

Termination for convenience, legal?

STUART JORDAN* tackles the issue of the lawfulness of a provision in contracts for termination for convenience, looking specifically at the UAE law.

ONE of the most common questions in Middle East construction is: Is a contractual entitlement to terminate for convenience (termination “without cause”) enforceable? And if it is enforceable per se, can the exercise of it nevertheless be unlawful?

This comes up for several reasons; firstly, rights to terminate for convenience are popular in the Gulf region, but their efficacy needs to be understood in the light of legal principles. The most relevant of these are the mandatory tenets of contract law which impose limits on the terms that parties can agree. And secondly, we have the overriding duties of good faith and fair dealing in operating those contracts.

These legal principles differ across local jurisdictions but the principles are similar. We’ll concentrate on the UAE.

There is no express bar in UAE law to agreeing a right to terminate for convenience but there is an obvious potential objection in the form of Article 267 of the UAE Civil Code:

“If the contract is valid and binding, it shall not be permissible for either of the contracting parties to resile from it, or to vary or cancel it, save by mutual consent, or an order of the court or under a provision of law”.

Article 892 of the Civil Code (dealing with Muqawala, or construction contracts) is very similar to Article 267, stating that a contract may be terminated (among other ways) by “cancellation of the contract by consent”.

The question is whether, to avoid the need for a court order, “consent” needs to be given after termination has been proposed or whether it can be given in the contract. Relying on the latter reasoning, parties often include a contract term to the effect that their original agreement to the termination provisions constitutes the

“mutual consent” required under the law.

Others argue that such a solution cannot apply to termination for convenience because the contract itself would not be binding, according to Article 218 of the UAE Civil Code:

“A contract shall not be binding on one or both of the contracting parties despite its validity and effectiveness if there is a condition that such party may cancel it without mutual consent or an order of the court”.

What about exercising such rights? According to Article 246 of the UAE Civil Code: *“The contract must be performed in accordance with its contents, and in a manner consistent with the requirements of good faith”.*

The principles of good faith are detailed in Article 106 of the UAE Civil Code:

“(1) A person shall be held liable for an unlawful exercise of his rights.

(2) The exercise of a right shall be unlawful if:

- a. If there is intentional infringement [of the other party’s rights]*
- b. If the interests which such exercise of right is designed to bring about are contrary to the rules of the Islamic Sharia, the law, public order or morals*
- c. If the interests desired are disproportionate to the harm that will be suffered by others; or*
- d. If it exceeds the bounds of custom or practice.”*

This raises a few interesting questions: Firstly, under (a), what is “infringement” of another person’s rights in the context of

exercising rights which that party agreed you may have in the contract? This looks like circular reasoning but clearly the Code is referring to broader rights than those expressed in the contract.

In (b), we see prohibitions on operating a contract which would be in violation of the same principles as would make the contract term itself unenforceable: that is, if contrary to Islamic Law principles, public order or morals.

The grounds at (c) are probably closest to expressing the real policy objection to termination for convenience. It allows one party, for maybe only a marginal gain, to bring about possibly huge harm to the other party in losing the contract.

In conclusion, there is no complete consensus among commentators about the lawfulness of a provision for termination for convenience. It looks more clear at least, that such a provision can

be exercised unlawfully, either when examining the intention behind it (such as to stop a contractor reaching a payment entitlement) or the disproportionate effect of it – such as leaving a contractor with unrecoverable supply chain costs. As always with contentious provisions, enforceability is helped by drafting in clear terms which at least anticipates the objection. That might include acknowledgment that this is a legitimate commercial need for the owner.

Finally, looking at the unlawfulness ground under Article 246(2)(d) – that it exceeds the bounds of custom and practice – I don’t think this can be said of termination for convenience. Right or wrong, lawful or not, this happens a lot in our world! ■

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Jordan ... rights to terminate for convenience need to be understood.