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Considering Contract Termination Under English Common Law

By **John Laird** (August 22, 2018, 4:03 PM EDT)

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The judgment of Justice Jonathan Baker early in 2018 in Phones 4U Limited (in administration) v. EE Limited[1] has invited a reminder of the care with which contracting parties should consider their rights when their English law contracts appear to be failing.

Here, we consider how Phones 4U has fit into the developing position of English common law regarding the rights and circumstances claimants and defendants may deploy at trial. The review is in three parts:

- First, how claimants can pursue their rights depending on how they have sought to terminate a contract, and the nexus between the termination and rights of remedy under that contract as against the common law rights they might assert, ending with the most recent addition to the common law framework for claimants in Phones 4U.

- Secondly, this is contrasted with the position of defendants who have terminated a contract, and how the common law generally provides them with greater scope to move beyond what was said at the time of termination.

- Finally, revisiting Phones 4U, a consideration of contractual termination triggers based on insolvency, and their utility where contractual loss of bargain is important to a potential claimant.

Termination Reasons and the Consequences of Choice

It is a well-established first principle that no fundamental loss of other rights is to be assumed in the exercise of rights under a contract.[2] That has been expressly affirmed in the 21st century. For example, the Court of Appeal held that the purported use of a contractual mechanism for determination was not inconsistent with reliance on prior renunciation to discharge the contract.[3]

But contractual drafting is often crucial to the outcome on the nature of the rights a claimant can pursue, and in ways which may take one off-guard. First, an express term as to remedies on termination purporting to provide for common law loss of bargain even where there was not a common law repudiatory breach is penal.[4] That problem may be corrected by designating an event in the contract

as a fundamental breach, such as via a "time of the essence" clause.[5]

It is also the case, and with obvious logic in the common law in this regard, that an election of rights between contractual and common law termination is irrelevant if there is no consequential difference in the remedy available.[6]

However, in Dalkia Utilities Services plc v Celtech International Ltd,[7] a termination letter was solely founded on contractual breach. Here, the court found that there will be inconsistency if citing only a contractual breach gives rise to different consequences than reliance on common law repudiatory breach. An election at trial is no longer possible if the choice has been made to terminate under contract.

Shortly afterward, in Leofelis SA et al. v Lonsdale Sports Ltd et al.,[8] Leofelis had purported to terminate for repudiatory breach, which was found on summary judgment to be a legally ineffective ground. There was a good, but different, reason for termination for repudiation, and that could defend Loefelis from a claim for wrongful termination (discussed further below). But it could not give it a ground for a loss of bargain claim of its own. In essence, Leofelis's own loss of bargain could not be founded on the hypothetical. As noted by the Court of Appeal: "If the premature determination of the contract is for reasons other than those that subsequently emerge, a claim for post-termination loss cannot be sustained."[9]

But that was not the end of the matter. On appeal, Leofelis proposed a new claim framework, by which the act previously asserted as the cause for termination for repudiation was itself caused by a breach that could potentially be a basis for loss of bargain in a chain of causation. The Court of Appeal rejected summary judgment in order to let that newly formulated claim run its course.

Then, in Newland Shipping and Forwarding Ltd v Toba Trading FZC[10] remarks were made obiter in the High Court, suggesting that if a contract termination and a common law termination could not occur together, as discussed in Dalkia Utilities, a purported attempt to exercise both in a termination letter would not be effective to exercise either.

Finally, errors on the face of a termination letter may come to a claimant's rescue at later trial, if the letter can be interpreted as not expressly relying on a contractual termination mechanism.[11]

Perhaps surprisingly, a question remained apparently unanswered until Phones 4U: can a claimant seek a common law remedy in the courts when it had previously terminated a contract not for cause, but for convenience? In that case, Phones 4U Limited (a high street retailer of mobile phones) had entered administration, and sought recovery of monies payable under its marketing contract with EE Limited (a mobile network provider). EE Limited counterclaimed for loss of bargain in Phones 4U Limited no longer marketing and selling its services to consumers owing to the administration. EE Limited had previously terminated the marketing agreement by letter only days after Phones 4U announced it was going into administration, expressly invoking an automatic right to do so for convenience under the contract, and not alleging any breach of contract. Phones 4U Limited moved for summary judgment that EE Limited's loss of bargain counterclaim should be struck out.

Justice Baker was compelled to hold that "None of the authorities is a precise precedent for the situation in this case."[12] More specifically:

> It remains true … that 'acceptance' of a repudiation requires no particular formality or form of words (see Vitol v Norelf). But it must communicate a decision to terminate for the repudiation later said to found the claim, in exercise of the common law right to terminate arising upon that repudiation, if a normal loss of bargain claim at common law is to be viable (i.e. leaving aside the inventive alternative claim suggested on appeal in Leofelis v Lonsdale). Otherwise, the claimant cannot say the termination and therefore its loss of bargain resulted from the repudiation sued upon.[13]

This signals that, while loss of right is not to be assumed as a baseline principle of the common law, a claimant's action for repudiatory breach will fail on the causal nexus if it terminated the contract without signaling the breach. Indeed, Justice Baker confirmed this when he compared the fact pattern of EE Limited's conduct with Newland Shipping, stating that was "a case in which the basis upon which liability was pursued was one of the bases upon which the contract was in fact brought to an end. It decides nothing for a case such as the present, where it is said that the contract was brought to an end upon a sole basis other than that upon which EE now claims."[14] This also explains the comments regarding Leofelis SA et al. in the above passage.

Defending a Position After Termination or Refusal of Performance

Evidently, the general tenor of the English common law is that parties should base claims on reasons which were raised with their counterparty at the time they decided to end their contracts, establishing a causal chain that the contract was ended because of that or those reasons in the first instance. By contrast, policy allows greater scope to a party defending their position against contractual claims arising out of termination (although a party may still be restricted by its earlier decisions or statements in some cases).

Since the 19th century case of Boston Deep Sea Fishing & Ico Co v Ansell,[15] defendants have been allowed to rely on reasons other than those raised at the time when defending a claim for wrongful common law termination. This stands in obvious contrast to the policy restriction on bringing claims for reasons not asserted at the time the contract ended.

Of course, wrongful termination is itself repudiatory and gives rise to a right of damages, as recently reconfirmed.[16] More particularly, the same judgment makes clear that a letter terminating by attempting to accept a repudiatory breach, which makes no attempt to invoke a contractual right of termination, may not be retroactively reinterpreted to do so, but remains itself repudiatory.[17] In this sense, therefore, a defendant is hamstrung by its prior choices if it cannot produce alternative grounds which would have justified common law termination at trial.

What if a party refuses to perform a contract? In circumstances where a contract requires some future performance but a party does not believe the contract has been honored by its counterparty, it may refuse to perform in kind. However, refusal to perform without good reason is itself an anticipatory breach (i.e., the recalcitrant party is not yet in breach of its contractual obligations; it has instead declared its intention not to perform them). Similarly to the case of a claim of wrongful termination, as a general rule a party who refuses to perform a contract for an inadequate reason or no reason at all may later justify the refusal on grounds which it could have raised at the time.

An exception to this general rule is known as the "Heisler qualification:"[18] a defense may not be raised "where if the point had been taken steps could have been taken to avoid the [party claiming anticipatory breach itself] being in breach altogether, either by giving it an opportunity to perform its obligation in time or by enabling it to perform in some other valid way."[19] Again, the policy dynamic

allows defendants room to raise points they could have earlier and did not, but only insofar as it reflects the position that the contract would in such circumstances have come to an end in any event.

Finally, invoking a contractual right of termination for convenience may require a party to honor final contractual obligations even if there were grounds for termination for breach available at the time. In Cavenagh v William Evans Ltd,[20] the defendant company invoked the redundancy framework in a managing director's employment contract. It became clear that it could have terminated the director for gross misconduct, and refused to honor a claim for payment in lieu. The Court of Appeal agreed that the company could not rely on this when it had already chosen to, and had in fact, terminated the employment contract on the contractual redundancy grounds.

Counterparty Insolvency Triggers

Another aspect to the recent judgment in Phones 4U is that the contractual termination ground was an insolvency and administration trigger.[21] Such clauses are naturally typical in commercial contracts. But they are not a ground for termination for cause.

As noted earlier, Phones 4U Limited initially brought proceedings against EE Limited. It was at this time that EE sought to counterclaim, and did so by seeking to imply terms into the contract which made Phones 4U Limited entering into administration a repudiatory breach of its marketing and sale obligations, independent of the trigger EE Limited had previously relied upon to end the contract.[22]

Justice Baker did in fact find in the particular case it was possible such a claim could succeed,[23] although it was not finally determined owing to the dismissal of the counterclaim in general given the original nature of EE Limited's express termination under the trigger.

The circumstances of the developing case law therefore suggest that a full review of potential contract rights will be necessary before a termination letter is sent in these types of circumstances. In an ongoing contractual relationship, Phones 4U indicates that a reflexive termination letter could restrict one's position as a creditor to those payments already crystalized at the time. To advance creditor claims for ongoing performance, a party should look beyond its pure termination rights under such a clause before ending the contract. Further, and given the penalty restriction on express terms as to remedies on termination providing for common law loss of bargain without repudiatory breach, care would need to be taken to ensure the kind of contractual construction sought by EE Limited was possible for one's contract at the drafting phase.

Conclusion

As the above review shows, while the most basic position is that pursuit of contractual rights should not preclude other rights, the grain of policy development has made it clear claimants who terminate contracts must pursue remedies causally connected with the reasons invoked to end the contractual relationship. By contrast, defendants are allowed more room to bring different arguments from those raised at the time of contract termination at trial, as long as they are not fundamentally incompatible with the reasons the contract came to an end.

Furthermore, contractual termination for convenience if one's counterparty becomes insolvent should be considered carefully, given the attendant risk that a creditor could by its choice forego a larger claim than it may otherwise have.

Finally, Phones 4U may be contrasted with the obiter remarks in Newland Shipping. A contracting party minded to terminate under a contractual provision for convenience is warned by the former case that it may wish to add language asserting a common law right to its letter to keep its options open, although it is possible a general invocation of such a right may be treated with skepticism. However, in the circumstances of a choice between a contractual termination for cause and a common law termination, it is very likely that choice may need to be made expressly from the outset of a termination letter, or run the risk that it made be deemed later that no choice was made at all.

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[1] [2018] EWHC 49 (Comm).

[2] Gilbert-Ash (Northern) Ltd v. Modern Engineering (Bristol) Ltd [1974] AC 689.

[3] Stocznia Gdanska SA v. Latvian Shipping Co et al [2001] 1 Lloyd's Rep 537, [2002] 2 Lloyd's Rep 436.

[4] Financings Ltd v. Baldock [1963] 2 QB 104.

[5] Lombard North Central plc v. Butterworth [1987] 1 QB 527.

[6] Stocznia Gdynia SA v. Gearbulk Holdings Ltd [2008] EWHC 944 (Comm), [2009] EWCA Civ 75, [2010] QB 27.

[7] [2006] EWHC 63 (Comm).

[8] [2012] EWHC 485 (Ch), [2012] EWCA Civ 985.

[9] [2012] EWCA Civ 985, [44].

[10] [2014] EWHC 661 (Comm).

[11] Shell Egypt West Manzala GMBH et al. v. Dana Gas Egypt Ltd (formerly Centurion Petroleum Corporation) [2010] EWHC 465 (Comm).

[12] [2018] EWHC 49 (Comm) [118].

[13] [2018] EWHC 49 (Comm) [122].

[14] [2018] EWHC 49 (Comm) [116].

[15] (1888) 39 Ch D 339.

[16] Imperial Chemical Industries Limited v. Merit Merrell Technology Limited [2017] EWHC 1763 (TCC) [260].

[17] Imperial Chemical Industries Limited v. Merit Merrell Technology Limited [2017] EWHC 1763 (TCC) [190].

[18] From Heisler v. AngloiDal Ltd [1954] 1 WLR 1273, 1278.

[19] C&S Associates UK Limited v. Enterprise Insurance Company PLC [2015] EWHC 3757 (Comm).

[20] [2012] EWCA Civ 697, [2013] 1 WLR 238.

[21] Phones 4U [78]

[22] Phones 4U [16], [85].

[23] Phones 4U [54].