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LEGAL UPDATE

Constitutional Court clarifies rights of innocent contractors under invalid state contracts

18 June 2026 *6 min read*

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In *Minister of Defence and Military Veterans v Zeal Health Innovations (Pty) Ltd* [2026] ZACC 21, the Constitutional Court ("the Court") clarified the rights of service providers whose contracts with the State are later found to be invalid. As the Court noted in paragraph 47 of its majority judgment, the question concerning how to protect innocent contractors when public contracts are declared invalid is one that arises frequently in South African law.

The background: A familiar problem

Following a procurement process, the Department of Military Veterans ("the Department") appointed Zeal Health Innovations (Pty) Ltd ("ZHI") to provide healthcare and wellness services to military veterans for a three-year period between 2015 and 2018 ("the Tender"). ZHI rendered services under the contract for approximately two and a half months, from 1 June to 12 August 2015, and submitted invoices that became due and payable. On 11 August 2015, the Department informed ZHI that it intended to review the procurement process. Acting on this intimation, ZHI in effect suspended all services, except for emergency services, under the contract on 12 August 2015. The Department also refused payment of ZHI's outstanding invoices, prompting ZHI to institute proceedings for specific performance. The Department, in turn, filed a counter-application to review and set aside the award of the Tender and the contract. The High Court ultimately reviewed and set aside the Tender and the contract, primarily because it exceeded the Department's approved budget in breach of the statutory requirements contemplated in the Public Finance Management Act 1 of 1999. The High Court nevertheless found that ZHI was blameless in the irregularity and was therefore an innocent contractor. It did not, however, grant relief under section 172(1)(b) of the Constitution, nor did it consider what remedy would be just and equitable to compensate ZHI for the services it had rendered or to protect its position as an innocent contractor.

ZHI appealed to the Supreme Court of Appeal, primarily arguing that the review should have been dismissed. Alternatively, it sought relief under section 172(1)(b), preserving its contractual rights despite the declaration of invalidity. The SCA dismissed the appeal on invalidity. It further held, however, that section 172(1)(b) confers a true discretion to be exercised case by case. Although the contract was invalid, ZHI had rendered services, was not complicit in the irregularities, and had been found to be an innocent party. The SCA therefore held that ZHI was entitled to "*payment of any amount it is able to establish*."

On appeal, the central issue before the Constitutional Court was what remedy, if any, is available to an innocent service provider that has performed under a State contract later declared invalid. In particular, and to quote the Constitutional Court, the question before it was: "*does the absence of a right to benefit from an unlawful contract amount to an exclusion of such benefit from the exercise by a court of its just and equitable discretion under section 172(1)(b)?*"

The Constitutional Court's approach

The Court confirmed that a just and equitable order under section 172(1)(b) of the Constitution involves the exercise of a judicial discretion, which must be applied judiciously and with regard to the facts of each case. In this matter, several features were relevant to that discretion: ZHI was an innocent party and was not complicit in the Department's irregularities; for a period of two and a half months it had performed actual services under the contract; it incurred costs in delivering those services and submitted invoices for payment; the Department had approved the invoices and the erstwhile Director-General had approved a memorandum authorising payment to ZHI which was later overturned by the Minister who instructed that ZHI should not be paid; and the Department only challenged the Tender after ZHI had already performed its obligations for a period.

Furthermore, the Court rejected the Department's contention that ZHI's recovery should be limited to out-of-pocket expenses without any allowance for profit. The Court correctly affirmed that where an innocent contractor has rendered services pursuant to an invalid contract, the appropriate point of departure is the preservation of accrued contractual rights, as recognised in *State Information Technology Agency SOC Ltd v Gijima Holdings (Pty) Ltd* 2018 (2) SA 23 (CC).

Mathopo J held that this principle entails that compensation for services actually rendered must be calculated at the contractual rate, which necessarily includes the contractor's profit margin. In other words, while the contract cannot be enforced in full, an innocent contractor is entitled to be compensated on the agreed terms for the period of actual performance, rather than being confined to mere cost recovery.

Why the judgement matters

The significance of the judgment extends beyond the specific dispute between ZHI and the Department. It provides welcome certainty for businesses that contract with organs of state by confirming that an innocent service provider will not necessarily be deprived of compensation merely because a procurement process and the resultant contract are subsequently declared unlawful.

The Court's approach recognises an important commercial reality. Service providers frequently invest substantial resources, incur operational costs, and allocate personnel in reliance on contracts awarded by the State. If contractors were restricted to recovering only their out-of-pocket expenses, or worse, left without any remedy at all, the risks associated with doing business with government would increase significantly.

The judgment therefore strikes an appropriate balance between two competing constitutional objectives. On the one hand, it preserves the principle of legality by confirming that unlawful procurement processes cannot simply be validated after the fact. On the other hand, it ensures that the consequences of invalidity do not unfairly prejudice innocent contractors who have acted in good faith and delivered value to the State.

Importantly, the Court's reasoning also discourages opportunistic conduct by organs of state. State entities cannot readily rely on their own procurement failures as a basis to avoid paying for services they have received and benefited from.

That said, the Court did not afford innocent contractors carte blanche to claim for any period. Rather, a contractor's entitlement is limited to the period during which services were actually delivered. Importantly, contractors should continue to undertake careful procurement due diligence, as the availability and scope of any remedy will remain dependent on the facts of each case.

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