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IN THE JAWS OF A DILEMMA

LITIGATION AND DISPUTE RESOLUTION

If your contractual counterparty commits a repudiatory breach of contract, you are entitled to elect between affirming the contract and terminating the contract. In either case you may bring a claim for damages. Difficulties arise, however, where it is not clear whether or not a court would consider a particular breach to be repudiatory. If a court subsequently decides that the original breach was not repudiatory, terminating the contract will itself be a repudiatory breach, which may give rise to a substantial damages claim against you. This situation arose in the recent case of *Valilas v Januzaj* [2014] EWCA Civ 436, where the Court of Appeal held that a refusal to pay sums due under a contract on time did not give rise to a right to terminate.

DENTISTS IN DISPUTE

The case concerned two dentists, Mr Valilas (V) and Mr Januzaj (J).

J ran a dental practice and V practiced there under an oral agreement (the facilities contract) whereby V could use the premises, equipment and facilities at the practice and in return would pay J 50 per cent of his receipts each month. V received most of his earnings under a contract with the local Primary Care Trust (PCT) where he received a fixed price per "unit of dental activity". Payment was made by the PCT in advance in equal monthly instalments but if V did not achieve the requisite number of units by the end of the year, he had to refund the overpayment to the PCT.

The relationship between J and V broke down in early 2010. V informed J that he would stop making his monthly payments to J. He said this because he was running behind on his units for the PCT and so a rebate could be necessary and he was worried that J would not make the rebate payment at year end. No further payments were made from that date. J subsequently told V that he could no longer work at the practice and excluded him from the premises.

REFUSAL TO PAY ON TIME WAS NOT A REPUDIATORY BREACH

The key issue was whether V had renounced the facilities contract (by saying that he would no longer make his monthly payments) or was in repudiatory breach of the facilities contract (by actually stopping those payments). If so, J was entitled to bring the contract to the end. Otherwise J would himself be in repudiatory breach by excluding V from the premises and would be liable in damages to V for the resultant loss of his contract with the PCT.

It was held at first instance and by the Court of Appeal (by a majority of two to one) that V's refusal to make the monthly payments did not entitle J to terminate the facilities contract. The key points were:

- ◆ Unless the parties agree otherwise, time of payment is not generally of the essence in a commercial contract. Therefore the obligation to make the monthly payments on the due date was not a condition of the facilities agreement, breach of which would automatically entitle J to terminate the contract.
- ◆ Rather, the obligation to pay on time was an "innominate" term. Case law contains a number of formulations of the test for when breaches of an innominate term will be repudiatory, such as where they "go to the root of the contract" or where a breach would "evince an intention no longer to be bound by the terms of the contract" or deprive the innocent party of "substantially the whole benefit" of the contract. While a declared intention by a party to perform a contract in a manner substantially inconsistent with his obligations may amount to a renunciation, the breach involved must be analysed to see whether it has any of these consequences.
- ◆ In this case, the outstanding PCT units could and should have been completed by the year end so that J would receive everything he was entitled to, albeit that some of it would be late. Withholding payment was different from a refusal to pay at all. J had not established that there would be serious consequences for him and his practice from the late payment.

Underhill LJ gave a dissenting judgment in which he took the view that V's refusal to make the monthly payments constituted a repudiatory breach because V had made a deliberate choice to depart from the agreed arrangements.

COMMENT

It will sometimes be difficult to predict with any degree of certainty whether or not the Court will find that a particular breach was repudiatory – as is demonstrated by the fact that, in *Valilas v Januzaj*, the three judges in the Court of Appeal could not agree on this very point. In such a situation, the safest approach may be for you to reserve your rights and to apply to the Court for a declaration as to whether the contract has been repudiated at an expedited trial. However, incurring the costs of applying to court may not always be possible or practical. In that case, you will need to choose between (i) affirming the contract and confining yourself to a claim for damages or (ii) terminating the contract and running the risk that a court subsequently finds that you were not entitled to do so.

We understand that there has been an appeal to the Supreme Court.

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