IN THE SUPREME COURT OF SOUTH AFRICA

(APPELLATE DIVISION)

In the matter between

Case No 542/93

SHELAGATHA PROPERTY INVESTMENTS CC APPELLANT

and

KELLYWOOD HOMES (PTY) LIMITED

RESPONDENT

Case No 558/93

SHELFAERIE PROPERTY HOLDINGS CC APPELLANT

and

MIDRAND SHOPPING CENTRE (PTY) LTD RESPONDENT

CORAM: JOUBERT, E M GROSSKOPF, VIVIER, EKSTEEN

et HARMS JJA.

HEARD: 18 November 1994.

DELIVERED: 1 December 1994.

J U D G M E N T

VIVIER JA:

The appeals in these two cases were heard together since the facts are broadly similar and the same issue arose for decision in i both cases. The issue was whether a contractor under a building contract was entitled to enforce payment in terms of an architect's interim certificate, issued while the contract was still in force, after the contractor had cancelled the contract due to the employer's breach of contract. The appellants, Shelagatha Property Investments CC ("Shelagatha") and Shelfaerie Property Housing CC ("Shelfaerie") were respective sureties for the due performance by Shelstaton Two (Pty) Ltd ("Shelstaton") of its obligations under two building contracts it had concluded with Imprefed (Pty) Ltd ("Imprefed") and Group Five Contractors (Pty) Ltd ("Group Five").

The suretyships were secured by mortgage bonds. The respondents, Kellywood Homes (Pty) Ltd ("Kellywood") and Midrand Shopping Centre (Pty) Ltd ("Midrand") were the respective cessionaries of Imprefed and Group Five. In an application brought on notice of motion in the Witwatersrand Local Division Kellywood sought judgment against Shelagatha for payment of a total amount of Rl 800 000,00, for an order declaring the mortgaged property executable, interest and costs. Kellywood's claim was founded on the amounts certified as due in terms of two interim certificates issued by the architect under the building contract between Shelstaton and Imprefed. In a separate application before the same Court Midrand applied for judgment against Shelfaerie for payment of a total amount of

R5 117 582,00, an order declaring the mortgaged property executable, interest and costs. Midrand's claim was similarly based on two interim certificates issued by the architect under the contract between Shelstaton and Group Five. The two cases were heard together by Leveson J who gave judgment for Kellywood and Midrand and granted the orders sought. Following petitions to the Chief Justice leave was given to the appellants to appeal to this Court against the judgments and orders of the Court a quo.

The two building contracts were the following: On 12 October 1990 a written contract was concluded between Shelstaton, as employer, and Imprefed, as contractor, which provided for the construction of the socalled Industrial Park Development at Midrand for a contract sum of R36 983 000,00.

The contract was the standard form of contract approved by the Institute of South African Architects and others (1981-1988 edition). On 8 May 1991 Shelstaton, as employer, and Group Five, as contractor, concluded a written building contract for the erection of a shopping centre at Midrand for a contract sum of R57 100 000,00. The conditions of contract governing the legal relationship between the parties to this contract can be taken to be identical to those in the first building contract. I shall refer to the two contracts as the Industrial Park Development and the Shopping Centre contract respectively.

In respect of each building contract Shelstaton was in default with the payment of interim certificates issued by the architect in terms of clause 25.1 of the contract. In the case of the Industrial

Park Development contract interim certificates no 9, issued on 5 July 1991 for the sum of R2 897 300,28 and no 10, issued on 2 August 1991 for the sum of R2 142 797,22, remained i unpaid after the time-limit provided in the contract for payment had expired. In the case of the Shopping Centre contract interim certificates no 6, issued on 20 June 1991 for the amount of R2 985 226,00, and no 7, issued on 22 July 1991 for the amount of R4 026 680,00, remained unpaid after due date. On 19 July 1991 Shelstaton drew two cheques, one for the amount of R2 897 300,28 in discharge of its indebtedness reflected in certificate no 9 issued under the Industrial Park Development contract, and the other for the amount of R2 985 226,00 in respect of its indebtedness reflected in certificate no 6 issued under

the Shopping Centre contract. Both cheques were stopped by Shelstaton before they were honoured. As will be seen later, the defences raised in the Court a quo that Imprefed had repudiated the Industrial Park Development contract and Group Five the Shopping Centre contract entitling Shelstaton to stop payment of the two cheques, were not persisted in on appeal.

Two surety mortgage bonds were thereafter registered to secure Shelstaton's indebtedness under the two building contracts. On 8 August 1991 Shelagatha caused a surety mortgage bond to be registered over certain immovable property in favour of Imprefed, in terms whereof Shelagatha acknowledged itself to be bound to Imprefed in the sum of Rl 500 000,00 as a continuing covering security "for and in respect of every indebtedness or

obligation of whatsoever cause and nature" which Shelstaton might from time to time incur to Imprefed, and a further sum of R300 000,00 as security for contingent payments, costs or outlays. Under "any indebtedness or obligation" were specifically included "negotiable instruments made, drawn, accepted, endorsed or otherwise executed" by Shelstaton. On 13 August 1991 Shelfaerie caused a surety mortgage bond to be registered over certain immovable property in favour of Group Five in terms whereof Shelfaerie acknowledged itself to be bound to Group Five in the sums of R4 500 000,00 and R900 000,00 in identical terms to those to which Shelagatha had bound itself to Imprefed.

On 19 August 1991 Shelstaton caused a letter to be addressed to the firm of attorneys acting for both Imprefed and

Group Five in which Shelstaton purported to cancel both building contracts. Imprefed and Group Five reacted by letter from their attorney dated 26 August 1991 in which it was alleged that Shelstaton had abandoned both building contracts before completion and had generally conducted itself in a way which showed a clear intention not to be bound to either contract and to repudiate its obligations thereunder. This repudiation was accepted and the contracts cancelled. The letter further stated that both building contracts were cancelled on the ground also of Shelstaton's breach in failing to pay the amounts due in terms of the interim certificates for more than seven days despite written notice to do so.

On 3 September 1991 Imprefed ceded its rights to its claims against Shelstaton to Kellywood Homes and on 19 September 1991

Group Five ceded its rights to its claims against Shelstaton to Midrand. The litigation to which I have already referred was then initiated.

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Mr Serrurier, who appeared on behalf of both Shelagatha and Shelfaerie at the hearing of the appeals, conceded for the purposes of the appeals that Shelstaton had no right to cancel either building contract and he further conceded the validity of the cancellation by Imprefed and Group Five on both grounds stated in their said letter of cancellation of 26 August 1991. It was further common cause that the interim certificates in question are true payment certificates and were not intended merely to evaluate work and material on hand. (Cf Simmons NO v Bantoesake Administrasieraad (Vaaldriehoekgebied) 1979(1) SA 940 (T) at 946F.)

It is convenient to deal with Mr Serrurier's argument only with reference to the Industrial Park Development contract. What is said in regard thereto applies equally to the Shopping Centre contract. For ease of reference I shall use the expressions "the employer" and "the contractor" when referring to Shelstaton and Imprefed respectively.

Mr Serrurier submitted that the contractor was not entitled to enforce payment under the interim certificates after it had cancelled the contract. He relied for this submission on the provisions of clause 23 of the conditions of contract and on the case of Thomas Construction (Pty) Ltd (in liquidation) v Grafton Furniture Manufacturers (Pty) Ltd 1986(4) SA 510 (N) which was upheld on appeal. The judgment of this Court is reported in 1988(2) SA

546(A).

Clause 23 provides for cancellation by the contractor and its consequences in the following terms.

"23. Determination by Contractor.

If the Employer does not pay the Contractor within the period stated in clause 25, and thereafter for seven days after written and registered notice from the Contractor fails to pay the amount due on any certificate of the Architect, or if the Employer interferes with or obstructs the issue of any such certificate, or if his estate is sequestrated as insolvent or, in the case of a company, it is placed under voluntary or compulsory liquidation, or if the whole or substantially the whole of the Works, other than Works in respect of defects under clause 13, is delayed under the provisions of clause 20, excepting local combination of workmen, strike or lock-out, for three months, the Contractor may by written and registered notice to the Employer or Architect determine the employment of the Contractor under this

contract, and thereupon, without prejudice to the accrued rights of either party, their respective rights and liabilities shall be as follows:

23.1

23.2 the Contractor shall be paid by the Employer:

23.2.1 the contract value of the Works completed at the date of such determination as aforesaid, subject to clause 10;

23.2.2 the value of work commenced and executed, but not completed at the date of such determination, the value being ascertained mutatis mutandis in accordance with the provisions of clause 10;

23.2.3 the cost of materials or goods properly ordered and delivered for the Works actually paid for by the Contractor, or of which he is legally bound to accept delivery, and on such costs being paid by the Employer the same shall become his sole property;

23.2.4 the reasonable cost of removal under clause 23.1;

23.2.5 any loss or damage caused to the Contractor owing to such determination as aforesaid;

> Provided that, in addition to all other remedies, the Contractor upon the said determination, may take possession of and shall have a lien upon all unfixed materials and/or goods intended for the Works, which may have become the property of the Employer under this contract, until payment of all monies due to the Contractor from the Employer....."

It is convenient at this stage also to quote the relevant provisions of clause 25 of the conditions of contract, in terms of which the architect's interim certificates were issued.

> "25. Certificates and Payments.
>
> 25.1 The contractor shall be entitled to receive from the Architect interim certificates at intervals not greater than one calendar month, a penultimate certificate and a final certificate (as more fully set out hereunder), stating the amount due to him and to payment of such amount by the Employer within the period set out in the attached schedule. The Architect shall notify the Employer of the

date and amount stipulated in each certificate at the time of issue thereof. If, after the expiry of the aforementioned period, the amount so certified has not been paid to the Contractor, the Employer shall be liable, without prejudice to any right the Contractor may have to determine his employment under this contract, to pay the Contractor interest on the amount so due,

calculated……

25.2.1 The amount so due as aforesaid shall, in respect of each monthly certificate, be a reasonable estimate:

23.2.6 of the total value of the work duly executed: and;

23.2.7 of the materials and goods delivered upon the site for use in the Works; assessed up to and including a date not more than seven days prior to the date of the said certificate, less the amount to be retained by the Employer, as hereinafter provided, and less any amounts previously certified under this clause: Provided that such certificate shall, subject to the provisions of clause 25.2.2 only include the value of the said materials and goods as and

from such time as they are reasonably, properly not prematurely brought upon the site, and then only if adequately stored and/or protected against weather and other casualties.

25.4

25.5 Upon the issue of the certificate of completion of the Works in terms of clause 13.4 and provided that the Architect has timeously received the documents referred to in clause 10.2 the Architect shall issue a final certificate of the value of the Works executed by the Contractor ...

25.6

25.7 A final certificate ... shall be conclusive evidence as to the sufficiency of the said Works and materials, and of the value thereof.

25.8

25.9 Save as aforesaid, no certificate of the Architect shall of itself be conclusive evidence that any Works or materials to which it relates are in accordance with this Contract."

Before dealing with the employer's defence based on clause 23 of the contract it is convenient to deal first with the legal nature of the instant interim certificates and with the defence based on the decisions in the Thomas Construction case.

It is clear from the provisions of clause 25 that an interim certificate, issued during the progress of an ongoing building contract, cannot be regarded as conclusive evidence of the sufficiency of the work and materials or of the correctness of their value as reflected therein. (Mouton v Smith 1977(3) SA 1(A) at 5 C-D.) It was common cause, nevertheless, that an interim certificate, duly issued in terms of the contract which is not paid by the employer within the stated time-limit, creates a debt due and as such affords the contractor a distinct cause of action in respect of which he could sue immediately without going beyond the certificate. See Mouton v Smith, supra, at 5 D-E and the

judgment of this Court in the Thomas Construction case, supra, at 562 E-F. The contractor's right which is embodied in the interim certificate clearly constitutes an accrued right. See the judgment of Nienaber J in the Court a quo at 515 D-F in the Thomas Construction case, supra.

In the Thomas Construction case an interim certificate was issued by the architect to the contractor under clause 25.1 of a building contract which was identically worded to clause 25.1 of the present contract. A few days later written notice was given to the contractor under clause 22 of the contract (which was the same as clause 22 of the present contract) to proceed with the works with reasonable diligence. Under that clause the contractor was required to comply with the notice within 14 days, failing which the employer was entitled to terminate the contractor's employment under the contract. A few days after the written notice was given

the contractor was provisionally liquidated. After the 14-day period had expired the employer cancelled the contract on the ground of the contractor's failure to remedy its breach in terms of clause 22. The employer's letter of cancellation stated that another contractor had been appointed to complete the works and that, in terms of clause 22.3.4, no payment would be made under the interim certificate until the work under contract had been completed. The contractor's provisional liquidators elected not to proceed with the performance of the contract but persisted in the claim for payment under the interim certificate, contending that the interim certificate provided the contractor with a self-sufficient cause of action, without the need to go beyond the certificate or to rely on the contract. The claim failed both in the Court a quo and on appeal.

In the Court a quo Nienaber J commenced his judgment by

applying the principle affirmed by this Court in Crest Enterprises (Pty)Ltd v Rycklof Beleggings (Edms) Bpk 1972(2) SA863(A) at 870 G-H to the facts of that case. That principle is to the effect that a claim ex contractu may survive cancellation of the contract if, prior to the cancellation, it was accrued, due and enforceable as a cause of action independent of any executory part of the contract. The learned judge held that the contractor's claim was not so independent of the executory part of the contract. His reasoning in arriving at this conclusion was as follows. He pointed out (at 517 A-B) that the interim certificate was not intended as compensation for a completed segment of the work. It was a medium for making progress payments which payments represented only an approximate and proportional value of the work done and material on site at a specified date. The purpose of a progress payment was to supply the contractor with working capital

as an advance on the contract sum and it was dependent upon the ultimate completion of the work (at 516 G-J). Payment on an interim certicate was thus not only made in respect of work done by the contractor but conditionally upon the contractor's willingness and ability to complete the rest of the work. In this way payment on an interim certicate was linked to what was at that stage the executory part of the contract. The right which had accrued was therefore not independent of the executory part of the contract (at 517 E-I). Nienaber J next dealt with clause 22.3.4 of the contract which provided that if the contract was cancelled by the employer on account of the contractor's breach of contract or liquidation, the employer would, inter alia, be entitled to employ another contractor to complete the works and until completion of the work no payment would be made to the contractor under the contract. The learned judge held (at 519 E-J) that those provisions were in

line with what he considered in any event to be the true position according to the law of contract.

On appeal the judgment in the Court a quo was upheld. With reference to the provisions of clause 22.3.4 it was held that payment under an interim certificate was necessarily a payment under the contract and accordingly fell within the purview of that clause which constituted a valid defence in favour of the employer against the contractor's claim based on the interim certificate (at 562 D-E). With regard to the nature of an interim certificate and the effect of a payment made in terms of it Botha JA, in delivering the judgment of this Court, said (at 563 E-H) -

> "... it was contended that payments under interim certificates were not to be regarded as advances on account of the ultimate contract price; that the sum certified was indeed to be regarded as compensation for a completed segment of the work; and that the sum certified was not to be treated as provisional and subject to adjustment and re-adjustment in later certificates. I have no hesitation in rejecting this entire

> line of argument, coupled with all the submissions made in support of it. Not only does it do violence to the fundamental nature of a building contract and the reciprocal obligations of the parties to such a contract; it flies in the face of the clear authorities cited and discussed by Nienaber J in the reported judgment at 516F-517D and 519D."

Botha JA further held that the principle enunciated in the Crest Enterprises case, which applied to all forms of breach of contract culminating in cancellation, afforded the contractor no avenue of escape from the fact that the contract had been cancelled or from the consequences of such cancellation, which included the coming into operation of the provisions of clause 22.3.4 of the contract (at 566 E-F). In so holding Botha JA rejected an argument by counsel for the contractor that the words "prior to" in the expression "prior to the cancellation of the contract" in the Crest Enterprises principle, meant that the ascertainment of the existence of an accrued and enforceable cause of action could be isolated

entirely from both the fact and the consequences of the cancellation of the contract. Dealing with this argument Botha JA also

warned against, what he called, the dangerous process of applying

a dictum in a judgment in another factual context not contemplated by the dictum (at 565 A-B).

In the present case Mr Serrurier has attempted to elevate to a general rule what was said about the nature of an interim certificate and the effect of a payment made in terms thereof in the Thomas Construction case. In so doing he has, in my view, done exactly what Botha JA warned against in the passage just referred to. The general rule contended for is that after cancellation of a building contract, regardless of the terms of the contract and who the defaulting party is, interim certificates previously issued in terms of the contract can no longer be enforced. In my view neither judgment in the Thomas Construction case

provides authority for such a general rule. What was said in that case related to a claim on a prior interim certificate by a contractor whose breach had caused the cancellation of the contract and who was unable to complete the work so that another contractor had to be engaged to do so. An innocent contractor suing on a prior interim certificate after he has cancelled the contract due to the employer's breach, is in an entirely different position. In the former case the contractor's right to remuneration is uncertain and can only be determined after completion of the work by another. He may eventually be found to be entitled to very little or nothing at all. In the latter case the innocent contractor is, upon cancellation, released from his obligation to finish the work and the employer has no further claim against him in this regard. The innocent contractor's right to remuneration is not conditional upon further performance under the contract and, while subject to final

adjustment, is not uncertain. The mere fact that it is subject to final adjustment does not, in my view, make the right dependent on any executory part of the contract. And I do not read either of the judgments in the Thomas Construction case as having decided that it does.

I come now to deal with the defence based on the provisions of clause 23, which provide for cancellation by the contractor in the event of the employer's breach of contract. The clause was clearly inserted for the benefit of the contractor. It facilitates both the cancellation of the contract and the contractor's claims for damages for breach of contract. Specific provision is made for the contractor's claims for damages under various heads (sub-clauses 2.1 to 2.5). As far as payment for the work done is concerned, provision is made for a final accounting. In terms of sub-clauses 2.1 and 2.2 the contractor is entitled to be paid the contract value

of the work completed at the date of termination as well as the value of work commenced and executed but not completed at the date of termination as actually measured and valued by a quantity surveyor in accordance with clause 10 of the contract. " Accrued rights" are specifically preserved. As I have said earlier, a contractor's rights which are embodied in interim certificates clearly constitute "accrued rights". The accrued rights must, of course, still be independent of the executory part of the contract in order to satisfy the Crest Enterprises principle, as Mr Gauntlett, for Kellywood, readily conceded. It is, however, significant to contrast the preservation of accrued rights in the event of cancellation by an innocent contractor, with the provisions of clause 22, which deal with cancellation by the employer due to the contractor's breach. Not only is there no corresponding preservation of accrued rights in clause 22, but clause 22.3.4

(which is identical to clause 22.3.4 of the contract in the Thomas Construction case) expressly provides that upon cancellation due to the contractor's breach he is not entitled to any payment until completion by another contractor.

Mr Serrurier contended that clause 23 substitutes a different formula for payment in lieu of the prior interim certificates. He submitted that clause 23 is a comprehensive provision as to the entitlement of the contractor after termination, ie to be paid the actual value of the work at the date of termination and that there is no provision that, in addition thereto, the contractor is still entitled to be paid amounts certified in interim certificates but not yet paid. He submitted that after cancellation the contractor has to bring all claims under clause 23 so that it cannot be said that his claims under any prior interim certificates are independent of the executory part of the contract.

I cannot agree with Mr Serrurier's submissions. I have already indicated that in the event of a contract being cancelled due to the employer's breach there is, in general, no reason to reconsider a prior interim certificate, except for adjustments. The final accounting provided for in clause 23 means no more, in my view, than that prior interim certificates are subject to adjustment, in the same way as if the contract had not been cancelled and the work completed in terms thereof. I can find no indication in clause 23 or in the rest of the contract to the effect that the innocent contractor's right under a prior interim certificate is made dependent upon the executory part of the contract in clause 23. Indeed, the provision in clause 25.1 that interest is payable by the employer on an interim certificate even after cancellation by the contractor, would indicate the contrary.

In the event of an overpayment to the innocent contractor on

the interim certificates, the employer will obviously be entitled to reclaim such overpayment from the contractor. I can see no inequity in that (cf the judgment of Nienaber J in the Thomas Construction case at 520 A-C). There is no defence in the present case that payment on the interim certificates will result in an overpayment. In my view it could never have been the intention that the innocent contractor should, after cancellation, lose his accrued rights embodied in prior interim certificates and that he should be limited to an eventual claim for damages, with all the uncertainty and delay involved in such a claim.

For the reasons stated I accordingly hold that according to general principles and in terms of the specific provisions of the contract, the contractor's right to payment under the interim certificates was independent of the executory part of the contract, and that it accordingly survived the cancellation of the contract.

It follows that both appeals must be dismissed with costs, such costs to include the costs of two counsel. In the Shelagatha appeal, Shelagatha is further ordered to pay the costs of the application to the Court a quo for leave to appeal, such costs to include the costs of two counsel, as well as the costs of opposition to the petition for leave to appeal. In the Shelfaerie appeal a similar order is made against Shelfaerie regarding the costs of the application to the Court a quo for leave to appeal and the opposition to the petition for leave to appeal.

W. VIVIER JA.

Joubert JA)
E M Grosskopf JA)
Eksteen JA)
Harms JA) Concur.