

Cerno

Distinguish; determine; resolve.

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Welcome

Welcome to this newsletter from Cerno, a consultancy providing dispute resolution advice and services to the construction, engineering, industrial and maritime industries and related professions such as lawyers, architects and engineers.

The purpose of Cerno's newsletters is to provide information on matters of general interest and updates on latest the developments in the field of dispute resolution and related case law. In this article consideration is given to the methods of terminating a contract and the potential difficulties arising, whether the termination was in consequence of a breach or for convenience. The right to terminate a contract, if exercised properly, is a powerful tool. If exercised carelessly it can lead to a claim for wrongful termination.

Termination

Neither party to a contract may avoid performance of its duties to the other unless the other party first materially breaches the contract or the contract provides for termination on the grounds of convenience. A party terminating must decide between terminating for cause or for convenience; that decision affects both the termination process and the parties' respective rights and obligations.

"Termination" means that the contract is "discharged"; that is the future unaccrued obligations owed by the parties fall away. The contract does not cease to exist.

The right to terminate exists in common law, but can also be provided for within a contract.

Beware the risks of terminating a contract!

Courts generally do not favour contract terminations and strictly construe contractual requirements. The consequences of getting it wrong are that the party wrongfully terminating a contract (or refusing to perform) entitles the other party to be placed in the same position it would have been absent the first party's breach.

Termination for Cause:

Termination for cause, or for the default of one party, allows the party effecting the termination to pursue damages. If grounds for termination for cause are weak or uncertain the terminating party may consider terminating for convenience instead, rather than risk terminating wrongfully.

Not every breach gives the innocent party a right to terminate for cause. To allow termination the breach must be: of a vital term or a condition (as opposed to a warranty); a refusal to perform; or a sufficiently serious breach of an intermediate, or innominate term.

The right to terminate following breach of a condition does not depend upon how serious the breach is, or how minor the consequences. On the other hand, a breach of a warranty does not absolve the affected party from future performance, no matter how serious; the contract continues and the parties remain obliged to perform their future obligations under the

contract. The only remedy for the breach of a warranty is in damages.

To constitute action entitling the innocent party to terminate on the grounds of refusal to perform there must be an unequivocal intention by words or conduct to abandon further performance, or an intention to perform some essential part of the contract. This gives the innocent party entitlement to treat himself as discharged from further performance.

A breach of an intermediate or innominate term, that is a term that is neither a condition nor a warranty, only justifies termination if the breach is sufficiently serious; that is, it must "go to the root of the contract" or "frustrate the commercial purpose" or "deprive the innocent party of substantially the whole benefit".

Termination for Convenience:

Termination for convenience provisions usually entitle one party to terminate contract at any time without liability for damages the other party might suffer as a result of the termination. Usually this right is without limitation and the party owning the right is free to terminate for any reason; however, limitations can apply and damages will be payable if the termination for convenience breaches those limitations.

Although on the literal meaning a party may terminate a contract without cause, this does not mean that contract can be terminated for any reason whatsoever; there is an implied obligation of good faith and fair dealing limiting the right.

An example of the limitation placed upon the right to terminate for convenience is seen in the FIDIC construction contracts, 1999 edition, where the Employer shall not terminate for convenience for the purpose of executing the Works himself or arranging for the Works to be executed by another contractor.

Wrongful termination and remedies:

Termination must be exercised always in accordance with the reasonable expectations of the other party.

Once the contract is terminated, if the terminated party makes a prima facie showing that termination was wrongful, or in the case of termination for convenience that it was not done in good faith the burden of proving that the termination was correct shifts to the terminating party and an objective standard applies.

In general, a terminating party acts in good faith if its determination of the risk of continuing with the contract is commercially reasonable but termination would be wrongful if it was for the purpose of obtaining a better price from another party; or to evade contractual dispute resolution provisions; or to avoid issuing a change order. Further, the terminating party is prohibited from creating an inconvenience for the other party as an excuse for terminating.

The remedy for wrongful termination is, very often, in financial damages; which can be extensive. The purpose of the remedy is to put the innocent party back into the position it would have been in had the wrongful termination not occurred. This can include not only payment for work done, but also loss of opportunity/loss of profit on the balance of work that remained at the time of termination.

Practical Issues:

A few practical considerations to be made when contemplating terminating a contract are:

- When entering into agreements, look carefully beforehand at the termination provisions. There is often an imbalance of power between contracting parties, leading to "unfair" terms.
- Once in a contractual arrangement and thought is given to termination, be certain of the grounds on which the termination will be made and state those grounds clearly. Observe and comply with any contractual requirement for the giving of notice before termination and, where applicable, allowing the defaulting party a reasonable opportunity to rectify the default.
- After issuing a notice threatening termination be careful not to take too long or engage in conduct which could be seen as an affirmation of the contract.
- Once the innocent party becomes aware of a breach or ought to have known of it has a reasonable time in which to take steps to mitigate. You cannot recover loss that could reasonably have been avoided but the duty to mitigate only requires a party to act reasonably, taking steps which are "in the normal course of business".
- Properly drafted provisions may allow a termination for cause to convert to a convenience termination if it is later determined that there was no default, so long as the obligation for of good faith and fair dealing is satisfied.

CIArb News

*News for members of
the Chartered Institute
of Arbitrators in Trinidad
& Tobago*

The Trinidad & Tobago chapter of the Chartered Institute of Arbitrators (CIArb) is a sub-branch of the regional, Caribbean Chapter and is looking to host regular meetings for its members; however it needs one or more venues.

If anyone can provide a suitable meeting place preferably with light refreshment facilities, to accommodate up to 50 persons, please contact Cerno.

Anyone interested in joining the CIArb can obtain information directly from the Institute (www.ciarb.org) or by writing to info@cerno.org.

Upcoming Events

It is intended that Cerno's newsletters will include details of local happenings and events of interest. Anyone wishing to have details of an event considered for inclusion here should write to info@cerno.org and provide relevant details.

Contact Information

Cerno can be contacted by e-mail to info@cerno.org.

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