

Right to terminate for convenience revisited

STUART JORDAN* discusses another aspect of a contract provision to terminate for convenience, where it could have the potential to operate as a limit on liability.

WE have previously considered whether a contract provision allowing a party to terminate for convenience is enforceable in the Middle East. We looked at whether it might be unenforceable in itself, because it is in conflict with the law (we looked at UAE Civil Code) or whether the operation of such a provision might be invalid, also on the basis of contravening the Code or the Islamic legal principles which underpin the Code.

These are important points for us, given that most Middle Eastern construction contracts contain provisions allowing one party (the owner in a main contract or the main contractor in a subcontract) to terminate for convenience – or “at will” or “without cause”.

A recent dispute has touched on another aspect of termination for convenience: the potential that it will operate as a limit on liability. The logic is this: if a party is in breach and has incurred liability to the other party, the calculation of that liability should take into account the question of whether the party in breach could at any time have terminated the contract for convenience. If so, that party’s liability should not exceed the maximum amount that the breaching party would incur on exercising that right.

To put it the other way: if your counterparty can terminate for convenience, your “expectation rights” of your benefit from the future continuing performance of that contract are no more than the agreed consequences of that provision.

That’s the theory anyway. The position (in English Law, at least) has not been fully clarified.

One Commercial Court decision from 2014 (*Comau UK Ltd v Lotus Lightweight Structures Ltd*) conformed to the above principle. Here, the parties entered into a

contract which included a right for Lotus to terminate the contract at any time by giving notice – and provided for the calculation of the sole liabilities of Lotus in that situation.

Lotus failed to make payments. Comau gave notice of termination for breach but also later submitted that Lotus’s actions amounted to repudiatory (fundamental) breach, allowing Comau to accept that Lotus had brought the contract to an end. Comau claimed its loss of expected profit for the remainder of the contract – but failed to recover them because Lotus always had the right to terminate for convenience, so their liability was held to be limited to the agreed consequences of such a termination.

However, in the same year, the Technology and Construction Court took a different approach in a claim brought by a contractor against a local government authority, for failure to award a 10-year term contract to the contractor – in breach of public sector procurement rules. The proposed contract allowed the local authority to terminate by giving six months’ notice at any time after 12 months from the start of the term. The local authority argued, on the above principle, that its liability was limited to sums payable in the first 18 months of the term. The court found that the local authority had not been in breach, which concluded the dispute, but it added anyway that it would have been open to the contractor to argue, with evidence of the way the contract would have worked commercially, that the authority would not in fact have terminated the contract early – so the agreed consequences of such termination would not

necessarily have acted as a cap on liability.

A most recent development takes another twist. This arises under Scottish Law, from a dispute about a contract for sale (by Edinburgh City Council) of scrap metal to a purchaser, Dalton Group. The parties fell out about the content of the scrap metal being delivered. Dalton said that the council stopped deliveries, and that this amounted to a repudiatory breach of contract, so they claimed for the lost profits from the remainder of the contract term. The council denied breach but also claimed (on the above principle) that its liability was anyway limited because it had a right to terminate for convenience on giving three months’ notice.

The court, however, decided that the council’s argument was irrelevant because the contract remained in effect. The council had not terminated the contract and Dalton had not accepted the council’s alleged repudiatory breach as bringing the contract to an end. If there had been such a breach (which is yet to be decided), Dalton had

elected instead to affirm the contract – so they could still pursue their claim for loss of profits for the remainder of the term. In short, Dalton were in a different position from Comau in the first case above, who had claimed that the breach against them had brought the contract to an end.

This decision was only in relation to the council’s liability cap argument. The dispute itself remains to be tried, and I assume that the council could still decide to terminate for convenience.

Would this liability cap argument work in the Gulf? On the one hand, the contractual logic of it is universal. On the other hand, as we discussed earlier, the right to terminate for convenience is potentially at odds with some Gulf legal principles – so there might be reluctance to allow another advantage to be gained from it.

As always, get advice. ■



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