

Valid repudiation and consequences of termination

By Amy Douglas-Baker

It is important for contracting parties to understand the circumstances in which procrastination or non-performance of contractual obligations by one party constitutes repudiation of the contract, particularly in the context of a commercial contract.

There are circumstances where it is in the interests of the 'innocent' party to bring a 'dud' contractual relationship to an end, obtain damages, and proceed to make alternative commercial arrangements. In other words, there are circumstances in which it is in the interests of an 'innocent' commercial party to be certain of the steps it can take to bring to an end a faltering or failing commercial arrangement and, in effect, cut its losses.

This article addresses the law that applies to repudiation of contract, examine the circumstances in which courts have found a contract repudiated, and briefly discuss the remedies available to an innocent party.

RELEVANT LEGAL PRINCIPLES

A valid and binding contract may be repudiated by conduct falling into one of two categories:

(i) conduct amounting to a renunciation of liabilities under the contract, which evinces an intention no longer to be bound by the contract; or

(ii) conduct demonstrating an intention to fulfil the liabilities under the contract *only* in a manner substantially inconsistent with relevant contractual obligations and in no other way.¹

Before the contract can come to an end, however, the 'innocent' party must terminate the contract on the grounds of the 'defaulting' party's repudiation.²

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How, then, does an 'innocent' party determine whether the conduct of the 'defaulting' party constitutes repudiation of the contract by falling into either category? When does the conduct of the 'defaulting' party give rise to a right on the part of the 'innocent' party to terminate?

To determine whether the conduct amounts to repudiation, the courts will consider whether the reasonable person in the position of the 'innocent' party would consider that the conduct of the 'defaulting' party conveys renunciation of the contract as a whole, or renunciation of a fundamental obligation or obligations under the contract.³ It is not necessary to show that the 'defaulting' party intended to repudiate the contract. The test is objective.

The legal test to determine whether or not conduct amounts to repudiation can cause difficulty for an 'innocent' party. Because each case will be determined objectively on its own facts, only limited assistance can be drawn from the decided cases. Further, in the context of commercial arrangements, it can be difficult for parties to maintain the objectivity that will be the touchstone for any court in determining whether the conduct of the 'defaulting' party conveys renunciation of the entire contract or a fundamental obligation under the contract.

SOME INSTRUCTION FROM THE DECIDED CASES

Notwithstanding that each case will be determined on its own facts, some instruction can be drawn from the decided cases. Inability, inactivity, procrastination (delay), recalcitrance, or repeated failure in the performance of contractual obligations, can all give rise to repudiation of contract.

For example, it may be that the inadequacies of Party A, revealed only after a contract has been entered into, indicate to the reasonable person in the position of Party B that Party A is unable to perform an essential obligation under the contract. One such scenario might be where a tradesperson enters into a contract for the performance of work that s/he cannot perform for lack of the necessary qualifications or skills. Or it may be that Party A has gone out of business and will no longer be able to meet its obligations under the contract.⁴ Equally, repudiation may arise in circumstances where there has been repeated delay or failure in the performance of a series of obligations under the contract. Repeated or gross failure to adhere to contractual obligations has been accepted as a ground of repudiation.⁵

In assessing whether repeated or gross failure to adhere to contractual obligations constitutes repudiation, a court will consider the circumstances relevant to both the contract and its performance. Such considerations will include

The validity of termination on the grounds of repudiation will depend on the terms of the contract and the seriousness of the alleged breaches.

the nature and context of the contract (including any legislative requirements to which any party is subject), the nature, extent and number of claimed breaches of the contract, the consequences of the alleged breaches and, whether having regard to all such matters, the breaches were sufficiently serious to amount to a repudiation of obligations under the contract giving rise to the innocent party's right to terminate.⁶

Whether procrastination or non-performance constitutes repudiation is a question of fact,⁷ to be determined by reference to the terms of the contract. It is for this reason that construction of the terms of the contract is an essential step in determining whether the conduct

complained of can be characterised as procrastination or non-performance of a fundamental obligation under the contract. In order to construe the terms of the contract, the court will discern the intention of the parties as expressed in the language of the contract in context of the relationship established by that contract. In this assessment, what is relevant is the intention of the parties at the time they entered into the contract. Similarly, any commercial purpose of the parties is also relevant to the proper construction of the contract.⁸

In order to determine the validity of termination on the grounds of repudiation, the court will focus on the terms of the contract, and the seriousness of the alleged breaches. Problems can arise where the innocent party errs in construing the contract, or where there is an issue as to the proper characterisation of the conduct of the other party in the context of the contract. In addition, problems can arise where the contract includes a term that purports to contain a complete statement of the circumstances in which the contract may be terminated. Such terms may or may not operate to exclude any residual common law right to terminate the agreement. Where a contract does contain such a term, there may arise an inconsistency between other terms of the contract, breach of which is said to convey repudiation, and the term purporting to contain a statement of the circumstances, which the parties have agreed, will give rise to a right to terminate. The view taken by the courts of such terms has been strict. Absent clear words, such terms will be construed not as limiting, but as augmenting, common law rights to terminate,⁹ including the right to terminate for repudiation.

Despite these practical difficulties, the doctrine of repudiation focuses on the conduct of the parties and what that conduct conveys as between the parties. What this means is that repudiation can provide a commercially calibrated basis for termination. For example, because repudiation has a prospective focus, it does not require

actual breach to occur before the innocent party can take action to salvage the situation by accepting the repudiation and terminating a 'dud' contract. It is not the case that an 'innocent' party must wait for the other party to actually default in its performance under the contract. Repudiation envisages that a party may evince an intention no longer to be bound by the contract either by its actual (past) or anticipated (future) breach. Whether the conduct said to constitute repudiation does in fact meet the test for repudiation will be determined by reference to whether or not the conduct demonstrates an unwillingness or inability to perform the contract. As indicated above, the test is an objective one.

What commonly sours a commercial relationship is the repeated non-performance of contractual obligations. In such circumstances, the innocent party may be entitled to conclude that the contract will not be performed substantially in accordance with its terms.¹⁰

In *Associated Newspapers v Bancks*, an employee, Bancks, agreed to provide each week a comic strip featuring the character Ginger Meggs, and the employer, Associated Newspapers, agreed to publish the comic on the front page of a particular Sunday paper. Some three years into the ten-year contract, Associated Newspapers decided to publish the weekly comic on the third page of the Sunday paper, contrary to the contract, and continued to do so despite protestation from Bancks. Bancks gave notice and the contract of employment was terminated. It was held that the conduct of Associated Newspapers amounted to a 'refusal to be bound by the contract' which entitled Bancks 'to treat the contract as discharged'.¹¹

More recently, in *Koompahtoo v Sanpine*, the High Court considered the circumstances in which a purported termination on the grounds of repudiation (repeated breaches) would be valid. Koompahtoo and Sanpine entered into a joint venture agreement for the development of residential land. Koompahtoo contributed the land, and Sanpine was to act as development manager. Under the agreement, Sanpine was required, *inter alia*, to obtain rezoning of the land, maintain proper records, and manage the financial aspects of the joint venture. Koompahtoo alleged that Sanpine had failed in its duties in a number of respects, outlined the claimed breaches in a letter to Sanpine, advised that it considered the breaches to constitute repudiation, and advised that it accepted Sanpine's repudiation of the contract. Campbell JA at first instance found substantial breaches of the obligations in respect to record-keeping and finance.¹² The High Court held that there had been repeated and gross breaches of the contract by Sanpine, which had serious consequences for Koompahtoo. As a result of the breaches, Koompahtoo had been deprived of a substantial part of the benefit under the contract, justifying termination of the contract.¹³

The High Court accepted that either breach of an essential term (or condition), or a sufficiently serious breach of a non-essential term (a term that goes to the root of a contract), may constitute repudiation of contract and justify termination by the innocent party.¹⁴ In determining whether

there has been a sufficiently serious breach of a non-essential term, the court will consider whether the breaches have deprived the innocent party of 'a substantial part of the benefit for which it contracted'.¹⁵ The focus of the court's attention is the contract, and the nature and seriousness of the breaches.¹⁶

ACCEPTANCE OF REPUDIATION

It is open to the innocent party to elect whether or not to terminate the contract for repudiation. Once repudiation has been accepted and the contract terminated, the innocent party may pursue damages for breach. Where the innocent party decides not to terminate the contract, that party should be aware that the contract remains on foot, and that the decision not to terminate has consequences. For example, the decision may give rise to an estoppel, or may constitute a waiver of the right to terminate. As the foregoing discussion has shown, it is important that an innocent party consider objectively whether the failures under the contract are sufficiently serious that the conduct of the defaulting party constitutes repudiation.

CONCLUSION

Both practical considerations and the interests of justice require that any right to terminate a contract is limited to serious and substantial breaches of contract.¹⁷ Parties to a contract should realise that courts will therefore not readily find that a contract has been repudiated.¹⁸ Bearing this in mind, an innocent party should take great care to consider the circumstances giving rise to repudiation of contract objectively before electing to terminate a contract on the grounds of repudiation. ■

Notes: **1** *Shevill v Builders Licensing Board* (1982) 149 CLR 620 at 625-6; *Laurinda Pty Ltd v Capalaba Park Shopping Centre Pty Ltd* (1989) 166 CLR 623 at 659, per Deane and Dawson JJ. **2** *Automatic Fire Sprinklers Pty Ltd v Watson* (1946) 72 CLR 435. **3** *Laurinda v Capalaba* at 659, per Deane and Dawson JJ. **4** *Roadshow Entertainment Pty Ltd v CEL Home Video Pty Ltd* [1997] 42 NSWLR 462. **5** Most notably in *Koompahtoo Local Aboriginal Land Council v Sanpine Pty Ltd* (2007) 233 CLR 115. **6** *Koompahtoo v Sanpine* at [5], [32] and [41], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **7** *Forslind v Bechely-Crundall* [1922] SC 173 at 191-2, per Lord Shaw. **8** *Koompahtoo v Sanpine* at [48], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **9** *Concut Pty Ltd v Worrell* (2000) 75 ALJR 312 at [23], per Gleeson CJ, Gaudron and Gummow JJ. **10** *Luna Park (NSW) Ltd v Tramways Advertising Pty Ltd* (1938) 61 CLR 286 at 304-5; *Associated Newspapers Ltd v Bancks* (1951) 83 CLR 322. **11** *Associated Newspapers v Bancks* at 339-40, per Dixon, Williams, Webb, Fullagar and Kitto JJ. **12** *Koompahtoo v Sanpine* at [28], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **13** *Ibid* at [71], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **14** *Ibid* at [47] and [49], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **15** *Ibid* at [55], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **16** *Ibid* at [68], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **17** *Ibid* at [52], per Gleeson CJ, Gummow, Heydon and Crennan JJ. **18** *Shevill v Builders Licensing Board* at 633-4.

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