

## **Management of Construction Contracts: Issues Intermination Clauses**

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**Abstract:** *Termination for default is one of the most serious provisions in a construction contract. Any right to terminate under certain contract terms requires careful consideration. Too often, a party wrongfully terminates a construction contract. This is usually done out of a misunderstanding as to when termination is authorised and proper. Penalties for such wrongful termination can be harsh. In view of the risks, it is important that employers understand when and how a termination can legally occur. The paper focuses on employers' termination for cause and provides construction stakeholders with understanding of pertinent issues when exercising the option to terminate a construction contract.*

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### **I. Introduction**

The construction industry is a complex industry with many parties involved in its process and operations, often brought together to work for a particular project. Due to its multi-faceted nature and involvement of numerous parties, disputes are often inevitable. One common dispute in the construction industry is the issue of termination of the contract by the Employer or the Contractor itself.

During contract formation phase, most parties are focused on performance rather than on possible breach. When a default termination is being considered, one can be sure that everyone will spend a considerable amount of time reading and re-reading their contract language, even if the contract is one of the construction industry's most widely used standard forms and the parties are somewhat familiar with the termination provisions included in it. At such times, both the factual history of the project and the familiar contract terms will take on a whole new light and significance.<sup>1</sup> Termination clauses are common in construction and design contracts. Such provisions allow parties to establish how they will end their contractual relationship if things do not go as planned. Iyer et al<sup>2</sup>. define termination of contracts as ending the contract work with no intention of resuming it in the foreseeable future. Termination of a contract occurs where a valid and enforceable contract is brought to an end prematurely, either by it becoming impossible of performance by circumstances which were unforeseeable at the time the contract was formed or by the action of one or both parties.

Commercial contracts including construction contracts often contain express termination clauses which provide for termination for breaches. Some contractual termination clauses work by expressly classifying terms as conditions or warranties so as to make clear those circumstances in which the contract can be brought to an end and those which only give a right to claim damages. Some contractual provisions attempt to give rights to terminate for "material" or "substantial" breaches or for "any" breaches (however minor) or for repeated breaches. In addition to the grounds upon which either party may terminate, the steps that ought to be taken to achieve lawful termination are also stipulated.<sup>3</sup> Typically, a contract will require a series of notices to be issued by the innocent party prior to termination.<sup>4</sup> These notices are to be followed by a grace period, allowing the defaulting party the opportunity to remedy the breach before termination of the contract becomes effective. A contractual right to terminate provides certainty as to the procedure to be followed by the aggrieved party. Basic principles of contract law are at issue in any termination for cause situation. Just because they are basic, however, does not mean that they are straightforward or clear cut. The greatest risk of either the owner or the contractor in terminating a contract is that the termination could be determined by a court or arbitration panel to be wrongful. If the termination is proved to be wrongful, then the party terminating the contract not only fails to collect its additional funds spent to complete the project, but must also pay the wrongfully terminated party its contract payments through the date of termination and potentially the loss of profit on the work not performed.

The discussion of this paper focuses primarily on a default termination by the owner. The aim of the paper is to examine some legal issues in termination of construction contract for cause at common law and in standard form contract, using the 1999 Federation of Consulting Engineers (Red Book) as the basis.<sup>5</sup> It also examines the legal standards applied by courts in reviewing construction contract termination procedure.

## **II. Termination of Contract at Common Law**

Common law right of termination exists unless the contract expressly sets out a complete and exhaustive termination regime<sup>6</sup>. Such rights to terminate construction contracts arise when there is a breach of a condition (as opposed to warranty) of the contract; a serious breach of an 'intermediate' or 'innominate' term of the contract; or conduct that shows the defaulter is unable or unwilling to comply with the contract or a refusal to perform, known as "renunciation".<sup>7</sup> Any of these three situations constitute a repudiatory breach of contract justifying termination at common law. Repudiatory breach of a contract arises when an act or omission of a party to the contract is such a serious breach that the innocent party is entitled to treat it as evidence that the breaching party no longer intends to be bound by it. Repudiation is not to be inferred lightly. It is a serious matter.<sup>8</sup> Whether there has been repudiation is a question of fact to be determined objectively<sup>9</sup> and this depends on a number of factors. The approach of the courts is firstly to consider what benefit the injured party was intended to obtain from the performance of the contract and secondly to consider the effect of the breach on the injured party and whether it operates to deprive the aggrieved party of substantially all of the benefit the parties intended that party to obtain under the contract. Repudiatory conduct may be a single act, or the accumulation of conduct in circumstances where one act constitutes a repudiation.<sup>10</sup> Persistent poor quality work could be treated as repudiation<sup>11</sup>. Relevant case law discusses the typical grounds that may constitute repudiation by the employer or contractor, as the case may be, to cause a termination of contract at common law. These include failure to give possession of the site<sup>12</sup>, failure to pay<sup>13</sup>, completion of work is made impossible by prevention or hindrance<sup>14</sup>, abandonment of works<sup>15</sup> and defective works<sup>16</sup>. Many conceivable repudiatory breaches (for example, suspension of the works or non-payment) are already covered by the express termination clauses in standard form construction contracts.

### **a. Termination for Breach of condition**

Regardless of whether a construction contract contains express termination provisions, a party may be entitled to terminate under the common law as a result of a counterparty's breach. It is well established that simple breaches of a contract will not create a common law right to terminate.<sup>17</sup> Therefore, in order to terminate a construction contract, the term must be an essential term by way of being a condition of the contract or a non-essential term that has caused substantial loss.<sup>18</sup> A condition is a term in the contract that is of such importance that the promisee would not have entered into the contract without assurances that the term would be strictly adhered to.<sup>19</sup> Where a term is categorised as a condition, any breach of the term, regardless of the consequences, gives the innocent party a right to terminate the contract. In the construction industry, essential terms usually deal with timely performance of works or services or with payment.

In determining whether a term is properly to be construed as a 'condition', the courts apply a test of 'essentiality'. This test was famously explained by Jordan CJ in *Tramways Advertising Pty Ltd v Luna Park (NSW) Ltd*:<sup>20</sup>

The test of essentiality is whether it appears from the general nature of the contract considered as a whole, or from some particular term or terms, that the promise is of such importance to the promisee that he would not have entered into the contract unless he had been assured of a strict, or a substantial, performance of the promise, as the case may be, and that this ought to have been apparent to the promisor . . . If the innocent party would not have entered into the contract unless assured of a strict and literal performance of the promise, he may in general treat himself as discharged upon any breach of the promise, however slight.

In other words, in determining whether or not a term is to be characterised as a condition, the court asks whether the parties would have entered into the contract had they not been assured of strict compliance with the term.

### **b. Termination for Sufficiently Serious Breach of an Innominate Term**

A breach of an intermediate or innominate term, i.e. neither a condition nor a warranty, only justifies termination if the breach is sufficiently serious. The term "sufficiently serious breach" is described as a term that must "go to the root of the contract", "frustrate the commercial purpose" of the contract or "deprive the party not in default of substantially the whole benefit"<sup>21</sup> of the contract. In every case, the court will look at the nature and consequences of the breach to decide whether termination is justified. In *Hong Kong Fir Shipping Co. Ltd v Kawasaki Kisen Kaisha Ltd*<sup>22</sup> Upjohn LJ said:

Does the breach of the stipulation go so much to the root of the contract that it makes further commercial performance of the contract impossible, or in other words is the whole contract frustrated? If yes, the innocent party may treat the contract as at an end. If nay, his claim sounds in damages only.

The NSW Court of Appeal summarized what constitutes a sufficiently serious breach in four propositions:

First, it is the effect of the breach on the contract as a whole which matters: in order for a right to terminate to exist, the performance of the contract must be rendered substantially different from that intended by

the parties, as a consequence of the defaulter's breach. Second, the seriousness of the breach depends not only on the breach itself but also on the consequences of the breach, both actual and foreseeable, for the innocent. Third, the assessment of the consequences of the breach is essentially a factual matter on which opinions are likely to differ. The innocent bears the onus of proof. Fourth, there is a link with the doctrine of frustration in that, in commercial contracts at least; the degree of seriousness required is the same as that applied under the doctrine of frustration.<sup>23</sup>

The Court decided that the right to terminate a contract for breach of an intermediate term depended on the seriousness/gravity of the breach, and its ensuing consequences.

### **c. Refusal to Perform or Renunciation**

Any event (including an emotional feeling by one of the parties that he has made a bad bargain), can cause one of the parties to a construction contract to feel that he cannot or should not perform as agreed. The party may then inform the other of his decision not to perform the contract; the result of such a notice is referred to as a "renunciation" or "anticipatory breach". An anticipatory breach of a contract is one committed before the time has come when there is a present duty of performance. It is the outcome of words or acts evincing an intention to refuse performance in the future.<sup>24</sup> The party may expressly declare that it no longer intends to perform, or the party's conduct may be such as to lead a reasonable person to conclude that the party is unwilling or unable to perform the contract in accordance with its terms. Not just any threatened breach will amount to a renunciation. Where a party intends to perform some, but not all, of its obligations, the question is whether the anticipated non-performance will amount to a breach of a strict condition or a sufficiently serious breach of an intermediate term. If it is a mere breach of warranty, or a minor breach of an intermediate term, there will be no renunciation.

A key consideration in deciding whether an act is, in fact, an anticipatory repudiation is the intent of the breaching party as manifested by his overt actions, as opposed to any secret intentions the breaching party may harbour.<sup>25</sup> Merely expressing a negative attitude toward the contract or indicating that more negotiations are necessary does not indicate that a contract should be considered to be repudiated anticipatorily.<sup>26</sup> A disclosed intent to breach in the future cannot be asserted to make a party presently liable or to confer a present right of action in the other party if the breach is merely being contemplated but not actually committed.<sup>27</sup> Mere probability that a breach will be committed is insufficient to support a finding that a right of action for breach of contract exists. Certainty, not probability, of breach is required. Courts have firmly adhered to the doctrine that a repudiation must be definite and unequivocal; the repudiating party must indicate with certainty that he will not perform the terms of the contract within the time specified.<sup>28</sup> Thus, doubtful or indefinite statements made by one of the parties that he may or may not perform in the future do not create an immediate right of action in the other party.<sup>29</sup> The United States Supreme Court has held that whenever an alternative to a contract is proposed, along with what appears to be an anticipatory repudiation, such a statement is too equivocal to be considered actionable.<sup>30</sup> Likewise, a request that certain terms of the contract be changed or that the contract be cancelled does not, in itself, constitute an actionable anticipatory repudiation.<sup>31</sup>

Termination under contract provisions or common law is not automatic. The innocent party may elect either to accept the breach and treat the contract as discharged or to affirm the contract and press the party in breach to perform.<sup>32</sup> A party cannot affirm a contract following a repudiatory breach unless he has a full understanding of the facts leading to that breach<sup>33</sup> and is aware of the right that he has to choose between acceptance and affirmation.<sup>34</sup> The law does not lay down a particular period in which the election must be made. The nature of the contract may determine the length of time given to the innocent party. If, for example, time is of the essence or the contract has been entered into in a volatile market, the time allowed is likely to be relatively short.<sup>35</sup> However, it is crucial for the innocent party not to do anything to jeopardise the right of election, either by waiting too long to decide how to respond,<sup>36</sup> or by losing the right of election by inconsistent conduct. In practice this area can be fraught with difficulty because, while the innocent party is deciding how to treat the contract, he risks taking a step which constitutes an election to affirm it and, once an affirmation has been made, it cannot be revoked.<sup>37</sup>

## **III. Material/Substantial Breach of Contract**

Most construction contracts contain general provisions which permit the owner to terminate if the contractor commits a material breach of the contract. A party is said to be in breach of contract when he acts contrary to the terms of the contract<sup>38</sup>. In some standard construction form contracts, material or substantial breach is generally required before an employer can terminate a construction contract for default. The types of material or substantial breaches that may warrant a default termination are sometimes, but not always, set forth in the default clause.<sup>39</sup> AIA Document A201<sup>40</sup> clause 14.2.1 provides that an employer can terminate a construction contract if the contractor materially breaches the contract in one of the ways stated in the document. Clause 39.2 of the Australian Standard General Conditions of Contract (AS 4000)<sup>41</sup> states that "if the

Contractor commits a substantial breach of the contract, the Principal may... give the Contractor a written notice to show cause". Many courts have addressed the term "material or substantial" breach, and while the definitions they provide vary slightly, a substantial or material breach is generally characterized as a (i) substantial failure to perform, (ii) a breach so substantial as to defeat the purpose of the contract, or (iii) one so substantial as to defeat the object of the contract.<sup>42</sup> Other courts characterize the breach as one that goes to the root<sup>43</sup> or essence<sup>44</sup> of the contract, or a breach of such significance or materiality as to preclude adequate compensation in money damages.<sup>45</sup> Williston considers a "material" breach as a failure to do something that is so fundamental to a contract that the failure to perform that obligation defeats the essential purpose of the contract or makes it impossible for the other party to perform under the contract. In other words, for a breach of contract to be material, it must "go to the root" or "essence" of the agreement between the parties, or be one which touches the fundamental purpose of the contract and defeats the object of the parties in entering into the contract. A breach is "material" if a party fails to perform a substantial part of the contract or one or more of its essential terms or conditions, the breach substantially defeats the contract's purpose, or the breach is such that upon a reasonable interpretation of the contract, the parties considered the breach as vital to the existence of the contract.<sup>46</sup> Thus, even when dealing with highly standardized construction industry forms, a court will have to evaluate the overall facts and circumstances to determine whether there has been a material, or substantial breach entitling the employer to terminate the contract. If or perhaps more appropriately, when the declaration of termination is challenged in court or arbitration, a finder of fact (be it a judge or arbitration panel) will decide after the fact whether the breach was sufficiently material so as to justify termination of the contract.<sup>47</sup> When making this inquiry, the finder of fact will look not at the subjective beliefs or understandings existing at the time the termination decision was made, but instead, will determine whether the decision was justified based on an objective evaluation of the facts as they actually existed at the time the termination decision was made.<sup>48</sup> A breach that is incidental or subordinate to the main purpose of the contract, or one that is not so substantial and fundamental as to defeat the object of agreement, is not a material breach.<sup>49</sup>

What constitutes a material breach will depend, of course, on the provisions of the contract. Where the contract is silent or ambiguous, the parties' intent will be inferred by the court, as a question of fact, from extrinsic evidence of the circumstances.<sup>50</sup> The material breach will be a matter of interpretation in each case<sup>51</sup> but, as a general rule, courts are willing to find that a material breach does not have to be repudiatory; something less will suffice. In *Mid Essex Hospital Services NHS Trust v Compass Group UK and Ireland Ltd*<sup>52</sup>, English Court of Appeal held that the defendant had not been entitled to terminate its contract with the claimant under a clause allowing termination for "material breach". Jackson LJ stated "In my view this phrase connotes a breach of contract which is more than trivial, but need not be repudiatory... having regard to the context of this provision, I think that 'material breach' means a breach which is substantial.<sup>53</sup> The breach must be a serious matter, rather than a matter of little consequence." As stated by Bruner and O'Connor "an unexcused breach is material only if it reasonably compels a clear inference of unwillingness or inability of one party to meet substantially the contractual future performance expectations of the other party. . . ."<sup>54</sup>

There may be a right to terminate for "any breach", which on its face appears very broad. But the courts have tended to interpret such terms restrictively, e.g. to mean a breach that is repudiatory at common law, on the basis that a broader interpretation would flout business common sense.<sup>55</sup> It is, however, worth noting the recent trend for the courts to downplay considerations of business common sense unless a clause is ambiguous.<sup>56</sup> Contracts may also provide a right to terminate in circumstances which do not amount to a breach of contract at all. This is common with a right to terminate for convenience, so that the employer can bring the contract to an end without having to establish particular grounds for termination.

#### **IV. Grounds for Termination Of Contract Under The Red Book**

Clause 15 of the FIDIC Red Books sets out the circumstances that may lead to a termination of the contract by the employer as a result of a default by the contractor, and describes the procedures that must be followed. Sub-Clause 15.2 provides that the Employer shall be entitled to terminate the Contract if the Contractor:

- a) Fails to comply with Sub-Clause 4.2 (Performance Security) or with a notice under Sub-Clause 15.1 (Notice to Correct);
- b) abandons the Works or otherwise plainly demonstrates the intention not to continue performance of his obligations under the Contract;
- c) without reasonable excuse fails: (i) to proceed with the Works in accordance with Clause 8 (Commencement, Delays and Suspension), or (ii) to comply with a notice issued under Sub-Clause 7.5 (Rejection) or Sub-Clause 7.6 (Remedial Work), within 28 days after receiving it;
- d) subcontracts the whole of the Works or assigns the Contract without the required agreement; (e) becomes bankrupt or insolvent, goes into liquidation, has a receiving or administration order made against him, compounds with his creditors, or carries on business under a receiver, trustee or manager for the benefit of

his creditors, or if any act is done or event occurs which (under applicable Laws) has a similar effect to any of these acts or events; or

- e) gives or offers to give (directly or indirectly) to any person any bribe, gift, gratuity, commission or other thing of value, as an inducement or reward: (i) for doing or forbearing to do any action in relation to the Contract, or (ii) for showing or forbearing to show favour or disfavour to any person in relation to the Contract, or if any of the Contractor's Personnel, agents or Subcontractors gives or offers to give (directly or indirectly) to any person any such inducement or reward as is described in this sub-paragraph (f). However, lawful inducements and rewards to Contractor's personnel shall not entitle termination.<sup>57</sup>

Some of these grounds for termination can be more controversial while some are easier to apply than others and since it is almost inevitable that an employer's termination will be contested in arbitration or court, the employer needs to approach the possibility of termination with the caution.

The Employer's election to terminate the Contract does not prejudice any other rights of the Employer, under the contract or otherwise. This preserves a party's common law right to accept a repudiatory breach of contract and terminate the contract.

## **V. Procedures for Termination of Construction Contracts**

Contract provisions often lay down processes to be followed by a party seeking to exercise the right to terminate. Typically, if one party breaches a specified provision of the contract, the other party may issue a notice to 'show cause' requiring the contractor to give reasons why the contract should not be terminated. If the party fails to show cause, or the reasons are not satisfactory, the contract can be terminated. The right to terminate for failure to 'show cause' must be exercised reasonably (perhaps even where that requirement is not expressly stated).<sup>58</sup> Notices serve many important functions in construction projects. They are the means by which employers (usually acting through a contract administrator) issue instructions for matters such as variations, and the way contractors are able to claim for extensions of time and additional cost. They are also, crucially, the means by which either party may seek to terminate the contract.<sup>59</sup> The major FIDIC forms of contract (the 1999 Red, Yellow and Silver Books) contain almost identical provisions on notices. Where a contractor default is alleged, the employer is required to first issue a "notice to correct" prior to issuing a notice of termination. The notice to correct provisions in sub-clause 15.1 of the FIDIC Red Book permits the Engineer to issue a Notice to the contractor about a failure to carry out any obligation under the contract. The Engineer can require that the contractor make good the failure and remedy it within a specified reasonable time. The remainder of sub-clause 15.2 of the FIDIC sets out the procedure to be followed in the event of an employer's termination for cause "In any of these events or circumstances, the Employer may, upon giving 14 days' notice to the Contractor, terminate the Contract and expel the Contractor from the Site. However, in the case of sub-paragraph (e) or (f), the Employer may by notice terminate the Contract immediately". With the exception of sub-paragraph (e) or (f), it is unusual for the trigger event to discharge the contract automatically.

Clause 1.3 of the Red Book sets out that all notices must be in writing and delivered by hand (against receipt), or sent by mail, courier or by e-mail (if email is specified in the contract). The notice must be sent to the address specified in the contract, unless either the recipient gives notice of another address or sends a request for approval or consent from a new address (this might occur, for example, if the contractor sends a request from a different email address). As part of the termination process, the question as to whether or not a notice has to strictly comply with contractual requirements is an important one. The basic rule for the service of notices is that all contractual requirements must be strictly complied with, otherwise the termination may be deemed wrongful. As Lord Hoffman said in *Mannai Investments Co Ltd v Eagle Star Assurance* "If the clause had said that the notice had to be on blue paper, it would have been no good serving a notice on pink paper, however clear it might have been that the party wanted to terminate to satisfying all the contractual requirements, an effective and valid notice "must be sufficiently clear and unambiguous to leave a reasonable recipient in no reasonable doubt as to how and when the notice is intended to operate"<sup>60</sup>. In the case of *Vivergo Fuels Ltd v Redhall Engineering Solutions Ltd*<sup>61</sup>, the court adopted the following principles in interpreting notices: unilateral notices are to be interpreted in the same way as contractual documents. They are to be looked at objectively, against the relevant background or context known to both parties. The question is "how would a reasonable recipient understand it?", the reasonable recipient would have the terms of the relevant underlying contract in the forefront of his mind when reading the notice; the notice must be sufficiently clear and unambiguous to leave a recipient in no reasonable doubt as to how and when the notice is intended to operate; immaterial errors will be ignored if the notice unambiguously conveys the purpose; and in the context of clauses which require a warning notice followed by a termination notice, the two notices must be connected both in content and time. In *Architectural Installation Services v James Gibbons Windows*<sup>62</sup> the court held that an ordinary, commercial businessman would not see a sensible connection between a warning notice and a termination notice that were issued some 11 months apart.

Contractual notice provisions should be strictly observed. Broadly speaking there are two approaches, which may be described as the formalistic<sup>63</sup> approach and the common sense business approach. The formalistic approach construes the contract termination notice very strictly. In New Zealand, the courts have held that termination clauses must be complied with to the letter if they were to be relied upon.<sup>64</sup> In contrast is the approach adopted by the English case of *Goodwin v Faucet*<sup>65</sup> which construed the relevant contract in a 'common sense businessman' way when deciding whether a termination was effective.<sup>66</sup> In *ObrasconHuarte Lain SA v Her Majesty's Attorney General for Gibraltar*,<sup>67</sup> Justice Akenhead stated that within the context of building and engineering contracts, commercial realities need to be taken into account including what was the "primary purpose" of the clause.<sup>68</sup> If the purpose could be achieved without strict compliance, as was the case here, then strict compliance was not necessary. However, the Judge was also keen to stress that termination was a "serious step" and that there "needs to be substantive compliance with the contractual provisions to achieve an effective contractual termination". This required the notice to be given in sufficiently clear terms, and served on a person with appropriate seniority within the company. It is clear that under the FIDIC forms of contract a "commercially realistic interpretation" needs to be taken, and that strict compliance is not necessary in order for a termination notice to be effective. That said, in all cases it will be necessary to show that the notice has actually been served, and the easiest way to do this of course will be to comply with the contractual provisions. Whether or not a particular provision is mandatory will be a question of interpretation; if the court finds that a mandatory requirement has not been complied with, the notice will be invalid.<sup>69</sup>

Once the 14 days' notice under the FIDIC has been given then the employer should wait for the 14 days to elapse before expelling the contractor from site. In *Final Award in Case 1089211*<sup>70</sup> the employer failed to wait the 14 days before entering the site. The arbitral tribunal, considering a similar provision under Clause 63 of FIDIC's 4th edition, held that the failure to wait was a violation of Clause 63.1(e). On appeal to the High Court of Trinidad and Tobago, the court inferred that this failure to wait the 14 days may have been a breach of clause 63.1(e) but might not have resulted in the termination being wrongful.<sup>71</sup> The requirement to give 14 days' notice gives the contractor a final opportunity to comply with the relevant obligation or discuss the issue with the employer. It is unclear whether the notice has automatic effect; that is whether the contract is terminated automatically 14 days after a valid notice has been given under sub-clause 15.2 or whether the employer must give a further notice of termination. This sub-paragraph does not mention whether the employer's right to terminate is lost after giving the required 14 days' notice if the contractor resolves the event or circumstance giving rise to the notice. This is a potential area of uncertainty that the parties might want to clarify before concluding the contract. To be on the safe side, it may be advisable for the employer to give the contractor notice that the contract has been terminated on the expiry of the 14-day period.

Where a contract contains no express termination provisions, in some cases the courts may imply a right to terminate on reasonable notice, particularly where the contract is for an indefinite period. In *Debenhams Properties Ltd*<sup>72</sup>, the court considered a clause in an agreement for lease which allowed termination if "either party shall in any respect fail or neglect to observe or perform any of the provisions of this Agreement". It concluded that the clause did not, in fact, allow termination for just any breach, however minor. In the case the judge accepted that, taken out of context, the words of the clause might be understood to allow termination for any breach, however minor. However, in the context of the agreement, that could not have been intended. Where a party is terminating for repudiatory breach under the common law, the innocent party may not need to comply with a notice and cure period. The common law right to terminate is not affected by the restrictions in the contract which applied only to contractual rights to terminate. In *Vinergy International (PVT) v Richmond Mercantile Ltd FZC*<sup>73</sup>, Richmond entered into a long term agreement to supply bitumen to Vinergy. Richmond sought to terminate the agreement on common law grounds based on the breach of the exclusivity clause. Richmond also sought to terminate on common law grounds based on Vinergy's non-payment of an invoice and other charges. Under the contractual termination procedure Richmond would have been required to give Vinergy an opportunity to remedy its breaches before being able to terminate the contract. Because Richmond was purporting to terminate the contract at common law, it did not follow this procedure. Vinergy argued that Richmond's failure to give it an opportunity to remedy the alleged breaches in accordance with the contractual termination clause was unlawful amounting to wrongful termination. The contractual termination clause provided:

Either party may terminate this Agreement immediately upon: (i) failure of the other party to observe any of the terms herein and to remedy the same where it is capable of being remedied within the period specified in the notice given by the aggrieved party to the party in default, calling for remedy, being a period not less than twenty (20) days...

The High Court disagreed that the contractual termination procedure would also automatically apply when a party sought to terminate at common law. Whether a termination at common law had to comply with the contractual requirements is a matter of interpretation of the particular provisions in the contract. It is pertinent to state here that a sudden termination of construction contract without notice and cure period may be very risky. A

cautious approach would be to comply with the contractual procedure even when terminating at common law, whilst making it clear that the termination is at common law. This means that generally where a breach is capable of being remedied, an opportunity to do so should be given prior to a contract being terminated at common law. The position under Scots law, specifically, is that a party in material breach should be given a “second chance”.<sup>74</sup>

A wrongful termination of the performance of a contract will constitute a repudiation of obligation.<sup>75</sup> If a contract is terminated without cause, but the employer states that the termination is “for cause,” the contractor can sue to recover for wrongful termination. The contractor would be entitled not only for compensation for work performed prior to termination, but also the net profit the contractor anticipated making on the unperformed portion of the contract.

## VI. Conclusion

Termination of contract at common law is a serious step which should be taken only after careful consideration. The right to terminating a construction contract depends on the nature and the seriousness of the consequences of the other party’s breach. The breach must either be of a fundamental term of the contract, often described as one that goes to the root of the contract, or alternatively the consequences of the breach must be such that they substantially deprive the innocent party of the entire benefit intended by the contract, otherwise the risk of a counter-claim for wrongful termination is obvious. A cautious approach is called for when utilising termination clauses that extend the rights of the party beyond the common law position. Where a procedure is laid out, it must be followed to the letter. The case of *Diploma Construction v Marula*<sup>76</sup> shows that courts do not offer lenience to those who liberally interpret the contract clause to their own benefit to achieve termination. In that case, the West Africa Court of Appeal examined whether a building contract had been legally terminated. Marula was a plastering subcontractor engaged by Diploma to carry out solid plastering on a three-storey multi-unit development. The contract included clause 8.1(a): If (Marula):- (a) fails to carry out any of its obligations under this Subcontract and fails to rectify the default within 3 days of becoming aware of details of the default (by notice from (Diploma or otherwise)); Diploma may, at any time and without prejudice to any other rights or remedies available to it under this Subcontract or otherwise, by notice to Marula terminate this Subcontract. On any view of it, this is a draconian termination clause in that the 3 - day period for remedy of any default after “becoming aware of details of the default” is very short in the context of a construction project and further, the clause renders every obligation under the contract to be a “condition”.

As a practical solution to the problem of termination, it is always important to assess the relationship between the parties before terminating – if there is an on-going relationship, an alternative approach may be appropriate, for example, formally renegotiating the contract with a view to varying its terms, or following a prescribed dispute escalation procedure (or instituting one) to try to achieve a mutually acceptable solution. In summary, a contracting party proposing to terminate a construction contract should assess the reasons for proposing to terminate the contract; assess whether such reasons are grounds for termination under the construction contract and/ or common law; understand the procedural steps required before formally terminating the construction contract; assess potential exposure to damages in the event of wrongful termination; and most importantly, analyse and exhaust all possible alternatives to termination, given the very serious consequences of termination.

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- [9]. *Laurinda Pty Ltd v Capalaba* [1989] 166 CLR 623.
- [10]. *Progressive Mailing House Pty Ltd v Tabali Pty Ltd* [1985] 157 CLR 7.
- [11]. *Sutcliffe v. Chippendale & Edmondson* [1971] 18 BLR 149.
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- [13]. *Haji Abu Kassim v Tegap Construction Sdn Bhd* [1981] 2 MLJ 149.
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- [16]. *DCMD Museum Associates v Shademaker (M) Sdn Bhd* [1999] 4 MLJ 243.
- [17]. *Bentsen v Taylor Sons & Co* [1893] 2 QB 274, 281.
- [18]. *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* [2007] HCA 61.
- [19]. *Tramways Advertising Pty Limited v Luna Park (NSW) Pty Ltd* [1938] 38 SR 632.

- [20]. (1938) 38 SR (NSW) 632, 641-2.
- [21]. Hong Kong Fir Shipping Co. Ltd -v- Kawasaki Kisen Kaisha Ltd [1962] 2 QB 26, 70.
- [22]. Above.
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- [24]. New York Life Insurance Co. v. Viglas, 297 U.S. 672, 681 (1936)
- [25]. Forward Publications, Inc. v International Pictures, Inc., 277 App. Div. 846, 98 N.Y.S.2d 139 (N.Y. Sup. Ct. 1950).
- [26]. Palmiero v SpadaDistrib. Co., 217 F.2d 561 (9th Cir. 1954).
- [27]. Daniels v Newton, 114 Mass. 530 (1874).
- [28]. Wonalancet Co. v Banfield, 116 Conn. 582, 165 A. 785 (1933).
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- [31]. Hixson Map Co. v Nebraska Post Co., 5 Neb. 388, 98 N.W. 872 (1904).
- [32]. White and Carter (Councils) Ltd v McGregor [1962] AC 413.
- [33]. Matthews v Smallwood [1910] 1 Ch 777, 786.
- [34]. Peyman v Lanjani and Others [1985] Ch 457; Kendall v Hamilton [1878-79] 4 App. Cas. 504.
- [35]. Force India Formula One Team Ltd v Etihad Airways PJSC [2010] EWCA Civ 1051, [2010] All ER (D) 41, 122.
- [36]. StoczniaGdanska SA v Latvian Shipping Co (Repudiation) [2002] 2 All ER (Comm) 768.
- [37]. Hain Steamship Co Ltd v Tate and Lyle [1936] 2 All ER 597; Bentsen v Taylor Sons & Co [1893] 2 QB 274.
- [38]. Jobi Trade Investment Ltd. v AdelekeOlubusi [2015] All FWLR 1871, 1872.
- [39]. Aaron Silberman, 'How State and Local Public Agencies May (or May Not) Terminate Construction Contracts' (2016) 36 Construction Lawyer 17.
- [40]. American Institute of Architects, AIA Document A201 contains general conditions.
- [41]. There is a draft new standard form general conditions of contract AS 11000, 2015 to supersede AS 4000 and AS 2124.
- [42]. Brazell, v Windsor, 682 S.E.2d 824, 826 (S.C. 2009); UHS-Qualicare, Inc. v. Gulf Coast Cmty. Hosp., Inc. 525 So. 2d 746, 756 (Miss. 1987); Wiljeff, LLC, v. United Realty Mgmt. Corp., 920 N.Y.S.2d 495, 497 (App. Div. 2011); Cent. Ark. Found. Homes, LLC v. Choate, 383 S.W.3d 418 (Ark. Ct. App. 2011).
- [43]. Vidalia Outdoor Prods. Inc. v Higgins, 701 S.E.2d 217, 219 (Ga. Ct. App. 2010); Forsyth Cnty. v Waterscape Servs. LLC, 694 S.E.2d 102, 110-112 (Ga. Ct. App. 2010).
- [44]. D'Andrea Bros. v. United States, No. 08-286C, 2013 WL 500346 (Fed. Cl. Feb. 8, 2013).
- [45]. Campbell v. Shaw, 947 S.W.2d 128, 131 (Mo. Ct. App. 1997) (quoting Curt Ogden Equip. Co. v. Murphy Leasing Co., 895 S.W.2d 604, 608-09 (Mo. Ct. App. 1995)).
- [46]. Richard Lord, Williston on Contracts (Lawyers Cooperative Publishing, 4th ed, 2000) § 63.2.
- [47]. Wiljeff, 920 N.Y.S.2d at 497; Madden Phillips Constr. Inc. v GGAT Dev. Corp., 315 S.W.3d 800 (Tenn. Ct. App. 2009); Premier Golf Mo., LLC v. Staley Land Co. 282 S.W. 3d 866, 873 (Mo. Ct. App. 2009); Venture Props., Inc. v Parker, 195 P.3d 470, 489 (Or. Ct. App 2008); Mustang Pipeline Co. v Driver Pipeline Co., 134 S.W.3d 195 (Tex. 2004).
- [48]. McDonnell Douglas Corp. v United States, 323 F.3d 1006, 1016 (Fed. Cir. 2003).
- [49]. Above.
- [50]. See., e.g., Kuswa & Associates, Inc. v. Thibaut Construction Co., 463 So.2d 1264, 1266 (La. 1985).
- [51]. See Hudson v Wakefield, 645 S.W.2d 427, 430 (Tex. 1983).
- [52]. [2013]EWCA Civ 200.
- [53]. Above, per Jackson LJ, 126.
- [54]. 5 Philip Bruner and Patrick O'Connor, Jr., Bruner and O'Connor on construction law (West Group, 2002) §18:4.
- [55]. The broad notion of "commercial common sense" is prominent in the modern law governing the interpretation of written contracts. See for examples Prens v Simmonds [1971] 1 W.L.R. 1381, 1389, H.L.; Lord Steyn said in Mannai Investment Co v Eagle Star Life Assurance [1997] A.C. 749, 771, H.L. ("Words are ...interpreted in the way in which a reasonable commercial person would construe them"); Rainy Sky SA v Kookmin Bank [2011] UKSC 50; [2011] 1 W.L.R. 2900 at [21], per Lord Clarke UK Supreme Court held "If there are two possible constructions, the court is entitled to prefer the construction which is consistent with business common sense and to reject the other".
- [56]. Lord Neuberger (with whom the majority agreed) restricted the extent to which the court could rely on commercial common sense as an aid to depart from the actual language used in a contract. See Arnold v Britton [2015] A.C. 1619 at 15
- [57]. There are also other sub-clauses which give the employer the right to terminate in certain circumstances. See sub-clauses 9.4(b), 11.4(c), 19.6, and 19.7.
- [58]. Renard Constructions (ME) Pty Ltd v Minister for Public Works [1992] 26 NSWLR 234.  
Moustafa, Abu, KhaledAlmedalah and Ahmed Elwan, 'Practical Guide for Termination of Construction Project' (2016) 5 PM World Journal 5.
- [59]. Delta Vale Properties Ltd v Mills [1990] 1 WLR 445.
- [60]. [2013] EWHC 4030 (TCC) para 420.
- [61]. [1989] 46 BLR 91.
- [62]. JM Hill & Sons Ltd v London Borough of Camden [1980] 18 BLR 31.
- [63]. Brown and Doherty v Whangarei County Council [1988] 1 NZLR 33.
- [64]. [1965]175 Estates Gazette 27 per Stephenson J
- [65]. This strict approach was not followed by English Court of Appeal in the case of JM Hill & Sons Ltd v London Borough of Camden above.
- [66]. [2014] EWHC 1028 (TCC)
- [67]. Strict approach was not followed by English Court of Appeal in the case of JM Hill & Sons Ltd v London Borough of Camden, above.
- [68]. London Borough of Camden, above.
- [69]. ObrasconHuarte Lain SA v Her Majesty's Attorney General for Gibraltar, above.
- [70]. ICC International Court of Arbitration Bulletin (2008) 19 (2), 91.
- [71]. HCA No. Cv. 1541 of 2002.
- [72]. [2010] EWHC 1193.
- [73]. [2016] EWHC 525 (Comm).
- [74]. Strathclyde R.C. v Border Engineering Contractors Ltd [1998] SLT 175.
- [75]. John Carter, Breach of Contract (Law Book Company, 1991) 282.
- [76]. [2009] WADC 1