

## WHEN CAN YOU TERMINATE A CONSTRUCTION CONTRACT FOR BREACH OF CONTRACT?

If a party breaches a construction contract, this will sometimes entitle you to terminate - but not always. This article explains how it works.

### **Overview**

Whether you can terminate a construction contract for breach will depend on two things:

- (a) First, whether the contract gives you an express right to terminate for the breach concerned; and
- (b) Second, whether the breach is so serious that you have a right to terminate outside of the contract (at common law).

There can be circumstances where you can have an express right to terminate under the contract, as well as a separate right outside of the contract.

These two different types of termination right are explained in more detail below.

### **Termination under the contract**

Most construction contracts will contain a clause that lists the types of breach that will allow a party to initiate the termination process (often involving a 'show cause' notice).

For example, in relation to contractor breaches, clause 39.2 of AS 4000 states:

*"If the Contractor commits a substantial breach of the Contract, the Principal may ... give the Contractor a written notice to show cause.*

*Substantial breaches include, but are not limited to:*

- (a) *Failing to:*
  - (i) *provide security;*
  - (ii) *provide evidence of insurance;*
  - (iii) *comply with a direction of the Superintendent pursuant to subclause 29.3 [defective work]; or*
  - (iv) *use the materials or standards of work required by the Contract*
- (b) *wrongful suspension of work;*
- (c) *substantial departure from a construction program without reasonable cause or the Superintendent's approval;*
- (d) *where there is no construction program, failing to proceed with due expedition and without delay; and*

- (e) *in respect of clause 38 [payment of workers and subcontractors], knowingly providing documentary evidence containing an untrue statement."*

Similarly, clause 39.7 of AS 4000 contains a list of substantial breaches by the Principal, which include a failure to provide security or evidence of insurance, to rectify inadequate possession if the failure persists for a specified period of time, or failing to make a payment that is due and payable under the contract.

Where this type of breach occurs, the contract will typically explain the process that must be followed in order to terminate it. If you are the party seeking to terminate, it is critical that you comply strictly with that process.

### ***Termination outside of the contract***

Not all breaches of contract will give you an express right to terminate under the terms of the contract. But there can be breaches that will entitle you to terminate, even if they are not specifically mentioned in your contract.

Putting to one side the concept of repudiation, to be able to rely on a right to terminate that is outside the contract:

- (a) The breach must be sufficiently serious; and
- (b) The provisions of the contract must not be expressed or interpreted to operate as an exclusive list of the circumstances in which the parties can terminate (so as to exclude your right to terminate at common law).

In relation to the first point, some breaches of contract will be relatively trivial. For example, if the contractor breaches an obligation to include certain information in a payment claim, this could be a breach of contract. But it is difficult to imagine this type of breach ever being sufficiently serious to justify termination.

By contrast, if the contractor were to (say) fail to effect the necessary insurances or provide the required security, or to routinely ignore valid directions given by the Superintendent (for example, in relation to safety or to minimise the risk of damaging property), these could be sufficiently serious to justify termination at common law.

### ***Essential terms and sufficiently serious breaches of intermediate terms***

In technical terms, to terminate outside the contract, there must be either:

- (a) a breach of an essential term (or 'condition') of the contract; or
- (b) a sufficiently serious breach of an 'intermediate term' of the contract

A term is essential if a party would not have entered into the contract unless assured of strict or substantial performance of that obligation by the other party. An essential term (or 'condition') goes to the very root of the contract. A contractor's obligation to effect insurance, or provide security, would likely be characterised as essential terms of the contract.

An intermediate term is not as important as an essential term. However there may still be circumstances where a serious breach of an intermediate term will entitle the other party to terminate. A persistent failure by the contractor to comply with directions given by the superintendent could fall into this category, depending on the wording of the contract and the nature of the directions involved.

### ***A recent example***

A recent case in NSW helps to demonstrate the issues.

In this case [here](#), a subcontractor was found to have persistently breached safe work practices and safety obligations despite repeated directions and warnings from the contractor's site supervisor concerning safety.

Although the court found that the safety provisions in the contract were intermediate terms, it also found that the contractor was entitled to terminate at common law due to the repeated and egregious nature of the subcontractor's misconduct.

### ***Practical considerations***

Determining whether you have a right to terminate under the contract is relatively straightforward, in that your contract will usually identify specific circumstances in which the right can be exercised.

In contrast, determining whether you have a right to terminate outside the contract can be more difficult. This is because the common law does not give you a clearly defined, exhaustive list of the circumstances in which you can terminate.

This is why, in a practical sense, you should always start with the terms of your contract to see whether termination is expressly permitted for the breach concerned. Your contract will often give you the simplest way forward. Keep in mind, though, that regardless of whether you have a right to terminate under the contract, you may still have a right to terminate at common law (which can be exercised at the same time as any right under the contract).

Having ascertained whether you have a right to terminate, the next step is to work out how to exercise it. This is something we will be writing about in a separate article shortly.



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