Co. v. Langlaagte, etc., Co.* (1898), 5 O.R. 216, show that the idea of two categories, namely, (1) a pre-estimate of damage and (2) a penalty, differentiated by reference to the intention of the parties expressed in the contract is being gradually developed though the necessary corollary that if this classification is adopted it follows that a sum falling within category (1) will be irreducible has not yet been fully appreciated or accepted (see judgment of Gregorowski, C.J., in the latter case). That the categories are to be determined by the intention of the parties seems to have been fully recognised later in *Mann & Harris v. Cohen* (1902), Rep. High Court Transvaal, 261).

In Natal it seems plain that prior to 1906 the two categories mentioned above had come to be recognised, though there were still those who thought that a sum intended to be a pre-estimate of damage could still be scaled down if shown to be in excess (see *Searra & Ferrandi v. The Durban Fishing Co.* (1896) 17 N.L.R. 166 and *Bartholomew v. Johnson* (1901), 22 N.L.R. 79), and *Chaffer & Tassie v. Richards* (1905) 26 N.L.R. 207).

In this position of affairs the case of *Commissioner of Public Works v. Hill* [1906], A.C. 368, came before their Lordships' Board on appeal from the Supreme Court of the Cape of Good Hope. There the amount claimed was held below and by their Lordships' Board to be on the construction of the agreement not a genuine pre-estimate of loss, but a penalty recoverable only on proof of damage and only to the extent of the damage proved. The Supreme Court held there was no proof of damage. Their Lordships' Board thought that a further opportunity of proving damage should be given.

Their Lordships' attention has been called to the fact that in the printed reasons of the appellants in *Hills'* case the point as to onus of proof discussed in the present appeal was raised. The decision of the Board seems in their Lordships' opinion to proceed upon the basis that in the Cape of Good Hope the Roman Dutch law had then come to recognise only the two categories already mentioned ascertained by reference to the intention of

the parties as exhibited in the contract, with the result that a sum which did not fall into the category of pre-estimate of damage could not be recovered unless and only to the extent to which damage was proved.

Subsequent decisions in South Africa seem to be consistent with this view, and to correspond with the experience in the Transvaal to which Stratford, J., refers in his judgment. In none of them is there any trace of any classification except that of the two categories already mentioned. In *Zietsman v. Vorster*, 1912, S.A.L.R. (Transvaal Provincial Division), 1144, the present Chief Justice (then Wessels, J.) treated a stipulation for a sum payable on breaches of contract as on true construction of the contract a stipulation for a penalty and held that the claimant must prove damage. To the same effect are *Union Government v. Foster*, 1915, S.A.L.R. (C.P.D.) 204, and *Postmaster General v. Van Niekerk*, 1918, S.A.L.R. (C.P.D.), 378.

Finally, in the Appellate Division of the Supreme Court of South Africa, in *Fraser, Ltd. v. Waller*, 1916, A.D. 494, Innes, C.J., held that a stipulation for the payment of a percentage commission to cover costs of collection in case of default was a penal stipulation and that in respect of a penal stipulation the Court would only award such damage as the claimant had actually sustained. Solomon, J.A., delivered judgment to the same effect and de Villiers, A.J.A., concurred.

It seems to their Lordships upon this review of the history and development of the Roman Dutch law in South Africa (1) that that law has for the purpose of applying the more effectively to modern conditions its own recognised principles gradually modified, its positive rules, so that to-day the field covered by the old "pœna" over which the Court could always have exercised a moderating jurisdiction on being satisfied that the pœna was excessive, having regard to the actual damage suffered—is now occupied by the two categories already mentioned ascertained by reference to the intention of the parties exhibited in the contract, and (2) that if the sum claimed falls into the first category of genuine pre-estimate of damage it can be recovered on proof of breach of contract without proof of damage and cannot be reduced, but that if it falls into the second category it is a penalty and actual proved damage (but not exceeding the amount of the "penalty") can alone be recovered in respect of it. The question whether if the damages exceed the penalty the excess can be recovered in other proceedings does not arise for decision.

The respondents have urged that this conclusion is wrong because, they say, that while the distinction between a genuine pre-estimate of damages and a penalty by reference to the construction of the contract has undoubtedly been introduced into the Roman Dutch law, yet the penalty category remains identical with the old pœna and can be recovered, unless the person from whom it is sought to be recovered establishes it to be "ingens,"

and that if this is done, then the claimant can only recover his actual proved loss. This was the conclusion reached by the majority of the Appellate Division.

With all respect to the Chief Justice and the learned Judge who formed the majority, their Lordships think that the conclusion cannot be supported. In their Lordships' judgment, when once the Roman Dutch law departed from its original view of a stipulatio pœnae as being a stipulation to pay a sum which was always recoverable unless the Court's moderating jurisdiction was invoked by proof that it was excessive in relation to the actual damage suffered, and adopted the two categories of (1) pre-estimate of damages and (2) penalty each ascertained by reference to the intention of the parties as exhibited in the contract there was no room left for the old pœna at all. If it were otherwise there would now be three categories, namely, (1) a pre-estimate of damage; (2) a penalty not being pœna ingens, and (3) a penalty being pœna ingens, although in that case for practical purposes, there would be no difference between (1) and (2) as in neither of these categories could the stipulated sum ever be scaled down.

It is interesting to observe that the Roman Dutch law viewed in the way in which their Lordships think it should be viewed, exhibits a development in this matter on lines similar to those found in the sister system in Scotland, which, like the Roman Dutch law, originally knew nothing of the distinction between liquidated damages and penalty.

Agreeing as they do with the Court below in regard to the first two questions under consideration their Lordships are of opinion that the Appellate Division was right in disallowing the exception.

Having regard however to what has already been said upon the third question, their Lordships think that it will fall to the respondents to prove damage and to give before trial such particulars thereof (if any) as may be asked for and as the appropriate Court in South Africa may see fit to allow.

In the result, therefore, their Lordships are of opinion that the appeal should be dismissed, but in the circumstances without costs on either side.

Their Lordships will humbly advise His Majesty accordingly.

In the Privy Council.

THE PEARL ASSURANCE COMPANY, LIMITED,

v.

THE GOVERNMENT OF THE UNION OF
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