Failed synallagmatic contracts : appraisal of the maxim "the party who has control and can insure against the loss should shoulder the risk"

Aimite Jorge
1 Introductory remarks

In enrichment situations arising from failed agreements the prevailing position in current South African law is that “if you have received a performance in terms of a contract which subsequently fails for whatever reason, you give it back if you still have it; if you cannot give it back, you are absolved, unless you were culpable in relation to the loss”. While on one analysis this position seems to serve the legal system in situations of failed agreements because it leads to certainty and predictability, it does not seem to always produce the most desirable results because it is prone to yielding unjust outcomes. The discussion that follows is an endeavour to deal with “failed agreements” in general and explores the applicability or non-applicability of the change-of-position defence in such circumstances. Firstly, the study briefly analyses the theoretical foundations on which are grounded both the unqualified adherence to the proposition that “whenever there is a bilateral agreement, the creditor always bears the risk of loss of the object of exchange unless the debtor was at fault” and the alternative theory of apportionment of losses which is at times applied in similar circumstances. The alternative theory is sometimes applied in English law. It must be noted, however, that although there are

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7 I would like to thank Professor Daniel P Visser (University of Cape Town) for commenting on an earlier draft of this article and Mr. Fritz (Deputy Dean of Law, University of Namibia) for proofreading the manuscript. All errors remain my own.
9 This is the position adhered to currently in South Africa Law. For detail on this position see Visser Unjustified Enrichment 475-500. For further details on the history and the evolutionary thinking of the “res perit domino” see Van der Bergh “Perfecta Emptione Pericullum est Emptoris: Why all the Fuss?” 2008 TSAR 613ff.
11 Visser articulates these two contentions in detail and deals with the pros and cons of each approach in his recent book, Unjustified Enrichment 475-500.
other related positions mostly suggested in common-law jurisdictions, they are not dealt with here because they are not pertinent to the purposes of this paper. The focus of the paper is on the aforementioned two approaches. The discussion not only scrutinises the grounds upon which both approaches are based, but also critically examines the desirability or the undesirability of each approach for current South African law. The argument also touches on the compatibility of each approach with the adoption of a general enrichment principle.

It also must be noted from the outset that several cases falling within this category are often borderline cases, and much of this discussion may traditionally not be regarded as part of the law of enrichment, or at least when the position is advanced that they are, some theorists resist the extension of enrichment liability to such situations. One of the arguments the opponents of the extension advance is that, if enrichment liability is extended to such cases, the resolution of some of the consequences of the failed agreements will inevitably bring with it the transposition of contract rules and mechanisms (or such resolution will still make reference to the contract) in the winding up process of such cases. However, although the arguments advanced by the opponents of the extension may sound strong at times, because it remains broadly true that the law of contract is concerned with the circumstances in which agreements are legally binding, it is equally logical to think that where such agreements are no longer binding for a variety of reasons, a different set of rules may apply. The application or applicability of these different rules, however, does not happen in a vacuum. General reference may still need to be made to the “contract” or the “supposed contract” for informative purposes, because that “contract” (which has now failed), or an “apparent contract”, constitutes the context in which the circumstances now giving rise to the other set of rules happened. That is all that is required and nothing more.

Given that the desirability or the undesirability of the defence of loss of enrichment being applied in such circumstances entails that the cause of action must first be characterised as arising in unjustified enrichment rather than in “contract”, the paper leans towards a unified approach in all cases of failed synallagmatic agreements. Considering, however, the vastness of the issues of failed agreements, the paper will only deal in some detail with one kind of ineffectiveness, namely, discharge due to impossibility of performance (frustration of purpose). Even then, the focus will mostly be on the risk allocation in cases of “loss” or “impossibility” of performance, with the objective of highlighting why it is significant to identify the person who has control and can insure against the loss. The argument is to a certain extent an appraisal of the approach suggested by Visser in his recent book on unjustified enrichment.6

Although it is generally admitted that an effective contract cannot found an unjustified enrichment claim,7 it is increasingly being acknowledged that to deny absolutely the availability of enrichment claims in the absence

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7 This statement is generally valid in both civil-law and common-law systems.
of termination of contracts “may neglect a small but theoretically important category of cases”. This is the case because, although the general rationale that an enrichment claim operating before the contract is declared “null and void” or it is “discharged” subverts the contract, this position would seem valid only to the extent to which a contract allocates the risk inconsistently with any duty to make restitution. As a result, one of the predominant approaches we come across in the last few decades, articulates the view that, except in the case of speculative contracts, it should not be assumed a priori, without more, that in contracts all risks have been distributed to one side or the other. That being the case, there might always be a gap in the contractual allocation of risk, which in turn might make room for adjustment either by applying the principle of unjustified enrichment or some other principle. Consequently, for some theorists it should, in principle, be possible to bring an enrichment claim where it would not reallocate risks or reassign value as an alternative to an action for breach of contract even before discharge. Nonetheless, despite the potential breadth of the issue, this paper, as mentioned, will only concentrate on failed agreements in general and specifically on failure of a contract due to frustration of purpose (or impossibility of performance). Other manifestations are not dealt with.

2 Ineffectiveness of contracts arising generally from failed agreements

As pointed out above, in cases of failed synallagmatic agreements South African law adheres to the following proposition:

“If you have received a performance in terms of a contract which subsequently fails for whatever reason, you give it back if you still have it; if you cannot give it back, you are absolved, unless you were culpable in relation to the loss”.

With this formulation, loss of enrichment, being a general defence under enrichment liability, might also be available in cases of failed synallagmatic agreements in so far as such failure is seen to give rise to enrichment liability. This position is fully stated, articulated and critically discussed by Visser. I refer the reader to that discussion for more details and nuances arising from such situations. What is discussed here is only whether it is a sound policy to

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8 See generally Beatson “Restitution and Contract: No Cumul?” 2000 Theoretical Inquiries in Law 83 86; Visser “Rethinking Unjustified Enrichment: A Perspective of the Competition between Contractual and Enrichment Remedies” 1992 Acta Juridica 203; Mead “Restitution within Contract” 1991 Legal Studies 172; Visser Unjustified Enrichment 61-155; Mason & Carter observe that “the fundamental point is that, as a general rule, restitutionary issues arise in respect of ineffective rather than effective contracts. Only rarely will the law of restitution operate in the context of an effective contract” (Mason & Carter Restitution in Australia (1995) 918).

9 Beatson 2000 Theoretical Inquiries in Law 94.

10 94-95.

11 Visser Unjustified Enrichment 475-500. For failed mutual contracts, and the contrary views expounded by other critics or those who share Visser’s position see more specifically pages 498-500 where Visser discusses them in detail, and where necessary he reconciles them with his position.
allow a general enrichment principle to always apply the defence of change-of-position when all the elements for establishing such defence are present regardless of the nature of the situation in which the claim arises. The reflection here will first focus on Visser’s suggested approach before advancing to a deeper analysis of some other interrelated problems.

Although it has long been established under South African law that enrichment law is a body of law separate from contractual obligations, it is still true, and unavoidable, that a contract lawyer cannot ignore unjustified enrichment law because that part of the law may and does solve certain problems not dealt with by the application of contract law. Such is the case, for example, where contract rules hold that there is no contract (for example, void or illegal contracts); and where agreements not recorded in due form (in writing, when required) are concerned. The same applies to many other analogous situations. In such cases, in South African law, enrichment rules are frequently applied to do justice between the parties in respect of performances rendered despite the invalidity. Hence, in the context of failed agreements, Visser summarises the South African position in this way:

“Here [South Africa], the person who makes the performance carries the risk. This state of affairs is brought about by the fact that the defence of loss of enrichment or change-of-position is available to each party. In other words, if you have received a performance in terms of a contract which is frustrated, you give it back if you still have it; if you cannot give it back (unless you were culpable in relation to the loss) you are absolved.”

Visser, however, thinks that this solution, though simple and sure, is not based on good philosophy. That is so because, says Visser, “the person who carries the risk has no control over the object”. Thus, Visser recommends that the model suggested by Hellwege should ideally be followed as the correct one; that is to say, “rather than res perit domino, the person who is in control of the object of the performance should bear the risk if it goes under”. A further advantage in structuring the law in this way, says Visser, is that “placing the risk in this way means that the person who is in control can

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15 Visser Unjustified Enrichment 498.
16 Visser Unjustified Enrichment 498. Visser also remarks that this position sometimes is justified by recourse to the maxim “res perit domino”, an explication that he finds unconvincing (Visser Unjustified Enrichment 498ff). He equally notes that the current South African position corresponds to the German model, Zweikondiktionenletheorie, in terms of which each party to a synallagmatic contract has his own claim against the other party. “In other words”, says the author, “the fact that you cannot give back what you have received is irrelevant because your claim for the return of the amount by which the other party had been enriched is completely independent from the claim of the other contracting party for that which he might have received from you” (499). Note however that according to Zimmermann at the time of his writing there appeared to be three theories vying for recognition in the aforesaid circumstances, namely, the Zweikondiktionenletheorie, the famous Saldtheorie and the Lehre vom faktischen Synallagma. Zimmermann “Unjustified Enrichment: The Modern Civilian Approach” 1995 Oxford JLS 403 413 n 17. Whether one of them has now triumphed is still to be ascertained. For a more detailed discussion of these theories see Zimmermann & Du Plessis “Basic Features of the German Law of Unjustified Enrichment” 1994 RLR 14 40ff and other sources cited there including König Ungerechtfertigte Bereicherung: Tatbestände und Ordnungsprobleme in Rechtsvergleichender Sicht (1985) 81ff.
18 Visser Unjustified Enrichment 499.
insure the object of the contract”. This model also “works with the identity of risk and insurability”, which also implies that “it recognises the autonomy of each contracting party to be able to make the decision whether or not to take the risk of making disbursements in preparations for performance”\(^\text{19}\). Put plainly, the defence of change-of-position is proscribed in situations of “synallagmatic frustrated agreements”. Hence, where “you have received any performance in terms of the frustrated contract you give it back; if you cannot give back what you received, you give back the value”\(^\text{20}\).

The issues that Visser’s model raises are indeed the identification of risk and its insurability. That being the case, it is vital to know what is understood by risk under contractual obligations. Is the party in control always the same as the one who can insure against the loss? Under what circumstances is risk assignable to one party? Is risk uniform or multiformal? Does the nature of the risk and its nuances matter? Which factors influence the decisions to take or not to take the risk of making disbursements in preparations for performance? At what stage must the conclusion of an insurance contract occur? Or, at what stage will the object of the contract be insured?

Depending on the angle of analysis one takes, risk can have differing nuances. In one sense akin to an economic analysis, risk under contractual obligations may be conceived as the factor that is equal to the probability of an event multiplied by its cost. The fact that people are willing to pay to avoid risk shows that risk is a cost. Generally, however, risk denotes the probability of specific eventualities. Its precise definition varies with the field in which it is used\(^\text{21}\) and within certain fields with the complexity of the endeavour. In some areas, the notion of risk is independent from the notion of value, while in others it is intertwined with that notion.\(^\text{22}\) Where risks constitute eventualities independent of the notion of value, such eventualities may have both beneficial and adverse effects. However, in general usage, risk

\(^{19}\) 499.
\(^{20}\) 499.
\(^{21}\) For example, the notion of risk in engineering is somewhat different from its counterpart in finances and that of statistics varies considerably with that of insurance, and so on. Commonly, in engineering the simplest definition is said to be the probability of an accident multiplied by the losses per accident, or is simply the probability of a risk occurring times the impact of such risk occurring. But as the engineering fields diversify and more complex endeavours are considered, the concept of risk becomes also more sophisticated, especially in potentially dangerous industries. In financial matters, risk is often understood as the unexpected variability or volatility of returns and it includes both potential worse-than-expected as well as better-than-expected returns. In statistics, risk is mapped to the probability of some event which is seen as undesirable. Usually, the probability of that event and some assessment of its expected harm must be combined into a believable scenario (an outcome), which combines the set of risk, regret and reward probability into an expected value for that outcome. A contractual risk, in several scenarios is associated with either the possible failure of contracting parties to deliver products, services or devices or (money) to the agreed cost, specification or at the agreed time, or with the adjacent notions of physical and natural “disasters”, such as theft, vandalism, arson, building related risks, storms, floods, droughts, or other weather related occurrences etc, or socio-cultural and regulatory occurrences such as changes in legislations, political regimes, national or multi-national regulatory bodies, or market changes, fundamental changes in supply and demand functions and global prices for commodities. For the concept of risk in the financial world see generally Bernstein Against the Gods: The Remarkable Story of Risk (1998).

refers more to potentially negative impacts that may arise from future events, both foreseen and unforeseen if they materialise. And, as such, there are some characteristics of value attached to it. Therefore, the concept of risk is complex. But before turning to the analysis of some of the preceding questions about risk and ancillary issues they may raise, a brief overview of the history of the maxims “res perit domino” and “periculum est emptionis” as well as the current South African doctrine of impossibility of performance in general are in order.

2.1 On “res perit domino” and “emptione periculum est emptoris”

Since Roman times a difficulty developed in the law of obligations in general on the correct approach to deal with the destruction of a thing where its ownership might have vested on one party, but its control still exercised by another. This is a simplified way of putting a very complex problem. Detailed discussions, however, of the intricacies and interactions of the maxims and the issues involved if one legal system opts exclusively for a “res perit domino” approach to the exclusion of the “periculum est emptionis”, or if the “periculum est emptionis” is sanctioned, are widely documented. It is not the purpose of this paper to go into the fine details of these issues. Very good starting points for derived questions are found in comprehensive surveys, published in different periods, of the matter. Among the surveys or analyses, the writings of Ernest, Van der Bergh, MacCormack and Lawson are good precursors to subsequent issues. In any event, the content of the maxims will now be discussed briefly.

Res perit domino literally means “the thing is lost to the owner”. This maxim is used to express the idea that when a thing is lost or destroyed, it is lost to the person who was the owner of it at the time. For example, an article is sold; if the seller has perfected the title of the buyer so that it is his, and it is destroyed, it is the buyer’s loss; but if, on the contrary, something remains to be done before the title becomes vested in the buyer, then the loss falls on the seller.

Periculum est emptoris, which is a short form of the full maxim “perfecta emptione periculum est emptoris”, means that “the risk passes to the purchaser from the moment of contracting”; that is to say, if the seller has perfected the title of the buyer so that it is his, from that moment there is an emptio perfecta, and therefore risk passes to the purchaser from the moment of contracting. Thus, if the thing was, for example, accidentally damaged, or wholly or partially ceased to exist after the conclusion of the contract, but before delivery, the seller merely has to deliver what is left, but the purchaser

24 Ernest “Periculum est Emptoris” 1982 ZSS 225.
still has to pay the price. The purchaser is only redeemed if the loss, damage or destruction is due to the seller’s fault.

Further details of the *periculum est emptoris* approach are also evident in the Roman *Institutes* and the Justinian Digest itself, among other texts. In terms of the Roman *Institutes*,

“once the sale is contracted (which takes place as soon as there is agreement on the price in the case of sale without writing), risk in the thing sold falls at once on the purchaser, even though the thing has not yet been delivered. In such a case the loss is that of the buyer who is bound to pay the price, although the thing no longer exists. The vendor is safe in respect of anything which happens without any fraud or negligence on his part.”

The provisions of the *Digest* are to the same effect as the Roman *Institutes*. The *Digest* further adds that

“it is essential to know when a sale is perfecta because then when we know who bears the risk in the thing; for once the sale is perfecta, the risk is on the purchaser. And if the thing sold be identified, what it is, its nature, and quantity, the price be fixed, and the sale be subject to no condition, the sale is perfecta”.

The presence of these two maxims and the underlying issues they embody in the legal discourse of various legal systems is a clear manifestation of the fluidity of the boundaries between the various branches of the law of obligations and the private law in general. The fluidity of the boundaries between unjustified enrichment, property law, contract (and even the law of delict or tort) is, for example, apparent in the historical difficulty in explaining why the Romans themselves who stipulated that “*res perit domino*” made an exception in cases of contracts of sale with the famous “*periculum est emptoris*”. Several authors throughout history have offered different interpretation for the reasons why the “*emptione est emptoris*” was needed. Some think of it as an anomaly, while others think of it as justified in the light of the nature of the contract itself or due to the “underdevelopment” of some principles in the legal system as a whole at the time when the maxims were formulated or for other reasons. The rationale of the “underdevelopment” of some principles in the legal system as a whole can probably be discounted as somewhat unsatisfactory, because modern legal systems which are very complex still manifest the issue. Such is the case of French law, for example, which in one way or another deals with

28 D 18 6 8. See also Van der Bergh 2008 TSAR 624.
29 I 3 23 3 The Institutes of Justinian (tr Thomas (1985)).
30 D 18 6 8pr.
31 D 18 6 8pr (Krueger & Watson (eds) The Digest of Justinian V II Mommsen (tr Watson (1985)); see also Van der Bergh 2008 TSAR 624ff for further details.
32 Windscheid, for example, justified the Roman exception in the following terms:

“The reason for this exceptional provision is to be found in the fact that the declaration of intention to sell is a declaration of intention to alienate. That means that its content is not so much that the seller binds himself to surrender the thing sold, as rather that he actually surrenders it. In consequence of this characteristic of the declaration of intention to sell, the thing sold is treated by law, so far as the relation of the seller to the buyer is concerned, as though it had already been severed from the seller’s estate and passed into the buyer’s. (…) The reason for this rule is the alienatory character of sale, which has led to the point that the thing sold, so far as the relation as between the parties is concerned, is regarded as being, even without delivery, severed from the seller’s estate and transferred to the buyer’s” (Windscheid *Lehrbuch der Pandektenrechts* (1906) 330 as cited in Lawson 1949 LQR 361). But it is also plain that Windscheid’s interpretation has not been well received.
the issues under article 1583 of the Civil Code. The common law has also not escaped these difficulties either.33

In South Africa there still is no obvious consensus on the right explanation of the reasons of the maxims in the law as evidenced by Pahad v Director of Food Supplies & Distribution34 (“Pahad”) While to some the rule of risk in sale, pericullum est emptoris, is an exception to the res perit domino, the view of the counsel (approved by Van der Heever JA) in Pahad’s case peremptorily says that:

“There is no general rule of Roman-Dutch Law res perit domino; the rule of risk in sale is not an exception to a general rule res perit domino. The general rule of risk in Roman-Dutch Law of an individually determined thing, ie species, is pericullum creditoris est or species perit ei cui debitur, sale being the foremost example of a transaction in which this rule operates. The maxim res perit domino or damnum sentit dominus is not found in the Corpus Juris Civilis”.35

Van der Heever JA sanctions counsel’s view on the matter by saying that

“I agree with counsel that there is no general rule of law to the effect that res perit domino. The maxim does not contain a principle of law; it is merely a self evident platitude and subject to a number of exceptions”.36

In demonstrating the applicability of the exceptions the judge adds: “a party to a contract may safeguard his interests by seeing to it that adequate provisions are incorporated in it, for conventio legem dat contractui”.37

Meanwhile Van der Bergh,38 discussing Roman law sources and by implication Roman-Dutch law, manifests the view that in cases of sale “only when the object sold had been damaged, lost or destroyed due to an event which nobody could have prevented, did the purchaser have to pay the price without receiving anything (or damaged goods)”. Given that such situations arose from failed synallagmatic contracts, Van der Bergh also found that in classical Roman law “the two performances, however, could be set off against each other: the purchaser’s claim was then limited, practically, to the difference by which his interesse exceeded the as yet unpaid purchase price”.39

Let us now consider the application of the doctrine of impossibility in South African law.

2.2 Impossibility of performance in South African law

One of the main differences between common-law and civil-law systems on the doctrine of impossibility of performance comes down to the primary remedy for breach each system subscribes to. On the one hand, if a system

33 For details on the difficulties arising on the issue in common law jurisdictions see generally Lawson 1949 LQR 352.
34 Pahad v Director of Food Supplies & Distributions 1949 3 SA 695 (A).
35 697.
36 709.
37 711.
38 Van der Bergh 2008 TSAR 630.
provides that its primary remedy is specific performance,\(^{40}\) then, as a logical consequence, if performance of the obligation becomes impossible, the obligation is discharged.\(^{41}\) That is so because the courts cannot enforce an obligation that is impossible - *impossibilium nulla obligatio*.\(^{42}\) On the other hand, if a system subscribes to the damages (compensation) approach as the primary remedy for contractual breach, save exceptions, then on the occurrence of the “*impossibilium*”, the value can always be given, unless it is entirely infeasible. South Africa being a mixed legal system, where does it stand between these two approaches?\(^{43}\)

It is well established under South African law that the primary remedy upon breach is specific performance, which is the logical consequence of the principle *pacta sunt servanda*. If that [specific performance] is no “longer possible” or it would be unreasonable to demand enforcement, then an award of damages is the next step. This also aligns with the principle of good faith in contract. However, one must be aware that not all contracts are equal in nature, for some are of a personal nature, where a specific thing which is the subject matter of the contract may have been destroyed; in other cases the alleged impossibility is brought about by operation of law and there are even instances in which the impossibility is caused by the promisee himself, but where he is not at fault. In all these circumstances the courts may follow different approaches to deal with the specific case of impossibility of performance.\(^{44}\) However, it may be said that under South African law, a supervening impossibility, in general, discharges the obligations of both parties to the contract if the impossibility is complete, ie it affects the obligation as a whole, whatever type of contract is involved. It extinguishes the parties’ obligation by operation of law.\(^{45}\) Therefore, if the obligation that would compel the defendant to give up the enrichment is extinguished by operation of law on the occurrence of a supervening impossibility, its effect is the same as an acknowledgement of a change-of-position exonerating the defendant from liability. Put differently, in such circumstances, the creditor ordinarily bears the loss, if the thing does go under.


\(^{41}\) Where performance of a contract becomes impossible after it was entered into, the general rule in terms of Roman law is that it then ceases to be binding. See for example *Wilson v Smith* 1956 1 SA 393 (W) 396ff.

\(^{42}\) D 50 17 185 and also D 45 1 140 2, especially as applied in *Wilson v Smith* 1956 1 SA 393 (W) 396. See also *Bischofberger v Van Wyk* 1981 2 SA 607 (W) 610-612 discussing the different approaches between Civil law and English law on the application of the “supervening impossibility of performance”.

\(^{43}\) For some early interaction between the views expressed in the South African sources and the English doctrine of impossibility in courts see the case of *Herman v Shapiro & Co* 1926 TPD 367 372-373. See also *Peters, Flammant v Kokstad Municipality* 1919 AD 427; *Benjamin v Myers* 1946 CPD 655; *Rousouw v Haumann* 1949 4 SA (C) 796 799-801.

\(^{44}\) See generally Ramsden *Supervening Impossibility in South African Law of Contracts* (1985) 46-58. Ramsden offers several references in the Digest for the application of the principle to specific areas of law, as well as references to Roman-Dutch and other European authors on the subject.

\(^{45}\) Voet 18 6 2; 19 1 14; Grotius *Int* 3 19 12; 3 47 1; 3 47 3; *Justianian Digest* D 13 1 20. Note, however, that under French law, supervening impossibility does not necessarily have the effect of discharging the contract. This French view is based on Pothier *Obligations* 3 6 2 621; 3 6 3 622.
Is there anything wrong with this approach? Before I address this question, some brief remarks on the insurance agreement in general will be made.

2 3 Insuring against the loss

2 3 1 General considerations

Because the maxim under appraisal, “the party who has control and can insure against the loss should shoulder the risk”, contains an insurance segment, a few words must also be said on the insurance agreement and on the insurable interest generally that may provide some insight into understanding the maxim.

The essence of insurance is to provide protection against the risks of uncertain events befalling the insured, normally events that would be adverse to him. The concepts of risk and/or loss are fundamental to an insurance pact. Nonetheless, there are a number of general points of universal application that need to be noted beforehand. Such points may well apply regardless of whether the loss appears to be covered as a matter of construction of the contract or not.

Firstly, subject to important qualifications, it is generally acknowledged that the fact the loss is occasioned by the negligence of the insured is usually irrelevant, but insurance does not cover losses deliberately caused by the insured. One of the important qualifications is that the insurance policy may objectively exclude the insurer’s liability in respect of negligence, by imposing on the insured an obligation to take reasonable care. Secondly, although the notion of insurance interest (the notion will be described in detail further below) that is central to an insurance agreement gravitates around “loss” understood in its various forms, generally there exist two kinds of insurance, namely, an indemnity insurance and a non-indemnity or contingency insurance (Only the indemnity insurance is relevant for our purpose. I merely refer to the contingency insurance in passing.) These two types of insurance have specific characteristics which may not necessarily be shared between them. In this regard, certain perils are never covered by an indemnity insurance. Primarily these perils are wear and tear and inherent vice. In other words, what occurs and happens naturally. Simply put, these perils are not fortuitous events and therefore are not capable of being covered by an insurance contract, the essence of which is to cover uncertain risks. So, for example, decay in food or the rusting of a motor-vehicle or the natural wear of tiles on a roof cannot be insured against. This general rule, however, does not apply in cases of contingency insurance, because such cases admit certain perils which are not fortuitous events. One of the major exceptions is certainly in the field of life insurance contracts. A life contract obviously covers the natural process of dying. The same is also applicable to a health insurance contract which also covers what may be an inevitable illness.46 Apart from these and few other instances, the general rule still applies.

Thirdly, there is a relation between insurable interest and indemnity as an explanation for an insurable interest in the case of indemnity insurance. In addition to this relationship, the notion of indemnity also brings with it another characteristic on the insurance pact. An assured, subject to the express terms of the policy, can only recover up to the full amount of the insurable value of his particular interest in the subject matter insured.47

Be that as it may, in the contract of insurance in general, the insurer takes upon him the risks to which the subject of the insurance is exposed, and agrees to indemnify the insured when a loss occurs. This norm applies equally in all sorts of insurances, be they cases of maritime, terrestrial insurance, as well as other forms of insurance. But thereafter there are variations in some aspects of the insurance contract according to the branch of the insurance aspect to which the principle applies. In any event, most insurance contracts entail a loss prevention aspect. Such loss prevention may be directed at financial loss or safety issues. It may equally comprise a “systematic approach to preventing hazardous events or minimizing their effects”.48 In whatever way loss prevention is seen, it generally also embodies a form of risk management, which need not necessarily be quantitative.

2.3.2 Insurable interest

One of crucial issues in the treatment of an insurance agreement is the identification and characterization of the insurable interest.49 Generally understood, an insurable interest is the object of the insurance contract, that is, the interest for which the insurer undertakes liability. There are various approaches and different trends of thought in defining and identifying an insurable interest, but ultimately all instances of insurance or insurable interest are tied to the idea of “loss” in its many forms.50 Because an insurance interest is a basic requirement of any contract of insurance, 51 unless it can be, and is lawful waived, it is also generally considered that, at a general level, it means that the party to an insurance contract who is the insured (or

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49 See for example Manderson T/A Hillcrest Electrical v Standard General Insurance Co. Ltd 1996 3 SA 434 (D) 439F-G, where McCall J said “the problem of identifying and defining an insurance interest is a vexing one”. Gordon & Getz On the South African Insurance Law 4 ed (1993) 96 put the problem in this way: “A definition of insurable interest, broad enough to embrace the immensurable cases it should include and precise enough to be of value, is difficult to supply”. See similar problems arising in English law in Birds Birds’ Modern Insurance Law 68-69.
50 An old Transvaal decision put the matter of insurable interest in these terms: “If the insured can show that he stands to lose something of an appreciable commercial value by the destruction of a thing insured, then even though he has neither a jus in re nor a jus ad rem to the thing insured, his interest will be an insurable one” (Littlejohn v Norwich Union Fire Insurance Society 1905 TH 374).
51 See generally Hosten, Edwards, Nathan & Bosman Introduction to South African Law and Legal Theory (1977) 564; Reinicke & Van der Merwe General Principles of Insurance Law (2002) § 52. See also Midgley “Enforcing Insurance Contracts: Insurable Interest and Stipulatio Alteri” 1986 SALJ 18. Note, however, that there is no unanimity in South African law as to the exact weight the notion of an insurable interest plays in the contract of insurance. For some it is simply a policy tool, while for others it is the very essence of an insurance contract. Contrast for example the view expressed in Reinicke & Van der Merwe General Principles (2002) 610 and those of Midgley 1986 SALJ 19.
a policy-holder) must have a particular relationship with the subject matter of the insurance, whether that is a life or property or a liability to which he might be exposed. If there is no such relationship the agreement is vulnerable to be construed as a wager. Very often, however, the questions that arise are mostly whether there are qualifying conditions and whether the perceptions of loss may be influenced by external factors. On one approach, insurable interest is generally described as including “any lawful and substantial economic interest in the safety or prevention of property (or other right) from loss, deterioration or pecuniary damage”. This is essentially a pecuniary interest approach. Currently, however, there are, among others, two further formulations arising from the legal discourse: one of them is sometimes termed a “legalistic approach” and the other a “pragmatic commercial approach”.

In short, the legalistic approach defines insurable interest as based on legal rights and obligations in, about or relating to the subject matter insured. The relationship between the assured and insured subject matter must be founded on a legal nexus. On this legalistic approach it is also the case that the legal right or obligation must be “existing”: an “expected” or “future right” or obligation is insufficient to found an insurable interest. A mere hope or expectation, however compelling, of acquiring a future right or becoming subject to an obligation does not establish an interest. Consequently, a future buyer of goods has generally no insurable interest in the goods. However, the limitation highlighted here relates clearly to the time of loss. For example, there is generally nothing to preclude a future buyer of goods from entering into an insurance policy. But if he remains a future buyer at the time of loss, he has no interest in the goods and cannot recover under the policy. Nonetheless he does have, of course, an interest in the pecuniary risk that the goods may not be delivered. However, when a legal interest is established, it will support an insurable interest notwithstanding that it may be partial, or contingent.

The underlying idea behind the legalistic approach to an insurable interest is the notion that an insurable interest is “a right in the property, or a right derivable out of some contract about the property, which in either case may be lost upon some contingency affecting the possession or enjoyment of the property”, as an old English case put it.

The pecuniary interest approach is a much wider factual view to the question of insurable interest because the emphasis is placed wholly on the pecuniary interest; that is to say, the approach is “free” from the additional constraint of having to prove that the pecuniary interest arose from the assured legal right or its relationship to the subject matter insured. Therefore, in contrast to the legalistic approach, this approach bases its insurable interest test on the single factual matter element of pecuniary interest, which, in this context, means that the risk of loss is capable of being valued in monetary

52 Thomas Marine Insurance 31.
54 Thomas Marine Insurance 32.
55 33.
56 Lucena v Craufurd case (1806) B & P (NR) 269, per Lord Eldon.
terms. The fact that such a valuation may on occasion be exceptionally difficult to make does not disqualify the approach, because it runs parallel with the fundamental economic nature of the insurance contract which is to indemnify an assured for direct and indirect pecuniary losses. For some analysts, the attraction of the pecuniary interest approach lies in the fact that it renders the test of an insurable interest less technical and legalistic. It seems to give the law a desirable flexibility. It broadens the range of legitimate insurance without necessarily undermining considerations of public policy. However, the approach is prone to several difficulties. One of them is the fact that if it is not clear what degree of evidence is required to establish an insurable interest, no one will know exactly what the content of the insurance is. For this reason, it is thought that the pecuniary interest theory is not a stable formulation and distorts certain factual scenarios. It is vulnerable to attracting multitudes of shades of meaning and ultimately to obliterating the insurance pact itself. Because this approach does not delimit its boundaries, it encourages the parties to an insurance contract to become ambitious in their claim on an insurable interest, which in turn may generate more dispute and litigation.

The “pragmatic commercial approach” to an insurable interest is not really a well defined approach yet. However, recently, now and then commercial considerations creep into the judicial perception of insurable interest. In one sense these commercial matters take the subject beyond a purely legalistic approach. By doing so they bolster the factual pecuniary interest approach to an insurable interest. Despite this possibility, it can, however, be said safely that these commercial considerations are, at present, subsidiary or contributory only to the pecuniary interest approach. That is so because once a pecuniary interest is established the fact that there also exists a supporting commercial dimension adds considerable weight to the argument that the pecuniary interest should be recognised as establishing an insurable interest. But this “pragmatic commercial approach” is equally vulnerable to being accused of facilitating the introduction of wagering contracts into the realm of insurance law. The validity of this approach can only be sanctioned if it can be shown that the assured has indeed a sufficient interest to prevent the contract of insurance being construed as a wager. Otherwise, the approach is a nonsensical one.

In sum, the proper understanding of an insurance agreement depends to a large extend on the proper construction of the object of the insurance itself. If one takes a strict approach to the notion of an insurable interest, the outcome might be an undesirable one, because the strict interpretation may be “incorrect” and undermine the full scope of an insurance agreement. That is the case because an insurable interest does not seem to be as narrow as the notion of a “loss or diminution of any right recognised by law or in any

57 Thomas Marine Insurance 34-35.
58 36.
59 36-37.
60 37-39.
legal liability, but it is rather more in line with the economic interest of the insured”.61 The notion of “interest” seems less encompassing than that of a “right”. Therefore, under this understanding, the notion of insurable interest should be wider in its ambit as well. In order to reach the wider scope of the notion of insurable interest and consequently the insurance agreement itself, it is crucial to analyse the intention of the parties in identifying an insurable interest and therefore avoiding confusion between an insurance agreement and a mere wager. Because a wager is a situation where the risk of loss arises from the very making of the agreement, it is clearly distinguishable from an insurance contract (especially an indemnity insurance) in terms of which the contract is aimed at indemnifying the insured against loss of something already possessed.

In essence, the ultimate conclusion is this: Because the concept of insurable interest is inextricably interwoven with the question of loss, it is equally logical to think that the interest theory prevalent in current South African legal discourse has some merits. It emphasises that the real purpose of the theory is to assist the parties in ascertaining a loss which could then be compensated. The loss referred to in the old Transvaal case of Littlejohn v Norwich Union Fire Insurance Society62 (a case which is still authority on the concept of insurable interest) has been described to mean a “loss with a real value in trade or commerce”.63 While there is a contention to the effect that “neither a ‘mere expectation’ unaccompanied by any present legal right nor ‘a right’ binding only in honour will constitute an insurable interest”,64 a contingent right is arguable insurable.65

In whatever way the notion of an insurable interest is understood, most insurance contracts will always entail a loss prevention aspect. As said earlier, such loss prevention may be directed at financial loss or safety issues. It may equally comprise a “systematic approach to preventing hazardous events or minimizing their effects”.66 Because the average individual or entity is neither risk neutral nor indifferent to changes in their wealth, but ordinarily “risk averse” at some level of their wealth, and given that risk aversion can be described as a dislike of uncertainty about the extent of losses, the degree to which individuals dislike that uncertainty (and hence how much they will pay to get rid of it) depends on the size of the loss in relation to their total wealth.67 Put differently, people will always tend to allocate their resources optimally and prevent their wealth being depleted by unforeseen events. To do so they will very often resort to insurance.

62 1905 TH 374.
63 Manderson T/A Hillcrest Electrical v Standard General Electrical Insurance 1996 3 SA 434 (D) 442C-F (per McCall J).
64 Gordon & Getz South African Law of Insurance 97.
65 See, however, doubts of this approach by De Villiers in Phillips v General Accident Insurance Co SA Ltd 1983 4 SA 652 (W); Steyn v A4 Onderlinge Assuransie Assosiasie Bpk 1985 4 SA 7 (T).
67 22.
2.4 Risk allocation: “the person who has control and can insure against the loss”

2.4.1 A brief overview of Visser’s approach

Thus far South African law, as far as the passage of risk in general is concerned, adheres unqualifiedly to the view that “res perit domino”. Based on this view it is generally thought, for example, that in sales contracts “the risk passes to the buyer the moment the contract is perfecta and if the object of the sale is destroyed before it has been transferred to the buyer, the latter cannot reclaim the price that he paid unless the destruction was the fault of the seller”. Scrutinizing this aspect of the law, Visser contends that this position has always known exceptions. That is so because if one considers that “all payments in terms of reciprocal contracts have an unstated future purpose hovering over the primary purpose to fulfill an obligation: namely that the other party will also perform”, it is also logical to think that there will always be ways of fulfilling that future purpose, which will ordinarily be the payment of the value if performance in the agreed “species” or “manner” cannot be fulfilled.

The current approach being inadequate, Visser then asks whether the law should move towards apportionment of losses in cases of supervening impossibility outside what is achievable under the principle of unjustified enrichment as tempered by the loss of enrichment defence, or if that is a bridge too far, whether the application of the condictio sine causa specialis should be adapted in any way.

In answering these questions, Visser argues that “it is not appropriate to make apportionment of losses a goal of the winding up of frustrated contracts, neither is it appropriate to make the change of position defence available to frustrated bilateral contracts”. Visser also thinks that “loss apportionment” is sometimes defended to protect the “reliance interest” of the parties, but he questions the soundness of that approach in cases of frustration by supervening impossibility, save where the contract is divisible and parts of which were capable of having been performed independently, for, says Visser, “one might

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68 Visser Unjustified Enrichment 484.
69 De Vos expressed such a view in this way: “In Roman-Dutch law, with its relatively well-developed contract system, impossibility of performance as a result of casus fortuitous or vis major arising subsequent to the conclusion of the contract extinguishes the obligation to perform in most cases, (with the result that that which had already been performed can be reclaimed), but that there was an exception in regard to the return of that which had been performed in term of a contract which in Roman law had been innominate real contract” (De Vos Verrykingsaanspreeklikheid in die Suid-Afrikaanse Reg 3 ed (1987) 64 (Visser’s translation); See also Visser Unjustified Enrichment 484-485.
70 Visser Unjustified Enrichment 484.
71 The risk with this, however, is that if “the substitute performance” is radically different from the one agreed upon at the conclusion of the contract, we may be entering the territory of a different contract, and if the court were to substitute for the parties one performance by another, it might be accused of making the contract for the parties, thereby imperilling the voluntariness of contractual agreements.
72 See also Krebs who argues that “where exchanged performances are concerned, there is a general agreement that the change of position defence needs to be modified or disregarded completely” (Krebs “Stable Claims & Stable Defences - Change-of-Position and Disenrichment in England and Germany” in Schrage (ed) Unjust Enrichment and the Law of Contract (2001) 295 311).
argue that it is not the contract as such that is being relied upon, since there is no contract”.
However, there is no unanimity on this last categorization.
As there is no clear-cut answer, Visser then suggests that the way forward is placing the risk on the person who has control and can insure against the loss. In essence, Visser’s suggestion is to the effect that there must be a “judicial identification” of the “superior” risk bearer at the moment the loss occurs, and therefore, there should be no pre-determined liability in cases of “impossibility of performance” due to frustration. In other words, the principle “res perit domino” should not be accepted without exception. In order to make his point clearer, the author illustrates the argument with the following example:

“A and B have a contract of sale [of a horse]. B has transferred the horse to A; the full price is already payable but A has so far paid only half. A and B are in different countries and the contract is frustrated by an outbreak of war between them. The war destroys the horse”.

With this illustration Visser argues that “if A sues for the return of the payment that he has made (the amount by which B can be said to have been benefited), B has to give the value of the horse which he is unable to return. If B sues A for the return of the horse, he must give back what he received”. At this point, Visser enters the realm of risk insurance in the illustration process before he concludes the argument. So he continues explaining that “if A has not insured the horse, the fact that the value received is the measure of enrichment means that he will be out of pocket, but because he was able to insure it and elected not to do so makes it completely unobjectionable that he should shoulder the loss”. Obviously, there are exceptions to every rule, and according to Visser, the only exception to the principle that each party must restore what they received, or its value, is “where the loss would also have happened if the enrichment creditor had had it under his control, and it is not an instance where it is customary for the enrichment creditor to insure the object even though it is not under his control”. On the other hand, continues Visser:

“If B has spent the money that he received while it is still possible for the contract to be frustrated, the same principle will mean that he will be out of pocket, but the fact that this outcome is in accordance with recognizing his autonomy in determining the degree of risk that he wishes to take, also makes it appropriate that he should bear this risk”.

73 Visser Unjustified Enrichment 496.
75 This example is the same as that used by Hellwege “Unwinding Mutual Contracts: Restitution in Integrum v the Defence of Change-of-Position” in Johnston & Zimmermann (eds) Unjustified Enrichment 272 and Hellwege Die Rückabwicklung gegenseitiger Verträge als einheitliche Problem (2004) 130ff.
76 Visser Unjustified Enrichment 500.
77 500.
78 Visser Unjustified Enrichment 500.
79 Visser Unjustified Enrichment 500; also citing Hellwege’s Rückabwicklung 130, who also cited Flume “Der Wegfall der Bereicherung in der Entwicklung vom Römischem zum Geltenden Recht” in Schwartz (ed) Festschrift für Hans Niedermeyer zum 70 (1953) 103 172ff (Göttinger rechtswissenschaftlichen Studien 10).
80 Visser Unjustified Enrichment 501.
The person “who has control and can insure against the loss”:

an appraisal

Visser’s argument presented above is concise, articulate and clear; it needs no further glosses to understand it. The pros and cons of his approach are clearly set out in his own argument and explanations, a task that he did thoroughly and persuasively. The further question that however arises is whether the suggested approach has touched upon all the nuances of risk allocation in the event of failed synallagmatic contracts, especially those that are terminated due to impossibility of performance. That is so, because, impossibility of performance is a complex and intricate doctrine. First of all, it may be argued that in the contractual context, impossibility as such is an “artificial” concept, as performance is almost never impossible, because if that which was agreed is not physically possible, its value is always possible, unless it is an agreement that involves the status of a person. What is really logical is to say that on the happening of certain events, requiring a party to perform can be so “uneconomical” with the result that if the law stood silent, it would be ridiculed. But even if one immediately accepts the conventional wisdom that there is such a thing as impossibility of performance, it is not always self-evident from the case law what exactly impossibility of performance means. For example, no one would doubt that either “commercial impracticality” or “frustration of purpose” constitutes impossibility of performance; but the case law sometimes lump them together as cases of impossibility of performance. Thus, for practical purposes and brevity’s sake one can agree with Posner and Rosenfield that the subject of impossibility could be subdivided into three subheadings, namely, “impossibility of performance,” “frustration of purpose” and “extreme impracticability”. “Impossibility” per se is the rubric to use when the carrying out of a promise is no longer “physically possible”, and “frustration of purpose” is the rubric to use when performance of the promise is physically possible, but the underlying purpose of the bargain is no longer attainable. Impracticability, in turn, should be the catch-all term for any discharge case that does not fit comfortably into either the pure impossibility or the frustration moulds. Impracticability is therefore suitable for use when performance of the promise is physically possible and the underlying purpose

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81 Visser’s explanation does refer to some of the complexities such as objective and subjective impossibility, and the difference between legal impossibility and physical impossibility, and the contention of divisibility or otherwise of the performance (Visser Unjustified Enrichment 479-486).

82 For example, where the agreement is for marriage and the bride dies, but if the agreement is a trip to the moon, the performance may be technically feasible, but economically prohibitive. On subjective and objective impossibility see also Unitbank Savings and London Ltd (formerly Community Bank) v ABSA Bank Ltd 2000 4 SA 191 (W) 198.

83 Other terms used in practice are “physical impossibility”, “legal impossibility”, “impracticability”, “personal inability”, “increased difficulty”, and of course “frustration of object”.


85 See for this subset the famous English “coronation cases” in which landlords rented premises to customers who were eager to view the coronation procession of King Edward VII, but the coronation was cancelled due to Edward’s illness and discharge of contracts was sought on the ground that the underlying purpose (the viewing of the procession) had been frustrated. For comments on these cases see McElroy & Williams “The Coronation Cases” 1941 MLR 241; Posner & Rosenfield 1977 Journal of Legal Studies 85 nn 8-9.
of the bargain achievable, but as a result of an unexpected event enforcement of
the promise would entail a much higher cost than originally contemplated. It
is noteworthy highlighting that for this third subset it is difficult to articulate a
standard as to what magnitude of cost change is necessary to justify discharge
on the ground of impracticability. Where courts have used it as applying to
impossibility cases, they are prone to say that “mere hardship” is not enough.
They thus safeguard the integrity of the bargain principle. Some cases point to
examples of costs being infinite, if performance were required; hence the label
of impossibility applied to them. But whether the cost is infinite, or merely
prohibitive relative to the gains from performance (as in the impracticability
and frustration cases), it is really a distinction without much relevance to the
purpose of contract law in general. For this reason, thus, it is thought that there
is no functional distinction between impossibility and frustration cases on the
one hand and impracticability cases on the other. The reality indicates that in
every discharge case the basic problem is the same: to decide who should bear
the loss resulting from an event that has rendered performance by one party
highly “uneconomical”.

Based on the reflection and observations above, I explore some further
contours of risk allocation in this section. In doing so, I will not repeat the
discussion which is already clearly set out in detail in Visser’s work, save
to direct the reader to some salient points, should the need to do so arise.
My objective here is to highlight those additional nuances associated with
the concept of risk allocation in contractual contexts that may deepen the
understanding of the “person who has control and can insure against the
loss”.

243 Is “the person who has control” also and always the same as
the “one who can insure against the loss”?

If the answer lies in identifying the “person who has control and can insure
against the loss”, and remembering that we are dealing with situations where
the “contract” was initially “validly” concluded, then the further inquiry that
arises is knowing how the parties allocate risks in contractual settings. We
must first ask ourselves, what is a risk? At what moment must the risk be
allocated in contractual settings? Is the risk of loss allocated invariably and
similarly between the parties? Does allowing a “judicial identification” of the

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86 For some practical examples, see ALI Restatement (First) of Contracts (1932) § 454.
87 Discharge on this ground is normally not objectively recognised in most of the jurisdictions under
consideration. But a more critical analysis can yield unexpected subtle recognitions even on this ground.
89 See Comment “Quasi-Contract: Impossibility of Performance – Restitution of Money paid or Benefits
Conferrered where further Performance has been Excused” 1948 Mich LR 401. For related issues to
impossibility of performance see Birmingham “A Second Look at the Suez Canal Cases: Excuses for
Non-Performance of Contractual Obligations in the Light of Economic Theory” 1969 Hastings LJ 1393
1399; Schwartz “Sales Law and Inflation” 1976 S California LR 1 (This author discusses contract cases in
which inflation was the event causing no performance. In that light, inflation is a risk which, if it becomes
uncontrollable, is tantamount similar to frustration of purpose cases.)
superior risk bearer at the moment of loss conform to an “ex post facto” (a posteriori) allocation of risk or to an a priori allocation?

2.4.4 The dynamics of risk allocation

There are two possible differing effects in evaluating the risk allocation in the context of failed agreements due to a supervening impossibility. In either case, the first question is to ascertain whether the contract is deemed to have been discharged or not on the occurrence of the unforeseen event. That is so because, on the one hand, the effect of discharging the contract is to place the risk of the event preventing performance on the promisee, while the effect of upholding it is to place the risk on the promisor. These effects, of course, depend in part on how the parties themselves allocated, or are assumed to have allocated, the risk of the unforeseen events from the inception of the agreement itself.

At the stage of the formation or negotiation of the contract the parties may directly or indirectly have chosen to allocate the risk of the unknown and unforeseen events differently, depending on how the parties could have estimated the probability of the occurrence of such a risk. Unquestionably, if the parties have objectively chosen to allocate the risk of unforeseen events in a particular way, that manner should be followed. This, of course, brings back the contention that “reliance” must be placed on the contract, and the resulting remedy should also be “contractual”. Whatever perspective one chooses, the resulting approach is not a contentious issue for the time being.

To start with, one must distinguish two types of risks: an “endogenous risk” and an “exogenous risk”. Equally important is the risk attitude assumed by each party towards the various subsets of possible future risks. While an “endogenous risk” is generally more amenable to control, obviously, depending on its nature, an “exogenous risk” tends to be completely independent of the parties and sometimes nothing can be done to control it. If a party to an agreement assumed an attitude that was risk neutral, it cannot be expected of him to take measures beyond ordinary risk control, because, in principle, that party would only be interested in the adverse risk. However, a risk-averse party is not precluded from adopting secondary strategies to minimise the chances of it happening and the costs of bearing the residual risk. This possibility of a risk-averse party bearing the residual loss is, in my view, what underpins Visser’s approach in its second leg when he asserts that the method also “recognises the autonomy of each contracting party to be able to make a decision whether or not to take the risk of making disbursements in

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91 Patterson “The Apportionment of Business Risks through Legal Devices” 1924 Columbia LR 335 348-353.
92 As examples of an “endogenous risk” one can cite a mechanical failure of an aircraft engine, which is ordinarily and mostly preventable, though no total assurance can be given for its preventability; the insolvency of a Bank, although it depends on which side of the coin one sees, etc.
93 The following are ordinarily considered exogenous risks: “acts of God” (or natural disasters), fires, acts of war, riots, insurrections, orders of court or regulatory agencies, destruction of machineries, strikes, lockouts, or other industrial disturbances.
94 Triantis 1992 Univ Toronto LJ 450 455.
95 455.
preparation for performance”. In essence, Visser’s account on this second leg is about the optimal allocation of the risk. An optimal allocation of the risk is ordinarily a function of the parties’ comparative advantages in risk control and the residual risk management, as well as their risk preferences. In circumstances where all things remain equal, a given risk should ordinarily be borne by the party who can implement measures to control it at the lower cost. This is typically the party whose performance is affected by the risk, should there be such a party. If that party is also risk neutral, it should bear the risk.

It must be highlighted, however, that the optimal allocation is less clear where the superior risk controlling party is averse to the residual risk. In this situation, if all other things remain equal, the residual risk should be allocated to the party that is the superior risk manager. However, in real life, the superior risk manager is not always easy to identify, and is often not the party with the comparative advantage in risk control. This being the case, in ascertaining “the person who has control and can insure against the loss” further consideration must be given to the parties’ attitudes to the risk, because such attitudes also vary according to the context and the nature of the agreement entered into. As already highlighted above, in some cases a party may be risk neutral, while in others he may be risk averse. Even where the parties have agreed on risk allocation, there may remain a possibility of under-assessing the extent of the risk by one party or by both. But it should still be emphasised that if the parties have expressly assigned the risk to one of them, there should normally be no occasion to inquire into which of them is the superior risk bearer. Nonetheless, a party can be a superior risk bearer for one of two reasons: first, he may be in a better position to prevent the risk from materializing. Here because, either he has control of the object (or of the situation), as in the first leg of Visser’s approach, or he is the superior insurer. As insurance is a method (alternative to prevention) for reducing the cost associated with the risk that a performance of a contract may be more costly than anticipated, it is a particularly important process of cost avoidance in the impossibility context because the risks with which that doctrine is concerned may not necessarily be preventable by the party charged with non-performance.

Given that prevention is but one way of dealing with risk, insurance is then the other means of dealing with the effects of risk, if it materialises. Here we encounter the second leg of Visser’s approach, as mentioned above. Should the promisor be the one in the position of a “superior risk insurer”, then his inability to prevent the risk from materializing, should normally not operate to discharge him from his contract, anymore than an insurance company’s inability to prevent, for example, a fire on the premises of an insured should excuse it from its liability to make good the damage caused by the fire.

On this insurance leg of the analysis, one must also take into account two further aspects that may arise, should the parties have directly or

96 Visser Unjustified Enrichment 499.
indirectly assigned the risk in their agreement. There may be a mutual under-assessment or simply a unilateral under-assessment of the risk. If both parties under-assessed the risk to the same extent, the allocation of the risk should appropriately be determined by other factors, such as differences in risk management capabilities and risk preferences. If there was a unilateral under-assessment of the risk, the party so assessing it should bear the loss, if all other factors also militate against him. It must be noted however that to the extent that the unilateral under-assessment was influenced either due to persistent cognitive errors or due to bias, the party to whom such risk is allocated may suffer disproportionate loss in the contract for bearing the risk. In such circumstances, judicial intervention might be justified to redress a possible inequity, and avoid potential unjustified enrichment of one party to the detriment of another.

In certain other circumstances, the determination of the superior risk manager may be a complex exercise, because from time to time it depends on factors that may frequently point in opposing directions. If this is the case, sophisticated parties may usually be able to weight themselves at the stage of the formation of their agreement the comparative advantage in each aspect of risk management and allocate the risk to the lowest bearer in the aggregate. Alternatively, they may agree to a risk sharing arrangement. For example, one party may be in a better position to estimate the probabilities of the occurrence and the other party may be better able to estimate the magnitude of the loss in the event risk materialises. But all of these depend on the parties’ attitudes to risk in the particular circumstances. One cannot pre-deterministically assign the risks in such circumstances.

2 4 5 The challenges of an ex-post facto risk allocation

The challenges to Visser’s suggested approach is that to a certain extent it postulates a judicial identification of the superior risk bearer and it makes the case for an ex-post facto judicial allocation (or reallocation) of risks. That is so because it rejects a “pre-determination” of a loss bearer, as hitherto advocated in South African law. The virtues of the current South African position are that it avoids “uncertainty” in the judicial interpretation of contractual allocation of risks. Its main “axiom” could equally read thus: “better have one person know for certain that he is responsible, even if the other [person] is the superior risk bearer”, regardless of whether that might result in injustice or not. Visser’s suggested approach is, however, essentially to the effect that if on the same factual scenario, one of the parties was in control of the thing (or of the situation) or he is deemed to be the superior risk bearer and the situation might result in injustice to the creditor, the risk can be re-allocated. That allocation (or rather re-allocation) must however follow an “optimal” approach.

99 Triantis 1992 Univ Toronto LJ 476.
100 452.
On the face of it, Visser’s suggested approach will come up against, among others, two possible hurdles, namely: the “competence” of the courts to identify the superior risk bearer and the predictability of such determination. It might face the predictability hurdle because critics might argue that if it is not clear when a risk is allocated and when it is not, one cannot be sure what a court will do under any particular scenario. Someone who is risk averse and who values certainty and predictability might prefer a fixed, predictable (albeit, perhaps, inappropriate) allocation of risks to a more flexible (but, perhaps, more appropriate) allocation of risks that offers only an imprecise idea of what a court will do. Given that in many contractual situations some parties are risk averse, the legal system might be tempted to stick to the current approach that seemingly offers more predictability with its pre-deterministic view.

The suggested approach, however, makes it clear that the factors that make one party a superior risk bearer are the party’s ability to prevent or control the materialization of the risk, as well as its risk preferences and its ability to reduce the cost of the residual risk through insurance or perhaps even through “hedging in the financial markets” if there is such opportunity in some complex business dealings. That is so because when Visser remarks in the Hellwege’s hypothetical example of a horse that he cites to illustrate the new approach that “because he [the party] was able to insure it and elected not to do so makes it unobjectionable that he should shoulder the loss”, or earlier in acknowledging the exception that “where the loss would also have happened if the enrichment creditor had had it under his control, and it is not an instance where it is customary for the enrichment creditor to insure the object though it is not under his control”, Visser’s approach demonstrates that the fears of unpredictability may be unfounded or at least overstated. Although it is mostly true that allocations of risks by law to the superior risk bearer fulfil their purpose only to the extent that they are certain or predictable, Visser also makes it plain that should the risk be “exogenous” and at the time of contracting could be deemed to be remote, but the materialization of which could be severe, the contractor should always avail him or herself of the residual risk management opportunities available to the parties, as safety nets. A party who unreasonably ignores them, must bear the loss should the risk materialise. Furthermore, Visser’s position when he asserts that “he was able to insure it and elected not to do so”, seems to me to exactly express these precautionary measures that are available to the contracting parties in order to offset any supervening risks.

3 Conclusion

In sum, the suggested approach that in synallagmatic agreements the way forward is to first identify “the party who has control and can insure against the loss” is founded on solid grounds and accords more with justice.

101 “Hedging in financial market” here is understood as the practice of purchasing and/or selling a financial instrument specifically to reduce or cancel out the risk in another investment.

102 Visser Unjustified Enrichment 500.

103 500.
in situations of frustration of purpose for supervening impossibility, than the “pre-deterministic approach”. This view also squares with the general principle of unjustified enrichment that places emphasis not only on what is happening with the assets of the claimant but also on what is happening with those of the defendant. But because there are mechanisms available to the parties to avoid the consequences of unforeseen future risks, even if such risks might seem remote at the time of contracting, common sense dictates that the one that was able to take measures to avert the risk or minimise its impact, if it should happen, must shoulder the risk of the loss. Put differently, loss of enrichment (change-of-position), as a general defence, should not be available to the parties.

The loss-sharing approach is also rejected because of its potential to inject some confusion into the administration of justice. That being the case, notwithstanding the possibility of being satisfactory in some circumstances, it would be utterly unsatisfactory in a range of other cases if it is scrutinised. The loss-sharing approach is prone to taking away the incentive to obtain insurance or to take sufficient precautions. That is so because the approach postulates that the risk can be on one of the parties or the other, but it fails to explain why it should not be on the party who might not have chosen to shield itself from the risk of some unforeseen future event rather than on the party that did not want to take any.

Furthermore, where one of the parties is risk-neutral, if the risks were truly unexpected, so that no precautions could have been taken against it, and if neither party was better equipped to deal with the problem when it arose, then it would make no difference who bears the loss. The amount of the loss being borne is the same. It cannot be reduced by dividing it into smaller pieces. In such scenarios the reality dictates that there is no reason to keep the risk on one party, but there is equally no compelling reason to shift it away either.104 Hence, where the balance does not favour one party or the other, the risk should lie where it now stands.

**SUMMARY**

The current position in South African law on enrichment situations arising from “failed agreements” is that “if you have received a performance in terms of a contract which subsequently fails for whatever reason, you give it back if you still have it; if you cannot give it back, you are absolved, unless you were culpable in relation to the loss”. Daniel Visser, however, challenges this approach and proposes a new one in his recently published book, *Unjustified Enrichment* (2008). This article evaluates both this position and the newly suggested approach and it argues that in cases of failed synallagmatic contracts “the person who was able to take measure to avert the risk or minimise its impact, if it did happen, must shoulder the risk of loss”. However, such a determination must consider the nature of the risk, whether “exogenous” or “endogenous”, and the attitude of each party towards risk.

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