05 February 2021

THE ENFORCEABILITY OF PENALTY CLAUSES IN SALE AGREEMENTS

Many agreements to purchase immovable property contain provisions whereby the purchaser forfeits his deposit upon cancellation of the agreement. This occurs when the purchaser is in breach of provisions in the agreement and ultimately fails to remedy such breach.

In terms of the Conventional Penalties Act, a court may reduce the penalty, should it find that the penalty is not in proportion to prejudice suffered by a creditor due to breach and cancellation of the agreement. The penalty amount should represent the damages actually suffered by the seller.

A purchaser may approach the court to claim reduction of the penalty amount even though the agreement provides that a purchaser will forfeit his deposit should the agreement be cancelled due to his/her breach.

It is important that these provisions are not confused with 'rouwkoop'. 'Rouwkoop' is a clause that entitles the purchaser to legally withdraw from the contract by paying a sum of money. Should this happen, the purchaser will be acting in accordance with the terms of the agreement and his withdrawal will not constitute a breach of contract. This is clearly very distinguishable from a penalty clause which comes into operation only where there is a breach of contract. A penalty clause and rouwkoop clause can also not be combined (for example: any deposit paid will be forfeited as rouwkoop), as they are 2 distinct concepts. Rouwkoop is a predetermined amount specified in the agreement which a party can pay to withdraw from such agreement, while a penalty can still be disputed in a court and must be proportionate to the damages suffered.