

The art of termination: how to protect your right to common law damages

Introduction

In *Phones 4u Ltd (In Administration) (“Phones 4u”) v EE Ltd (“EE”)*¹, the English Commercial Court had to decide whether EE could claim for “loss of bargain” common law damages for a repudiatory breach of contract by Phones 4u, even though EE’s termination notice relied solely on a contractual right to terminate. The decision shows that courts will pay careful attention to the drafting of a termination notice when establishing whether a terminating party’s right to common law damages is maintained or extinguished.

Background to EE’s termination

On 8 October 2012, Phones 4u made an agreement with EE to sell EE pay monthly connections until 30 September 2015 (the “**Agreement**”). However, soon after the Agreement was made, Phones 4u started facing a series of financial difficulties, with Three, O₂ and Vodafone all ending their relationships with Phones 4u.

On 12 September 2014, EE followed suit, and notified Phones 4u that it would not be renewing or replacing the Agreement when it expired. That same afternoon, the Board of Directors of Phones 4u met, and in light of the fact that Phones 4u’s contractual arrangements with all of the major mobile network operators were coming to an end, the Board resolved to seek the appointment of administrators. Phones 4u ceased trading on 15 September 2014.

At lunchtime on 17 September 2014, EE sent a termination letter to Phones 4u’s administrators by email. The letter stated that EE was terminating the Agreement with immediate effect, in accordance with clause 14.1.2 of the Agreement (which entitled EE to terminate without breach in certain circumstances, including if administrators were appointed).

Crucially, EE’s termination letter only referred to the exercise of its contractual right to terminate, and did not mention any breach on the part of Phones 4u.

The dispute

Phones 4u brought proceedings against EE seeking unpaid commission fees, and EE made two counterclaims. EE’s primary counterclaim was for common law damages in the sum of £200m for the “loss of bargain” resulting from Phones 4u’s “repudiatory breach”.

Parties to contracts may accrue both contractual rights to terminate (based on the wording of their agreements) as well as common law rights to terminate for a repudiatory breach. A repudiatory breach deprives the innocent party of substantially the whole benefit of the contract, and gives the innocent party a common law right to “accept” the other party’s repudiation and bring the contract to an end.

EE claimed that when Phones 4u ceased trading, it was in breach of its contractual obligation to market and sell EE products throughout the duration of the contract. EE argued that the breach was repudiatory because, at the point of termination, it appeared likely that Phones 4u’s cessation of trade would continue indefinitely.

Phones 4u made an application for summary judgment to dismiss EE’s primary counterclaim. It argued that EE had terminated the contract pursuant to clause 14.1.2, and not in response to the alleged repudiatory breach.

¹ [2018] EWHC 49 (Comm)

Breach by Phones 4u?

Mr Justice Baker found that EE could not allege a breach by Phones 4u after termination, and could only allege that Phones 4u failed to perform the contract on 15 and 16 September and the morning of 17 September (i.e. for 2½ days between the appointment of administrators and termination).

The judge considered that EE did have a real prospect of establishing breach (for the 2½ days), and a real prospect of establishing that the breach was repudiatory. However, he determined that for EE's counterclaim to succeed, it would need to show that the termination of the contract, which created the loss of bargain, was by its exercise of its common law right to terminate for Phones 4u's repudiatory breach. If EE's termination was solely based on a contractual right arising independently of any breach, its counterclaim would fail.

EE's termination letter

In its termination letter, EE had not identified any breach by Phones 4u as causing, justifying or having relevance to its decision to terminate the Agreement, even though grounds for arguing a repudiatory breach did in fact exist. The judge concluded that EE's termination letter had communicated unequivocally that EE was terminating only in exercise of its contractual right to do so.

Following previous case law authority, Mr Justice Baker found that a decision to terminate for a repudiatory breach that is later relied upon must have been communicated. The fact that valid grounds for terminating for repudiatory breach existed at the time of termination is irrelevant if the terminating party fails to communicate that it is terminating for repudiatory breach.

EE's termination letter had clearly stated that it was not waiving any breach that might exist, any rights in respect of which were reserved. However, the judge stated that "a right merely reserved is a right not exercised", and "EE cannot re-characterise the events after the fact and claim that it terminated for breach when that is simply not what it did".

Conclusions

Based on his analysis of EE's method of termination, Mr Justice Baker determined that EE's counterclaim for damages for loss of bargain at common law could not run, and that the counterclaim had no real prospect of succeeding. He therefore granted Phones 4u's application for summary judgment, dismissing EE's counterclaim.

This decision highlights the need for termination notices to be clearly drafted to state that a party's decision to terminate is based on repudiatory breaches (if such breaches exist), and not merely exercising a contractual right to terminate. Whilst parties may still be able to claim damages for breach of a contractual term (if proven), a terminating party loses the right to claim "loss of bargain" damages at common law if it fails to clearly communicate repudiation as a ground for termination. As this case demonstrates, a reservation of rights and no waiver statement will not sufficiently protect such common law rights. As such, care must be taken when drafting termination communications in order to ensure that when exercising a party's contractual right to terminate, any common law claims for damages are safeguarded.

If you have any questions or comments in relation to the above, please contact the authors or your usual Mayer Brown contact.

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