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INSIGHTS

Chapter 2

Strategic ends: some important decisions to be made about the terms of the contract

- Time: is it to be or not to be of the essence?.....18
- Positive obligations: firm undertakings or endeavours?20
- What is the distinction between ‘best endeavours’ and ‘reasonable endeavours’?.....20
- Other cases distinguishing between reasonable endeavours and best endeavours21
- Are there any problems in enforcing endeavours clauses?.....22
- Third party rights: should these be permitted, restricted or excluded?.....23
- Controlling assignment.....23
- The creation of a trust of the benefits arising from a contract.....25
- The Contracts (Rights of Third Parties) Act 199927
- Termination provisions: the choices to be made.....30
- Clauses providing for termination for breach of contract: the attitude of the courts31
- Material breach; substantial breach; repudiation33
- The nature of the breach.....33
- Material breach35
- Termination in relation to other remedies36

Chapter 2

Strategic ends: some important decisions to be made about the terms of the contract

Time: is it to be or not to be of the essence?

This is probably the most important question to be answered in approaching time obligations in a commercial contract. Whether the parties agree that time is to be of the essence or not will depend a great deal upon the overall commercial strategy that one or both of the parties will have in mind when negotiating the contract. With some commercial transactions, time is not critical and there will be no need to set particular deadlines. With others a delay amounting to a few minutes will be of commercial importance. It is in these latter instances that time is most likely to be of the essence. The fact that time is of the essence can sometimes be inferred from the nature and circumstances of the contract. However, there will be instances when either of the parties will wish to make it clear by the terms of the contract, one way or the other, whether or not time is of the essence. All that will be needed is a simple statement such as ‘time for the delivery of goods is of the essence’, or ‘time for the delivery of the goods is not of the essence’.

These statements can also be put into ‘plain English’ versions and in consumer contracts it would not be advisable to use the words ‘of the essence’, unless one is prepared to add in ‘plain English’ details of what is meant, since otherwise the terms might not be sufficiently plain for a consumer to be capable of understanding their true meaning. We will deal with this point in more detail when we look at the ways in which the validity of a contract can be contested in Chapter six.

The consequences of time being of the essence

Where the contract makes time of the essence, time is a condition of the contract, that is, a major or fundamental term. This means that the smallest breach, and even an unintentional breach of the term, will entitle the other party to terminate or rescind the contract. These are harsh consequences, but two cases will demonstrate their application.

Lombard North Central plc v Butterworth (1984) 2 W.L.R. 7

In this case, involving the leasing of a computer, time for payment of each instalment due to the lender had been made 'of the essence'. This meant that even an unintentional delay in making payment would permit the lender to exercise the same remedies against the borrower as if there had been a repudiation by the borrower. This had particularly harsh consequences for the borrower, who argued that what was being imposed upon him amounted to a penalty. However, the Court of Appeal held that to put into a contract a term making time for payment of the essence is to make a choice about the nature of a term, and this is not the same thing as stipulating damages (although it may affect the assessment of damages). So it did not amount to a penalty.

Union Eagle Ltd v Golden Achievement Ltd (1997) 2 All.E.R.

In this important case there was a contract for the sale and purchase of a flat in Hong Kong. In the contract there was a clause which stated that time was of the essence 'in every respect'. (This is somewhat unusual in ordinary domestic conveyancing, but may sometimes be a feature of a commercial conveyance of a particularly desirable property.)

Further, the contract stated that if the purchaser failed to complete in time, the deposit would be 'absolutely forfeited for liquidated damages (and not a penalty)' to the vendor. There was the usual deposit of 10% of the purchase price.

As it turned out, the cheque for the purchase price was delivered ten minutes too late, and the vendor rescinded the contract and claimed that the deposit was forfeited.

The purchaser raised a number of arguments which were eventually heard in the Privy Council. One of these was based on waiver, but this argument was clearly unsustainable. Another argument was that the forfeiture clause amounted to a penalty. This argument was prompted by the unfortunate drafting of that particular term, which referred to 'liquidated damages'. If the retention of the

deposit had been a form of liquidated damages, then arguably it could indeed have been a penalty, since the sum may not have been a genuine pre-estimate of likely loss to the vendor. But the Judicial Committee of the Privy Council held that this was a deposit, and the forfeiture of a deposit is not the same thing as damages. The rule against penalties would only have applied in the circumstances if the deposit had been too large to be a genuine deposit.

Finally, the appellant argued that equitable relief should be granted against the harsh consequences of time being of the essence. The Judicial Committee held that there was no general principle of equitable relief in this area, and that there were no specific grounds in this particular case. It was stated by Lord Hoffmann that if the court accepted the argument that ten minutes delay was not late enough for the normal rules of breach of an essential term to apply, then it would frequently be faced with arguments about how late was too late. So the usual rules applied.

Positive obligations: firm undertakings or endeavours?

When we draft terms about the things that each party is to do for the other, it is important to appreciate that there is a significant choice to be made as regards each term of this kind. The term can be a definite promise to do something (for example, a promise to pay a specified sum at a specified time) or the term can consist of a promise by one party to use ‘best endeavours’ to do something, or a promise to use ‘reasonable endeavours’ to do something. Each of these expressions has a different shade of meaning.

What is the distinction between ‘best endeavours’ and ‘reasonable endeavours’?

The difference between ‘reasonable endeavours’ and ‘best endeavours’ is that with best endeavours cost is not normally a material factor, whereas with ‘reasonable endeavours’ financial matters can be taken into account in deciding what is reasonable. There is an element of the subjective with reasonable endeavours, as the *Phillips v Enron* case shows.

Every term has to be taken as a whole and in its context.

Phillips Petroleum Co UK Ltd v Enron Europe Ltd (1997) CLC, 329

In this case there were long-term contracts that included the construction of facilities, as well as the sale and purchase of gas. The terms left certain terms to be agreed and stated that the parties were to use reasonable endeavours to agree as much in advance as possible, but in any case not less than 30 days in advance of the date on which the seller would commence deliveries of gas to the buyer (the commissioning date). The parties were also under an obligation to use reasonable endeavours to coordinate the construction of their facilities and to develop operationally necessary procedures.

The buyer argued that it was entitled to take into account its own financial position when seeking to agree a commissioning date. The seller argued that the only criteria were technical and operationally practical criteria (i.e. financial criteria were not relevant).

The Court of Appeal held by a majority that, when taken in their contractual setting, and in particular in view of the fact that there was a fall-back date if the parties were unable to agree, the words used did not impose upon the buyer an obligation to disregard the financial effect upon the buyer of agreeing a commissioning date.

Other cases distinguishing between reasonable endeavours and best endeavours

Sheffield District Railway Co v Great Central Railway Co (1911)

‘Best endeavours’ to develop through and local traffic meant ‘not second best’, and that the performing party should ‘leave no stone unturned’ and that there was ‘a duty to investigate alternative methods of performing the agreement’.

UBH (Mechanical Services) Ltd v Standard Life Assurance Co (1986) The Times, November 13

‘Reasonable efforts’ meant that the duty to perform had to be balanced against the performing party’s own commercial interests, its own financial situation, costs, etc.

P & O Property Holdings Ltd v Norwich Union Life Assurance Society (1994) EGCS

A covenant by a developer to use reasonable endeavours to obtain a letting did not create an obligation to pay substantial reverse premiums to attract tenants.

Are there any problems in enforcing endeavours clauses?

The answer to this is that it depends upon what it is that a party has to endeavour to do. If what has to be done is certain enough, such as delivery of goods, or commissioning of equipment, then a promise to use endeavours to carry out such functions will be enforceable. But if the thing promised is uncertain, such as endeavours to agree, or to negotiate, then the term may fail for lack of certainty.

Lambert v HTV Cymru (Wales) Ltd (1998) E.M.L.R.

In this case a term of a contract between the plaintiff, an author and the defendant, the purchaser of the copyright of the author, provided: 'The Purchaser shall... use all reasonable endeavours to obtain a right of first negotiation from any assignee of the Purchaser for the Author to draw or write 'conceptual' children's books in connection with the Film on terms to be negotiated in good faith...'

This case, as we shall see in Chapter 3, is an important authority on the subject of agreements to negotiate, or related agreements. However, for present purposes we need only note that in the Court of Appeal it was held that this particular obligation to use reasonable endeavours was capable of being enforced. It was argued that the obligation in the clause quoted in this case was too uncertain to be enforceable. However, Lord Justice Morritt stated that it was reasonably clear and sufficiently certain what the contracting party was to do. So, unlike a contract to negotiate, a term that one party would use all reasonable endeavours to obtain a right of first negotiation (i.e. to procure that a third party does something) is certain enough for a court to enforce.

Third party rights: should these be permitted, restricted or excluded?

What this issue has in common with other issues in this chapter is the commercial importance of making an appropriate choice at the outset. There are a number of ways in which all or some of the terms of a contract may become enforceable by a third party. The two parties to the contract have a choice, when making their contract, as to how far third party rights should be permitted, and on what terms.

Putting this into a commercial context, if a third party is permitted to take advantage of a contract, this could be potentially harmful to the commercial interests of one or the other of the two original contracting parties. To exclude, or control the rights of third parties, parties drafting a commercial contract need to bear in mind three concepts:

1. Assignment of rights.
2. The creation of a trust of benefits arising from a contract.
3. The rights of third parties under the Contracts (Rights of Third Parties) Act 1999.

Novation

Since novation can be agreed upon at any time, or declined at any time, it is not usual to draft clauses in a contract either permitting it or restricting it. However, there may be cases where a contract is created between A and B in the knowledge that it will later be novated to a third party. In such cases a provision to this effect may be drafted into the original contract so that:

- the third party is identified,
- a time-table is established, and
- there is a clear commercial expectation that this will occur.

Controlling assignment

Unless the contract contains terms restricting in some way the right of one or both of the parties to assign benefits of that contract, it is assumed as a matter of law that assignment is permitted. However, as Lord Browne-Wilkinson stated in one of the leading cases on this subject, "It is trite law that it is in any event impossible to assign the contract as a whole, including both burden and benefit.

The burden of a contract can never be assigned without the consent of the other party to the contract, in which case such consent will give rise to a novation.” (*Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd (1994) 1 AC 85, 103*).

The right to assign may be controlled in a number of ways: there may be a clause which states simply that neither of the parties may assign any part of the contract. Or the words ‘...without the prior written permission of the (other party)’ may be added. The clauses do not have to be bilateral: there are contracts in which one party, such as a major supplier or purchaser, restricts the right of the party it is dealing with to assign, while not mentioning its own rights to assign, which are assumed to have been preserved.

The Linden Gardens case (1994)

In the case mentioned above, the issue before the House of Lords was whether or not a clause prohibiting assignment, or restricting it in such a way as to require prior permission, was valid in English law. It was argued that as a matter of policy such clauses should be ineffective. However, the House of Lords held that there was no such rule of public policy in English law and these controlling clauses mean exactly what they say, so that where permission is required and there is no permission to assign, a third party will not be able to take the assigned benefit(s).

This raises some important issues of commercial planning. As we have already observed, there will be some instances in which parties actively want some form of restriction of the right to assign. In other cases, however, a restriction of the right to assign will be undesirable, since a purchaser of goods or services may wish to sell onwards, and to include the benefit of any term or contractual warranty relating to those goods or services. In the **Linden Gardens** case, a building had had decontamination work done to it and the question was whether claims relating to this could be enforced by any subsequent owner or lessee of the building, if the benefits of the contract had been assigned. The contract had a clause restricting assignment. The House of Lords held that claims could not be brought by any assignee.

There will be cases when a purchaser of services or goods will need, for commercial reasons, to take steps to preserve third party rights. This could be done by negotiating some form of exception to any prohibition of assignment, or a clause stating that permission to assign, ‘may not unreasonably be withheld’, may improve the position of the party who may wish to assign rights.

Hendry v Chartsearch (1998) CLC

In this case there were data processing and computer services agreements in which there were clauses preventing assignment by one party without the consent of the other 'not to be unreasonably withheld'.

In an action concerning the validity of purported assignments it was held that if the relevant clause is drafted in this way, then there can be no valid assignment unless and until prior permission is sought.

In this case, since no prior permission had been sought, the question of whether such permission could reasonably have been refused was not strictly necessary for the decision. Nevertheless, Lord Justice Evans did give some consideration to this question, and his view gives us an indication of how courts are likely to deal with this issue in the future. He was prepared to look at the facts of the case and at the differences between the assignor and the assignee. Chartsearch would presumably have refused to give permission to assign to Hendry, if such permission had been asked for. The original party to the contract with Chartsearch was a company and could have been made to give security for costs in litigation. The assignee, being an individual, and in any case entitled to seek legal aid, did not have to give security for costs. These were, in the opinion of Lord Justice Evans, grounds which would have made it reasonable for Chartsearch to have refused permission to assign.

The creation of a trust of the benefits arising from a contract

This possibility was first thought of in the nineteenth century but was seldom used commercially. Only recently, as a result of the cases involving *Don King Productions Inc v Frank Warren and others*, have the possibilities of either expressly providing for the creation of a trust, or expressly excluding the creation of a trust of one or more of the benefits of a commercial contract been considered as a normal part of the planning of a commercial contract.

Don King Productions Inc v Frank Warren and others (1998) 2 Lloyds Law Reports

In this series of cases the facts were as follows. A partnership agreement had been entered into by Mr King and Mr Warren, and there were purported assignments by Mr Warren and his company of boxing, promotion, management and

associated agreements. However, the supposedly assigned contracts contained provisions expressly prohibiting assignment. On behalf of Mr Warren it was argued that this meant that no valid assignments had taken place. This would have greatly assisted Mr Warren in his contention that the contracts were not partnership property.

The issues referred to the Chancery Division, and subsequently the Court of Appeal, as preliminary issues were whether, and with what effect, the purported assignment of non-assignable rights could be valid as a creation of a trust. To these questions Mr Justice Lightman, with whom the Court of Appeal agreed, gave the following answers:

1. A trust may exist of a contract.
2. A declaration of a trust in favour of a third party of the benefit of a contract or of the profits obtained from a contract is different in character from an assignment.
3. A clause prohibiting assignment does not extend to declarations of trust of the benefits of a contract.
4. There is no reason why the law should limit the parties' freedom to create such trusts.
5. If one party wished to protect himself against the other party declaring himself a trustee, and not merely against an assignment, he should expressly so provide. This had not been done in this case.

The immediate result of this case was that the parties reached a settlement on the basis that the contracts in question were indeed partnership property. The long-term result is that those who draft contracts might want to make it clear from the outset that they may wish to put into trust for one or more third parties some, or all, of the benefits arising from the contract. If they do this, then they must make sure that the wording of the contract is not inconsistent with this. If, on the other hand, a party to an intended contract does not wish the other party to be able to create such a trust, whether deliberately or unintentionally, then the clause which prohibits assignment will need to be improved and extended so that it also prohibits the creation of any form of trust.

The Contracts (Rights of Third Parties) Act 1999

This Act is one of the most important and far-reaching changes to the law of contract in recent years. Although some of its provisions have now been tested in the courts, its full implications will take many years to become clear. One of its more obvious effects will be to extend to third parties the protection of clauses excluding or limiting liability. This will have powerful commercial effects in areas such as shipping, transport, construction and design, where one of the original contracting parties uses third parties to carry out all or part of the work. This change in the law will be looked at when we deal with limiting and excluding liability.

Another important effect of the new Act will be to confer positive rights upon certain third parties, such as the right to enforce payment, or the right to enforce a warranty, or the right to enforce any terms about performance of duties. To this extent, the new Act will serve a similar purpose to that already served by the assignment of rights, or the assignment of debts. However, the difference will be that there will be no need for an assignment, so a term of a contract restricting or prohibiting assignment will not touch the rights conferred by the new Act. Moreover, the nature of the rights conferred upon third parties will be defined and structured by the Act itself, and not by the law of assignment.

The new Act was passed on 11 November 1999 and came into force at once, but with a period of grace which meant that unless contracting parties expressly agreed to make use of the new Act at once, it would not affect any contracts made before 11 May 2000.

Apart from this commencement provision, there are at least two main issues which have caused some apparent difficulty. These are:

1. To what extent, if at all, could a third party acquire rights under a contract without the two original contracting parties intending this to happen?
2. Once a third party has acquired such rights, to what extent does this tie the hands of the two original contracting parties and affect their ability to alter or to modify terms of the contract or to end the contract by agreement?

Section 1 (1) of the Act states that subject to the provisions of this Act, 'a person who is not a party to a contract (a third party) may in his own right enforce a term of the contract if:

- a) the contract expressly provides that he may, or
- b) subject to subsection (2), the term purports to confer a benefit on him.'

Subsection (2) provides that subsection (1)(b) above does not apply if on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party.

Several points of interest emerge from this text. Firstly, those who wish to make use of the new laws may expressly confer rights upon one or more third parties. The rights are to enforce terms rather than the contract as a whole, so one may select the particular terms to be enforced by the third party, and exclude others.

Secondly, third parties can acquire the right to enforce terms by a rather more indirect method 'if the term purports to confer a benefit on (them)'. This rather obscure provision contains potential dangers. If a third party can successfully claim that a term appears to confer a benefit on him, he can enforce it even though this might not have been contemplated by the parties to the contract. However, subsection (2) enables the parties to the contract to make their intentions clear in this respect if they so wish.

As a result of these provisions it is expected that it will be fairly standard for contract terms to contain a clause stating either that the parties **do not intend any term of the contract to be enforceable by a third party**; or that the parties **do not intend any term of the contract to be enforceable by any third party except where the parties have expressly stated that a named third party may enforce a particular term**.

Nisshin Shipping Co Ltd v Cleaves & Co Ltd and others (2004) 1 Lloyd's Law Reports 38

'This case is, I understand, the first time that the 1999 Act has been before the Courts.'

These are the words of Mr Justice Colman in a case in which shipbrokers sought to enforce terms of a contract made between owners of ships and the charterers of those ships. The terms provided that a commission of two per cent would be paid equally to two companies, one of which was Cleaves. But Cleaves was not a party to the contract.

The Commercial Court held that since the relevant clause of the contract purported to confer a benefit upon Cleaves, Cleaves was entitled to enforce the term under Section 1 of the 1999 Act. Further, since the contracts provided for arbitration, Cleaves was entitled to refer the matters to arbitration, as this is provided for by Section 8 of the 1999 Act.

This case is important not only because it is the first to apply the 1999 Act, but also because it touches upon the subject of the European Convention on Human Rights, a subject which we will look at in Chapter 6.

Identification

Another of the problems posed by the new Act is that under Section 1 (3) a third party can acquire the right to enforce a term either by being named in the contract (as was the position in the above case), or by being identified in the contract as a member of a class, or by being identified in the contract as answering to a particular description.

There need be no problem with named third parties. But the word ‘class’ is very wide, and could include large classes of people who were never intended to enforce terms.

If a description is used to designate third parties who have rights under the contract, then it should be born in mind that even descriptions (or classes) such as ‘members of our group of companies’ can create uncertainties: does the expression refer only to members at the time the contract is made, or to members at the time that a claim may be made? This is the kind of issue that would need to be clarified in the contract.

Variation and rescission

Section 2 of the Act creates further issues. It is headed with the words ‘variation and rescission of contract’, and its main point is to state that in certain circumstances a qualifying third party will be able to tie the hands of the original two parties if they wish by mutual consent to vary or to rescind the contract.

A third party qualifies by having acquired rights under the contract and by making the promisor aware that he intends to rely upon those rights.

The section is complex and its details will not be explored here. However, Section 2, subsection (3) provides that the parties are free to include an express term under which they may by agreement rescind or vary the contract without the consent of the third party.

It is expected that this will become a standard term of commercial contracts if third party rights are not completely excluded.

Termination provisions: the choices to be made

All commercial contracts require provisions for their termination, either because without such provisions the duration of the contract would be unclear, or because one's own client may wish to terminate the contract for good reasons concerning the position of the other party, or because events may have made the performance of the contract different from anything that the parties may have contemplated. In the last of these instances the common law principle of frustration may sometimes have a part to play, but in the absence of a clause providing for termination, the parties may have to resort to litigation to ascertain the true position.

A person drafting the termination provisions for a commercial contract will have to make a number of choices:

1. Should the clause state the termination rights of both parties? If a clause is drafted in this style, it will normally state that either of the parties may terminate the contract if any of the listed circumstances occurs. On the other hand, some lawyers would prefer to have a separate clause for each party, because the events would be different in each case.
2. Should the clause provide only for breach and insolvency, or should it provide for other events, such as change of control, or the departure of or unavailability of key persons?
3. Should the right to terminate be with immediate effect, or only after the expiry of a period of notice? The answer to this depends upon the ground for termination. Where insolvency is involved, it would be sensible to provide for termination by notice to take effect immediately. With breaches of contract, the position may require a distinction to be made between different terms of the contract, so that in the case of those breaches that are capable of being remedied, a stated period of notice would be provided for; while in the case of breaches that cannot be remedied, termination would be by notice to take effect immediately. Any right of either party to terminate by notice without giving reasons should of course provide for a commercially reasonable period of notice.

Apart from these points, it needs to be pointed out that there have been a great many important cases on the subjects of termination and notices. Almost invariably they have arisen out of ambiguities in the wording of the contracts concerned or unreasonableness of the provisions.

Clauses providing for termination for breach of contract: the attitude of the courts

Except in a few cases, such as consumer contracts and consumer credit agreements, clauses providing for the bringing to an end of a commercial contract are controlled by common law principles rather than by statute.

The courts require clear language, particularly where the exercise of a right to terminate on account of breach by one of the parties could bring about harsh consequences.

It is also essential that all provisions about termination should be free from ambiguity.

Wickman Tools Ltd v Schuler AG (1974) AC 235

This case is now much cited as an authority for the proposition that if one wishes to achieve an unusual effect by the wording of a term, very clear words are required.

Lord Reid famously stated:

“The more unreasonable the result, the more unlikely it is that the parties can have intended it, and if they do intend it, the more necessary it is that they should make that intention abundantly clear.”

The case involved an agency and distribution agreement. It required Wickman Tools Ltd to observe a number of terms about promotion of the products of Schuler AG, and all of these terms were described as ‘conditions’. Wickman Tools Ltd also had to use its ‘best endeavours’ to promote and extend the sale of Schuler AG’s products in its territory.

The agreement had only one clause that dealt with the subject of termination, and this was the clause headed ‘Duration of Agreement’. This clause provided for a party who had committed a material breach of the agreement to have 60 days in which to remedy the breach, after having been required to do so. These terms led to litigation. Schuler AG relied upon the status of the terms about the obligations of Wickman Tools Ltd, and argued that any breach of conditions could lead to immediate termination of the contract. Wickman Tools Ltd relied upon the express provision for 60 days’ notice. The House of Lords held that it would take very clear words to displace the natural meaning of the term providing for 60 days’ notice. The meaning of the word ‘condition’ is normally that the

term is so strong that any breach, no matter how small, permits the non-defaulting party to terminate with immediate effect; a period of notice is not normally needed. But presumptive meanings can be displaced when they come into conflict with other terms which are so clear that their natural meaning simply cannot be disregarded. The clause providing for 60 days' notice was simply too clear in its meaning to be disregarded.

Mannai Ltd v Eagle Star Assurance Co. Ltd (1997) AC

This more recent example shows how important it is to be clear about dates or periods for notices to terminate contracts.

In this case a clause in a lease provided that the tenant could determine the lease by serving not less than six months' notice in writing on the landlord, 'such notice to expire on the third anniversary of the term commencement date...'

Purporting to act under this clause, the tenant served notice on 24 June 1994, to end the lease on 12 January 1995. This was more than the required six months' notice, but the landlord argued that the third anniversary of the commencement date was in fact 13 January 1995.

The Court of Appeal held that as '12 January' could not mean '13 January', the notice was ineffective. The majority of the House of Lords held that when the tenant gave the notice he did in fact intend to terminate on the third anniversary, although the words that he used had misdescribed that anniversary.

For practical purposes it becomes clear that if anniversaries are relevant to dates for termination (or indeed any other dates), it would be good practice to state what that anniversary is, as a calendar date. Not least of the problems in the above case is that the tenant may have thought that what was required was a notice to expire at the last moment of the day before the anniversary, or the first moment of the actual anniversary, that is, midnight on 12 January 1995. A good contract term would have left no doubt as to what was really required.

Harbinger UK Ltd v GE Information Services Ltd (1999) Masons C.L.R. 335

Ambiguities in clauses about duration or termination must be avoided.

In this case the parties had entered into an agreement for the supply, support and maintenance of software by Harbinger. The terms of the agreement (as varied) provided for a supply of software for an initial period of three and a half years, and continuing thereafter for automatic renewal of terms of one year, unless

and until terminated by either party upon one hundred and eighty days' prior written notice.

The problem with a term drafted in this way is that it is not clear whether this means that there is an entitlement to at least one year of automatic renewal, or whether the notice can be given in such a way as to take effect at the end of the initial term.

The Court (QBD) opted for the latter interpretation. But it cannot be too strongly stated that a well drafted contract simply does not allow for these arguments.

Material breach; substantial breach; repudiation

If a term provides for termination on grounds of breach by one of the parties, it is helpful to provide for:

1. notice to remedy the breach (if it is capable of being remedied), and/or
2. notice of intention to terminate (either because the breach has not been remedied, or because it is not capable of being remedied).

It is also helpful to specify the nature of the breach that will give rise to the right of the party not in breach to terminate.

As far as notice is concerned, the **Wickman Tools** case already cited shows that the courts are reluctant to construe a term so as to allow for termination with immediate effect (except in recognized cases such as where time is of the essence). But a carefully drafted term may allow for this in the case of breaches which are not capable of being remedied (such as breaches of confidentiality). If a breach is capable of being remedied, then it is sensible to provide for a period of notice in which to remedy the breach, and that if it is not remedied in that time, termination will take effect immediately.

The nature of the breach

Rice v Great Yarmouth Borough Council (2000) TLR

This case concerned contracts for the maintenance and management of sports facilities of the council, and for the maintenance of the council's parks and gardens.

The contracts were for four years. In the event, the council was not happy with the performance of the contractor, served default notices and eventually terminated the contracts. The relevant clause stated:

“If the Contractor commits a breach of any of its obligations under the contract... the Council may, without prejudice to any accrued rights or remedies under the contract, terminate the Contractor’s employment under the contract by notice in writing having immediate effect.”

This term has some useful features but it lacks any qualifications about the nature of the breach, and it lacks any need to give to the defaulting party an opportunity to remedy the breach.

For these reasons the Court of Appeal took the view that the parties could only have intended the literal interpretation of this term to apply to extreme cases, which is to say, to repudiatory breaches. The court stated that single breaches, under this term, would have had to have been repudiatory, while multiple breaches would have had to have been cumulatively repudiatory, to justify termination by notice with immediate effect.

Part of the reasoning behind this case is that with long-term contracts in which the contractor has made considerable investment, without clear words, one would not normally expect the contractor to have put himself at the risk of having the whole contract terminated for comparatively minor reasons. In this respect, the Court of Appeal was following the decision of the *House of Lords in Antaios Compania SA v Salen Redeiera (1985) AC 191*.

Antaios Compania SA v Salen Redeiera (1985) AC 191

In this case the relevant clause in a charterparty provided that ‘on any breach of this charterparty, the owners shall be at liberty to withdraw the vessel’. The owners tried to enforce this clause and bring a charter to an end on the grounds that inaccurate bills of lading had been issued. The House of Lords held that this was uncommercial and unreasonable and conflicted with the whole purpose of the NYPE charter form, and that the contract should not be interpreted so as to defeat the whole commercial purpose.

From the point of view of a lawyer who may wish to give to his client an opportunity to terminate a contract on grounds of breach, it is desirable to avoid the effect of the above two cases, and to avoid the need to prove repudiation by the other party. Repudiation means one or more breaches that are so serious that either they show that the defaulting party has no real intention of performing his obligations, or they effectively deprive the non-defaulting party of a

substantial part of the benefit of the contract. In the **Rice** case, above, it was not possible for the council to prove that the breaches amounted to repudiation.

Material breach

The words ‘material breach’ are more likely to achieve the required effect of being credible and enforceable.

National Power plc v United Gas Company Ltd (1998)

In this case each party had the right to terminate the agreement, which involved the sale of natural gas, with immediate effect, if the breach was ‘material’, and if the non-defaulting party had given seven days’ notice to the defaulting party, within which time the defaulting party could avoid termination by commencing to remedy the breach.

National Power argued that by analogy with the **Antaios** case, if ‘any breach’ in a time charter meant ‘any repudiatory breach’, then ‘material breach’ must also mean ‘repudiatory breach’.

Here it was held, however, that the term had a provision for notice and for remedying the breach. It was not solely about termination. So the approach taken by the judge was less stringent than in the two previous cases. He held in particular that in this context a material breach did not have to be as serious a breach as a repudiatory breach.

When drafting such a term, some lawyers will leave ‘material breach’ undefined, on the basis that it is a breach of greater magnitude than a minor breach, but less than a repudiation. Other lawyers will attempt to define it. It can of course be simply defined in terms of whether it can or cannot be remedied within the period of notice.

An expression best avoided at present is ‘substantial breach’, which has been held to equate to repudiation. The case in which this was said was *Crane Co. v Wittenborg (1999)*, and one of the Court of Appeal judges thought that this would be the case even where there was an opportunity to remedy the breach.

Termination in relation to other remedies

Clauses providing for termination can, if the parties so wish, specify a remedial regime which is available to the non-defaulting party (or even the defaulting party in some instances). There is a presumption that even if such a regime is specified, a contracting party does not intend to abandon its common law remedies (although these may be affected by an arbitration clause).

Stocznia Gdanska SA v Latvian Shipping Co (1998) 1 W.L.R. 574

In, this case the House of Lords reversed the Court of Appeal and held that a clause allowing a shipbuilder to terminate and keep instalments of money paid, and to resell the ship if the buyer defaulted in its payment obligations, did not displace the seller's right to sue for damages and unpaid debts. Only the clearest words would rebut the presumption that exists in favour of keeping one's common law remedies.