Republic of South Africa
IN THE HIGH COURT OF SOUTH AFRICA (WESTERN CAPE HIGH COURT, CAPE TOWN)

CASE NO: 18783/2011

In the matter between:

MR VIDEO (PTY) LTD Applicant / Respondent

and
BROADWAY DVD CITY CC t/a
MR VIDEO STRAND ON BROADWAY First Respondent / Applicant
(Registration No. CK 2006/160331/23)

IEKRAAM JARDINE
(ID No.:) Second Respondent / Applicant

ZAHIEDA JARDINE
(ID No.:) Third Respondent / Applicant

JUDGMENT DELIVERED ON 24 JANUARY 2012

ZONDI, J:

[1] On 13 October 2011 the applicant ("Mr Video") brought an application to this Court for an order to have the Arbitration Award dated 29 July 2011 made an order of Court in terms of section 31 (1) of the Arbitration Act 42 of 1965.

[2] The arbitrator rendered an award in the following terms:

> *"(a) confirming cancellation of the franchise agreement which was entered into between the Claimant and First Defendant on 22 January 2007;*
>
> *(b) directing that the Defendants are liable, jointly and severally (the one paying the other to be absolved) to make payment to the Claimant of the sum of R77 772.34, being in respect of outstanding franchise and stock fees;*
>
> *(c) directing that the Defendants are liable jointly and severally (the one paying the other to be absolved) to make payment to the Claimant of the sum of R72 637.45, being in respect of outstanding advertising levies;*

(d) directing that the Defendants are liable jointly and severally (the one paying the other to be absolved) to make payment to the Claimant in the sum ofR22 143.41, being in respect of outstanding software fees;

(e) directing that the Defendants are liable for interest in the aforesaid amounts at the rate of 21% per annum, with effect from 1 June 2011 to date of payment of all outstanding amounts;

(f) directing that the Defendants are liable jointly and severally (the one paying the other to be absolved), for the Claimant's costs of suit (including costs of the arbitration and the arbitrator) on the scale as between attorney and client;

(g) directing that First Defendant shall immediately discontinue that use of all names, logos, marks, trade marks, trade names, signs, structures and forms of advertising indicative of the Claimant's trading name (Mr VIDEO, VIDEO EXPRESS, and VIDEO EXTREME), and cause to be made such changes in the signs, buildings and structures as Claimant shall reasonably direct, so as to distinguish same from its/their former appearance and from any business franchised by the Claimant or any business operated by any other franchisee in the "Mr Video" group:

(h) directing that First Defendant return forthwith to the Claimant, al supplies, signage and other materials bearing the name, logo or marks of the Claimant;

(i) declaring that First Defendant's right to use the name and logo or any similar name bearing the words "Mr Video", or any name or logo which may be utilised in the future by the Claimant, and any systems, procedures and know-how associated therewith, shall terminate forthwith; and

(j) directing that, in the event First Defendant fails or omits, upon request, to make the changes referred to in terms of paragraphs (g) and/or (h) (or as otherwise required in terms clause 11.4.2 of the agreement referred to in paragraph (a)), the Claimant shall be entitled to take whatever steps it may deem necessary to do so, including, but without limiting the generality of the aforegoing, entering the First Defendant's premises and causing such changes to be made."

[3] The basis of Mr Video's application is that the award still remains unsatisfied by the respondents despite its existence having been communicated to the respondents.

[4] The respondents responded to the application by launching on 16 November 2011 an application on an urgent basis for the setting aside of the franchise agreement concluded between the first respondent and the applicant on 22 January 2007 and pursuant to which the dispute between the parties had been referred to arbitration.

[5] In the alternative the respondent sought an order interdicting Mr Video from enforcing the arbitration award made in its favour pending the outcome of an action to be instituted by the respondents for the rescission of the franchise agreement. The respondents also sought an order suspending the hearing of Mr Video's application pending the final determination of the action to be instituted by the respondents.

[6] In that application the respondents also sought an order directing the applicant to make payment to the first respondent of the sum of R360 000.00 for delictual damages allegedly suffered by the first respondent by reason of Mr Video's misrepresentation.

[7] The ambit of the relief sought by the respondents was extended by the respondents in a supplementary affidavit which the respondents thereafter filed. **Mr Petersen** who appeared for the respondents has, however, in his heads of argument disavowed any reliance on the supplementary affidavit and has confined his argument to the relief sought in the founding affidavit.

[8] Notably in the notice of motion the respondents do not set out the nature of the relief which they will be seeking in their proposed action but upon reading para 87 of the founding affidavit it would appear that in the proposed action they will be seeking an order to have the franchise agreement *"set aside / cancelled and claim the necessary damages"* which in my view, to all

intents and purposes, is similar to the relief they are seeking in these proceedings.

[9] The respondents in their application sought the setting aside of the franchise agreement on the ground that the first respondent was fraudulently induced by the applicant to conclude it. The respondent do not dispute that they are aware of the arbitration award. They admit that it was brought to their attention on 8 August 2011 but they contend they could not challenge it or the agreement forming its basis due to financial constraints.

[10] The facts upon which they rely for the contention that the franchise agreement was fraudulently induced are briefly as follows: During 2006 the second and third respondents wanted to start a franchise business. After conducting some research in franchise business they got interested in Mr Video's business model and to that end the third respondent contacted Mr Video's regional offices in Johannesburg with a view to getting more information about its business model. The third respondent spoke to one Ms Geene who sent her an email regarding Mr Video's business and what the projected monthly turnover and expenses of the business were. The respondents were informed that the applicant's projected monthly turnover was about R90 000.00. On the basis of these projections the respondents formed a view that they would be able to make a profit of approximately R24 300 per month.

[11] The respondents also received from Mr Video undercover of a letter dated 5 April 2006 a document about its history and profile as well as the set up costs they had to pay for the franchise. In particular it was indicated in the profile that a Mr Video Express Store, comprising approximately 100 square metres would cost about R255 000.00 excluding VAT. These facts impressed the respondents and they became so much interested in Mr Video's business model to the extent that they even visited a website of the Franchise Association of South Africa of which they believed Mr Video was a member and downloaded a copy of a disclosure document in which the obligations of the franchisor to a prospective franchisee are set out.

[12] It is at this stage that the respondents became aware that the disclosure document *inter alia* required Mr Video to furnish a potential franchisee with firstly, written projections in respect of

levels of potential sales, income, gross or net profit or other financial projections for the franchise business and had to state the assumptions on which these projections were based. Secondly, in terms of the disclosure document the projections had to be clearly indicated whether they were profit or cash flow projections, franchise salary, capital and interest loan repayments had to be indicated.

[13] The respondents further allege that Mr Video exaggerated its image to them and even undertook to support and assist them with the negotiation of lease contracts, purchasing of stock, ongoing training and specific guidelines to improve turnover. Relying on these undertakings by Mr Video, the respondents applied for a franchise in about April 2006 and later in about November 2006 signed a franchise agreement after paying the set up costs. In their application for a franchise the respondents indicated Strand area as their first preference.

[14] The franchise agreement was entered into between Mr Video and the first respondent which is the close corporation of which the second and third respondents are members. The respondents point out that when they applied for the store they had budgeted for R255 000.00. Thereafter the first respondent with Mr Video's employee's advice proceeded to conclude the lease agreement with Shoprite in respect of Strand premises. This took place in June 2006.

[15] The respondents further allege that it was a tacit and/or implied term of the franchise firstly, that Mr Video would provide the first respondent's initial staff with one week's store and VHS training at another Mr Video branch; secondly, that Mr Video would provide the staff of the first respondent with ongoing training and specific guidelines to improve its turnover; and thirdly, that Mr Video would provide the first respondent with a grand opening at the initial launch of its store.

[16] The respondents state that the offer to purchase form which Mr Basset of Mr Video sent them on 26 August 2006, contrary to what they had been told they would pay, indicated the purchase price as R399 880.00 excluding VAT. When they refused to sign it Mr Basset told them it was too late for them to do so as they had already concluded a lease agreement with Shoprite and the latter could sue them for damages if they pulled out. Reluctantly they signed the offer to purchase.

[17] The respondents aver that in breach of its contractual obligations, Mr Video failed to provide training to the first respondent's initial staff and to provide the first respondent with a grand opening at its initial launch and as a consequence thereof the first respondent was unable to derive maximum benefit of being associated with the franchise brand of Mr Video and generate the monthly turnover of R90 000.00 as projected by Mr Video.

[18] The respondents point out that the first respondent managed only to make the average monthly gross turnover of R54 385.46 between the period December 2006 to February 2008; R49 298.15 between March 2008 to February 2009; R41 092.96 between March 2009 to February 2010 and R36 770.93 between March 2010 to February 2011 which they contend is far less than the projected monthly turnover of R90 000.00 promised by the applicant.

[19] The respondents allege that from inception the first respondent struggled to honour the agreement with Mr Video in respect of royalty fees, advertising fees and stock fees that were due and payable to it resulting in the latter instituting legal proceedings against them for the cancellation of the agreement and payment of monies due in terms of the agreement.

[20] The respondents contend that the contract arrangement with Mr Video, from its inception (when they were provided with the initial projections and set-up costs in

April 2006) right through to the conclusion of the franchise agreement in 2007, was done on a fraudulent basis with the intention to cause economic duress/pressure on the second and third respondents, which would coerce them "to *dance to the tune of the [applicant?* by entering into a franchise agreement which benefited Mr Video but prejudiced them.

[21] Mr Video opposes the respondents' application and has raised four points *in limine.* The consideration of the first point in *limine,* namely that the respondents should not be allowed to rely on matters raised in the supplementary affidavit as same was not filed with leave of the Court, has become unnecessary in view of the fact that the respondents have disavowed any reliance on it.

[22] The second point in *limine* raised by Mr Video is that the relief sought by the respondents is incompetent and ill-conceived as the agreement which they seek to have set aside was already cancelled by the applicant on 18 April 2011 which cancellation was confirmed by the arbitrator in his arbitration award.

[23] The respondents seek the setting aside of the franchise agreement on the ground that the first respondent, in respect of whose obligations the second and third respondent stood surety, was fraudulently induced by the applicant to conclude it. It must be emphasised that the respondents do not in any way challenge the arbitration which was conducted pursuant to the franchise agreement and the award rendered under the arbitration.

[24] It is correct that a party who has been induced to enter into a contract by the misrepresentation of an existing fact is entitled to rescind the contract provided the misrepresentation was material, was intended to induce him to enter into the contract and did so induce him (Christie: The Law of Contract in South Africa 5th ed page 271). The effect of a misrepresentation, whether innocent or fraudulent, is to induce in the mind of the innocent party a mistake of so fundamental a nature that his apparent assent to the contract is in truth not assent at all. The innocent party has an election. He may either stand by the contract or claim rescission. If he decides to rescind the contract he must do so within a reasonable time otherwise he may be taken to have elected to stand by the contract. He may not partially affirm and partially repudiate

the contract.

[25] The question raised in the present case is whether the respondents can still rescind the contract notwithstanding that Mr Video has cancelled it and has sought confirmation of its cancellation at the arbitration. It is common cause that the franchise agreement in the instant matter provided for the referral to arbitration of any dispute which may arise between the parties under it. When the dispute about non-compliance with certain provisions of the agreement by the first respondent arose Mr Video pursuant to the agreement referred the dispute for arbitration in which it *inter alia* sought certain relief and confirmation of the cancellation of the agreement. This was granted by the arbitrator.

[26] The object of cancellation is to terminate the primary obligations of the contract there and then but not retrospectively whereas the effect of rescission of the contract when it is claimed was induced by misrepresentation is to set aside the contract *ab initio.*

[27] Christie supra points out at 539 that:

> *"Termination of the primary obligations of the contract (the obligations of both parties to perform) does not terminate all secondary obligations, such as the obligation to pay damages for breach or (unless a contrary intention appears) the obligation to abide by an arbitration to abide by an arbitration clause in the contract".*

[28] In my view the respondents' claim for rescission must fail for two reasons. Firstly, where one party to a contract has, as a result of its breach, cancelled the contract the other party may not in an attempt the escape the effect and consequences of cancellation seek to rescind the contract on the ground that it was induced by misrepresentation. This is so because a party who wishes to rescind the contract on the ground of misrepresentation must decide whether it wishes to stand by the contract or rescind it. It may not wait for the other party to take steps in the enforcement of the contract before taking its decision to rescind the contract. In the present case the contract was for 10 years and subject to extension for another 10 years. It was concluded in January 2007 and the

parties acted in accordance with its terms until it was cancelled by the applicant on 18 April 2011. In that period the first respondent never sought its rescission on the basis of the facts which it now alleges. Secondly, the statements which the respondent contend were made by the applicant with an intention to induce the first respondent to enter into the contract which it otherwise would not have entered into do not, in my view, constitute misrepresentation and as such do not afford a basis for the rescission of the franchise agreement. For instance the monthly turnover of R90 000.00 was not guaranteed but projected. The document in which the projections are given makes it clear that *"the projections are in no way any guarantee from the [franchisor] to the [franchisee] or any third party, that the figures presented will be achieved"*

[29] With regard to the quoted set up costs it is clear to me that the set up costs which the first respondent was quoted were based on the store size of 100 square metres. The first respondent's store size is 112 square metres and this may explain the difference between what the first respondent was quoted and what it was asked to pay.

[30] In the circumstances I find that the statements made by the applicants do not constitute misrepresentation. The applicant did not make statements complained of by the respondents with an intention to induce the first respondent to enter into the contract, or to conceal from it facts the knowledge of which would cause it to refrain from entering into the contract. If the first respondent was of the view that it was induced to enter into the contract it should have participated in the arbitration proceedings and raised the defence which it now seeks to raise. The respondents may not seek to escape the consequences of the arbitration which was conducted with their full knowledge by seeking rescission of the agreement pursuant to which the arbitration was conducted. They should have sought the setting aside of the arbitration award in order to regain the opportunity which they lost when the arbitration proceeded in their absence.

[31] In light of the conclusion I have reached it follows therefore that the respondent's claim for damages in the sum of R360 000.00 and other interim interdictory relief must fail as the cancelled franchise agreement which the respondents want to rescind was validly concluded.

[32] It follows therefore that the order sought by the applicant in the main application should succeed. In the result the following order is made:

1. the arbitration award of Adv. M L Sher dated 29 July 2011 is made an order of Court in terms of section 31 (1) of the Arbitration Act 42 of 1965. The respondents to pay costs of the applicant's application on a scale between attorney and client jointly and severally.
2. the respondents are ordered to pay the costs of the application on a party and party scale.

D H ZONDI