Termination Of Contract Under Common Law: Is It A Defence That The Party Seeking To Terminate Was Itself Guilty Of Breaches?

Introduction

In the recent decision of the Singapore Court of Appeal in *Alliance Concrete Singapore Pte Ltd v Comfort Resources Pte Ltd* [2009] SGCA 34, the Court was confronted with a scenario where both parties to the contract had committed breaches and one of them had terminated the contract based on the other's breach, with the other party in turn claiming that the termination was wrongful and as such it was the other party that had repudiated the contract.

One question the Court had to consider was: If A is entitled to treat B as having wrongfully repudiated the contract between them and does so, does it avail B to point to A’s past breaches of contract, whatever their nature?

The decision below is important also because it touches on and gives some illumination on the Court of Appeal’s views on certain issues of common occurrence such as the following:

- whether a party is entitled to treat late payment (or even non-payment) of invoiced amounts as repudiatory conduct;

- whether a party can on hindsight choose to rely on an alternative ground to terminate the contract even though this new ground was not originally cited in the notice of termination (and even if so, what are the qualifications, if any?); and

- whether a party can, by issuing a letter making time of the essence, “convert” a contract provision into a “condition” (when it was not originally one), the breach of which entitles the innocent party to terminate.

Rajah & Tann LLP’s Toh Kian Sing SC, Winston Kwek and Charmaine Lim successfully represented the Appellant in this case.

Brief Facts

Alliance Concrete Singapore Pte Ltd (“the Appellant”) is a Singapore company that manufactures and supplies ready-mixed concrete to the construction industry. Comfort Resources Pte Ltd (“the Respondent”) is a supplier of sand.
By a contract evidenced in a letter from the Appellant to the Respondent dated 27 January 2006 and which the Respondent countersigned by way of acceptance on 6 February 2006 ("the Contract"), the Appellant agreed to purchase sand from the Respondent while the Respondent agreed to supply sand to the Appellant’s seven plants commencing 1 February 2006.

The material clauses of the Contract are set out below:

“2. Quantity

The Sub-Contractor shall supply and deliver to the aforesaid plants an aggregate total quantity of 40,000 +/- 25% metric ton per month.

The Purchaser reserves the rights to adjust the quantity in any manner it deems fit to suit the production requirements/demand.

………………

8. Terms of Payment

60 days from end of each month supply.”

Payments by the Appellant for all the months were late and on 20 July 2006, the Respondent suspended supply of sand to the Appellant to pressurize the Appellant to pay invoices that were due only on 31 July 2006. The Appellant refused to pay unless the Respondent resumed the supply of sand, and requested the Respondent to meet to discuss the impasse.

As at September 2006, despite written reminders by the Respondent, certain invoices issued by the Respondent in respect of sand already delivered to the Appellant and that had fallen due remain unpaid. The Respondent also claimed that the Appellant had consistently ordered less than the requisite monthly contractual quantities.

The Respondent alleged that the Appellant’s failure to pay for sand already delivered amounted to a repudiation of the Contract. The Respondent therefore terminated the Contract on that basis.

The Respondent then commenced proceedings against the Appellant claiming for the outstanding invoiced amounts, loss of profits in respect of sand which the Respondent alleged the Appellant had under-ordered, and loss of profits arising from the Appellant having – by its conduct – terminated the Contract.
The Appellant on the other hand alleged that the Respondent had repeatedly breached the Contract by under-delivering the contracted quantities of sand to the Appellant and subsequently, stopping the supply of sand altogether. The Appellant claimed that the Respondent's conduct in stopping the supply of sand and unilaterally terminating the Contract amounted to a repudiation of the Contract which the Appellant accepted thereby bringing the Contract to an end.

Therefore, the Appellant also commenced separate legal proceedings against the Respondent claiming damages arising from the Respondent's unjustified refusal to supply sand and its premature and wrongful termination of the Contract.

At the trial in the High Court, the Trial Judge held that the Appellant had repudiated the Contract in two ways. First, the Appellant had consistently failed to pay for the sand on time. The Respondent had put the Appellant on notice that timely payment of its invoices was made the essence of the Contract notwithstanding that the Contract was silent on the point. Yet, the Appellant failed to pay for the sand on time. This amounted to a repudiation of the Contract which the Respondent accepted by a letter to the Appellant. Secondly, the Appellant was in repudiation of the Contract by its continuous and persistent under-ordering of sand from the Respondent.

**Holding On Appeal**

**Whether The Respondent Was Entitled To Terminate The Contract**

Whether or not the innocent party is legally justified in terminating the contract depends on whether one of the situations summarised by the Court of Appeal in *Man Financial (S) Pte Ltd v Wong Bark Chuan David* [2008] 1 SLR 663 ("Man Financial") has been satisfied (these situations are set out in the paragraphs below).

But what if the party seeking the termination is not itself “innocent”? The Court observed quite rightly that on the facts, the Respondent was not an “innocent” party because at the time when it sought to rely on the Appellant’s breaches to terminate the Contract, the Respondent was itself in breach of the Contract by suspending the supply of sand to the Appellant (with effect from 20 July 2006) without any right to do so and just so to pressurise the Appellant to pay it the sums owed under the Contract.

Hence, even assuming that the Appellant was in fact guilty of conduct which justified a termination of the Contract (i.e. the conduct and/or its consequences fell within one of the situations summarized above), *does the fact that the Respondent was not itself completely innocent nonetheless disentitle the Respondent from terminating the Contract?*

What was the legal position in the context of the precise factual matrix of
the present case, given the fact that the Respondent was itself in breach of the Contract at the time it terminated the Contract (on 14 September 2006) for the Appellant's breach of the Contract?

Did The Respondent's Own Breach Of Contract Disentitle It From Terminating The Contract?

In this regard, the observations by Kerr LJ in the English Court of Appeal decision of State Trading Corporation of India Ltd v M Golodetz Ltd [1989] 2 Lloyd's Rep 277 at 286 found favour with the Court of Appeal:

“ The fact that in the present case both parties had committed breaches before one of them elected to treat the contract as repudiated appears to me to make no difference whatever; nor the fact that (assumedly) both had been breaches of condition. If A is entitled to treat B as having wrongfully repudiated the contract between them and does so, then it does not avail B to point to A's past breaches of contract, whatever their nature. A breach by A would only assist B if it was still continuing when A purported to treat B as having repudiated the contract and [this emphasis is in the original text] if the effect of A's subsisting breach was such as to preclude A from claiming that B had committed a repudiatory breach. In other words, B would have to show that A, being in breach of an obligation in the nature of a condition precedent, was therefore not entitled to rely on B's breach as a repudiation. [emphasis added]

Applying the above test to the facts, the Court found that the fact of the Respondent's breach of contract in its failure to furnish any sand to the Appellant since 20 July 2006, whilst subsisting at the time of purported termination in September 2006, was not of an obligation in the nature of a condition precedent and did not disentitle the Respondent from terminating the Contract for the Appellant's breaches.

Having found that the Respondent is not disqualified from having an ability to terminate the Contract by virtue of its failure to supply sand from 20 July 2006, the Court turned to consider if the nature of the Appellant's breaches of contract were of such a nature as to justify termination.

Did The Non-Payments By The Appellant Entitle The Respondent To Terminate The Contract?

We have mentioned earlier that the Court was of the view that whether or not a party is legally justified in terminating the contract depends on whether one of the situations summarised by the Court of Appeal in Man Financial has been satisfied.
We now set out these situations for the benefit of the reader:

153 As stated in RDC Concrete, there are four situations which entitle the innocent party … to elect to treat the contract as discharged as a result of the other party’s … breach.

154 The first (“Situation 1”) is where the contractual term in question clearly and unambiguously states that, should an event or certain events occur, the innocent party would be entitled to terminate the contract (see RDC Concrete at [91]).

155 The second (“Situation 2”) is where the party in breach of contract (“the guilty party”), by its words or conduct, simply renounces the contract inasmuch as it clearly conveys to the innocent party that it will not perform its contractual obligations at all (see RDC Concrete at [93]).

156 The third (“Situation 3(a)”) is where the term breached … is a condition of the contract. Under what has been termed the “condition-warranty approach”, the innocent party is entitled to terminate the contract if the term which is breached is a condition (as opposed to a warranty): see RDC Concrete at [97]. The focus here unlike that in the next situation discussed below, is not so much on the (actual) consequences of the breach, but, rather, on the nature of the term breached.

157 The fourth (“Situation 3(b)”) is where the breach of a term deprives the innocent party of substantially the whole benefit which it was intended to obtain from the contract (see RDC Concrete at [99]). (This approach is also commonly termed the “Hongkong Fir approach” after the leading English Court of Appeal decision of Hongkong Fir Shipping Co Ltd v Kawasaki Kisen Kaisha Ltd [1962] 2 QB 26; see especially id at 70.) The focus here, unlike that in Situation 3(a), is not so much on the nature of the term breached, but, rather, on the nature and consequences of the breach.

158 Because of the different perspectives adopted in Situation 3(a) and Situation 3(b), respectively (as briefly noted above), which differences might, depending on the precise factual matrix, yield different results when applied to the fact situation this
court in RDC Concrete concluded that, as between both the aforementioned situations, the approach in Situation 3(a) should be applied first, as follows (id at [112]):

“If the term is a condition, then the innocent party would be entitled to terminate the contract. However, if the term is a warranty (instead of a condition), then the court should nevertheless proceed to apply the approach in Situation 3(b) (viz, the Hongkong Fir approach).”

Applying the above to the facts, the Court held that the Respondent was not entitled to terminate the Contract just by virtue of the Appellants’ non-payment (or even late payment) of the invoiced amounts.

It felt that there was no evidence that the series of delayed payments by the Appellant (coupled with the non-payments vis-à-vis the amounts owed in May and June 2006) constituted a renunciation of the Contract by the Appellant.

The Court was of the view that the Respondent’s argument would have been far more persuasive if the Appellant had not paid the Respondent at all throughout the duration of the Contract. The fact that the Respondent accepted (albeit late) payments from the Appellant suggests that it did not consider the conduct of the Appellant – taken as a whole – as constituting a renunciation of the Contract.

There was no evidence construing the Contract (including cl 8 therein) in the light of the surrounding circumstances as a whole that cl 8 (which sets out the terms of payment) was intended by the parties to be a condition (see Situation 3(a) above).

Looking at cl 8 of the Contract in the context of the Contract as a whole, the Court was also of the view – particularly given the brevity of the clause itself (in which the heading is “Terms of Payment” and the body of the clause itself merely states “60 days from end of each month supply”) – that it was not the intention of the parties that any breach of cl 8, regardless of the seriousness of the consequences flowing from the breach, would entitle the innocent party to terminate the Contract without more.

Notwithstanding this finding, would the Respondent’s letter dated 8 September 2006 – indicating that it will not accept the Appellant’s failure to pay and demanding for full payment of all outstanding sums – nonetheless have the effect of making time for payment of the essence thereby “converting” it into a condition?

The Court answered in the negative. It held that a notice purporting to make “time of the essence” in respect of a breach of a non-essential term does
not serve to make time of the essence so far as the obligations in the original contract are concerned as one cannot unilaterally vary the terms of the Contract by turning a non-essential term into a condition.

In this regard, the Court agreed with Chitty on Contracts (30th edition) when it stated that:

“Given that the notice cannot have the effect of turning the non-essential term of the contract into a condition, the party giving the notice can only terminate where the failure of the other party to comply with the terms of the notice goes to the root of the contract so as to deprive that party of a substantial part of the benefit to which he was entitled under the terms of the contract. Failure to comply with the terms of the notice can therefore only be used as evidence of a repudiatory breach; it is not repudiatory breach per se. “ (emphasis added)

The Court thought that it was clear that the failure by the Appellant to pay the arrears due pursuant to the May and June 2006 deliveries by the Respondent did not deprive the Respondent of substantially the whole benefit of the Contract that it was intended that it (the Respondent) should obtain.

In the circumstances, the Court held that the Respondent was not justified in terminating the Contract for this particular breach of contract by the Appellant (relating to non-payments by the Appellant pursuant to cl 8 of the Contract).

**Did The Alleged Under-Ordering Of Sand By The Appellant Entitle The Respondent To Terminate The Contract?**

At the outset, the Court observed that the alleged under-ordering by the Appellant (raised by the Respondent very close to the actual trial itself) was not expressed in the relevant correspondence by the Respondent to be a ground for termination of the Contract.

However, the Court agreed with the Respondent that although an innocent party must justify an election to terminate for breach of contract by the other party, the authorities clearly establish that any ground of termination which existed at the time of election may be relied upon.

However, this right is not unqualified. The innocent party will not be entitled to rely on a ground not raised at the time of termination if the party in breach could have rectified the situation had it been afforded the opportunity to do so.

This is because it would be most unfair for a promisee to be able to rely on a basis for termination which the promisor could have removed had it been
given an opportunity to do so.

On the facts, the Court found, on a balance of probabilities, that the Appellant would have rectified the under-ordering and ordered the requisite amount of sand if it had been given the opportunity to do so. There would have been no incentive for the Appellant to under-order from the Respondent when faced with a rising market.

The Court therefore held that the Respondent could not have relied upon under-ordering as a ground for terminating the Contract.

Quantum Of Damages

Another issue on appeal was whether the Trial Judge had erred in awarding the Respondent damages (arising out of the Appellant’s breach of contract in under-ordering sand from the Respondent) assessed on the basis that the contractually mandated monthly order quantity is 40,000 mt.

The Appellant’s contention was that the contractually mandated quantity is 30,000 mt and not 40,000 mt as cl 2 of the Contract gives the Appellant a 25 % margin of tolerance to be exercised “as it deems fit to suit the production requirements/demand” (see cl 2 above). The Appellant therefore argued that the reference point for the assessment of damages for under-ordering should be 30,000 mt instead (being the minimum mandated sand quantity to be ordered).

The Respondent’s assertion was that because the Appellant had ordered quantities between 40,320 mt and 50,000 mt, its “production requirements/demand” must in fact be based on these quantities. Hence, the reference number should in fact be increased to these figures rather than decreased to 30,000 mt.

The Court of Appeal agreed with the submissions of the Appellant. It held that the Appellant should not be liable for not doing that which he is not bound to do (i.e. order 40,000 mt of sand). As such, the Court ordered damages for under-ordering to be assessed by reference to the minimum amount that the Appellants were bound to order, which is 30,000 mt. However, it went further to order that 30,000 mt should be the benchmark quantity which the Respondents are required to supply, although the margin of 25 % is only in favour of the Appellants. This aspect of the decision was not fully explained.

Concluding Words

For the reasons summarised above, the Court found that –

(a) the Respondent was not entitled to terminate the Contract based on the non-payments by the Appellant pursuant to a breach of cl 8 of the Contract (failure to pay or pay on time);
(b) the Respondent was *not* entitled to terminate the Contract based on the under-ordering of sand by the Appellant pursuant to a breach of cl 2 of the Contract (under-ordering of sand quantities); and

(c) damages to the Appellant as well as the Respondent should be assessed based on 30,000mt of sand per month.

If you would like more information on the above, please contact Toh Kian Sing SC, or Winston Kwek, whose contact details appear on the left of page 2, or contact the Knowledge and Risk Management Group at eOASIS@rajahatnn.com, and we would be happy to assist you.