NON-PERFORMANCE, TERMINATION, AND COMPENSATION:

SOME PRACTICAL ASPECTS OF THE LAW OF CONTRACT

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1. The purpose of this lecture is to draw attention to, and think about, certain aspects of the law which arise from contract terms which deal with performance and non-performance of a contract, and with terms which deal with the monetary obligations of the party who has broken his or her contract. The general conclusion to which we will come can be stated at the beginning: good and careful during a contractual negotiation will prevent a lot of unhappiness and avoidable expense after something has gone wrong and the parties need to work out what their options are.

2. Let us begin with performance of the contract, and with what happens when performance does not happen as it should.

(A) Terms relating to performance and non-performance

3. What happens when one party has not fully performed his contractual obligations ? The point of departure is Section 39 of the Contract Act, which says this:

> **39. Effect of refusal of party to perform promise wholly**. When a party to a contract has refused to perform, or disabled himself from performing, his promise in its entirety, the promisee may put an end to the contract, unless he has signified, by words or conduct, his acquiescence in its continuance.
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> *Illustrations*
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> (a) A, a singer, enters into a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night A wilfully absents herself from the theatre. B is at liberty to put an end to the contract.
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> (b) A, a singer, enters in to a contract with B, the manager of a theatre, to sing at his theatre two nights in every week during the next two months, and B engages to pay her at the rate of 100 rupees for each night. On the sixth night A wilfully absents herself. With the assent of B, A sings on the seventh night. B has signified his acquiescence in the continuance of the contract, and cannot now put an end to it, but is entitled to compensation for the damage sustained by him through A's failure to sing on the sixth night.

4. The opportunity, or the right, to put an end to a contract when the other party's failure has become a problem, is fundamentally important to the way in which contracts work. Of course, Section 73 of the Act allows a claim to be made for compensation when the other party has broken the contract, but that may not be good enough. Sometimes the failure of the other party to do what he has promised to do should allow the innocent party to say: right; that's it: the contract is at an end. The two big questions for us are: when does the Contract Act allow this to be done; and to what extent, if at all, can the parties to the contract alter the way in which the law of termination of contracts is to work. Unfortunately, there is a degree of doubt associated with each of these.

5. First of all: what does Section 39 actually mean ?

6. There appear to be two ways to read this provision, and it turns on the correct interpretation of the expression 'has refused to perform, or disabled himself from performing, his promise in its entirety'. On the one hand, it could describe a person who is refusing to perform every single element of his promise: that is to say, a person who is going to make zero performance. But on the other, it could also describe a person who will deliver most, but not all, of the promised performance: a person who will deliver perhaps 95 %, but not 100%, of what he has promised to do.

7. There is obviously a very big difference between these two ways of reading Section 39. How do we decide which one is correct ?

8. As a matter of English language it is impossible to say which one is correct: they are each perfectly sensible ways to interpret the language used by the draftsman. As a matter of Burmese language, there is, as I understand, no official translation of the Contract Act; and even if there were, I would not be able to tell you which of these two interpretations was the one which had been chosen or preferred.

9. The picture comes clearer when we look at the Illustrations to Section 39 and use them. The first Illustration tells us this. The singer is engaged to sing sixteen or eighteen times (twice each week for two months). If she sings five times, but then misses one performance, the theatre manager can terminate the contract. We are not told that the singer has said that she will refuse to come back at all, which would mean that she will be stopping after having performed only a third of what she had promised to do. If she had done that, the problem for the manager is a big one: for the next five weeks he will have no singer, so that it would be right for him to be able to terminate the contract immediately. It seems, though, that he can simply terminate it after she has missed one performance. One out of sixteen or eighteen. Or about five percent of what she was supposed to do.

10. And if we look at the second Illustration, we are told that the singer has missed one performance. We are told that the reason why the theatre manager cannot put an end to the contract is because when the singer, who had missed one night only, returns to the theatre, he allows her to resume her performance. It is implicit in this that if he had decided not to allow her to sing when she appeared on the seventh night, he could have put an end to the contract. In other words, he could put an end to the contract after she had missed one performance out of sixteen or eighteen. Or about five percent of what she was supposed to do.

11. What do we get from these two Illustrations ?

12. Do these cases tell us that the innocent party can put an end to the contract if, but only if, the other party makes absolutely no performance, or says that he or she will make zero performance ? The answer is no, it does not mean that, because in the two Illustrations the party who broke her contract had performed some of it.

13. Do these cases tell is that the innocent party can put an end to the contact when, and as soon as, there is any kind of breach, even if it is only a trivial or minor one ? On the basis that as soon as there is any kind of imperfection in performance the other party will not be performing the entirety of her obligation ? It could be saying that, but I doubt it. If that had been what the draftsman had intended, he could have given the example of the singer arriving five minutes late, but he did not do that.

14. Instead, what these two cases seem to be saying is that if there has been a failure to perform which is serious, and if it appears that the failure will only get worse in a way which could not be properly compensated in damages, the innocent party may terminate the contract. In other words, if the refusal to perform affects a vital part of the contract, an essential part of the contract, the innocent party can put an end to the contract. When the singer goes missing at the end of the third week, who knows whether she will come back next week ? How long should the manager have to wait before he can put an end to the contract ? Because each time he opens the theatre to an audience, but the singer does not appear, he loses money (he may have to refund the price of the tickets) and loses reputation (who will buy a ticket for a theatre in which the star performer may not appear) ? If this happens, there is no way to quantify the financial loss. Even if there were, the rules governing compensation for breach are (as we know) not generous to the innocent party; and the idea that the innocent party just has to wait and see what the extent of the failure of the singer to perform actually is is a bad idea. To use language which some may prefer, the breach strikes at the heart of the contract; and that is why Section 39 allows the contract to be put to an end.

15. I should perhaps say here that the singer example may have been more serious in 1872 than it is today. In 1872, if the singer did not appear at the theatre in Rangoon (were there theatres in Rangoon in 1872, I wonder?), there may be no way of finding out what had happened to the singer. Communication will have been very primitive, and an unannounced absence may be impossible to deal with. Today, by contrast, a quick telephone call or text message may be all it takes to clarify things; and today the absence of the singer might not be quite such a problem. But in 1872 it will have been very serious, striking at the heart of the contract and putting the manager in a very difficult position.

16. Let me take another example, which will perhaps show us the path. Suppose I make a contract with a driver who will collect me from my hotel at 7.30 to drive me to the airport to catch my flight to Singapore. At 7.30 he does not appear: does Section 39 allow me to put an end to the contract ? At 7.35 he has still not come: does Section 39 allow me to put an end to the contract ? At 7.45 ? I don't know what you would think (and you may not all think exactly the same thing), but at what point can I say that the driver has refused to perform the contract in its entirety ?

17. We actually have a kind of answer to this question about the 'time stipulation' in a contract.

55. Effect of failure to perform at fixed time in contract in which time is essential. When a party to a contract promises to do a certain thing at or before a specified time, or certain things at or before specified times, and fails to do any such thing at or before the specified time, the contract, or so much of it as has not been performed, becomes voidable at the option of the promisee, if the intention of the parties was that time should be of the essence of the contract.

Effect of such failure when time is not essential. If it was not the intention of the parties that time should be of the essence of the contract, the contract does not become voidable by the failure to do such thing at or before the specified time; but the promisee is entitled to compensation from the promisor for any loss occasioned to him by such failure.

Effect of acceptance and or performance at other time than that agreed upon. If, in case of a contract voidable on account of the promisor's failure to perform his promise at the time agreed, the promisee accepts performance of such promise at any time other than that agreed, the promisee cannot claim compensation for any loss occasioned by the non-performance of the promise at the time agreed, unless, at the time of such acceptance he gives notice to the promisor of his intention to do so.

18. The expression 'time is of the essence' is the way lawyers describe when doing something strictly on time is of fundamental importance, essential, of the essence of the contract. What Section 55 tells us is that if the driver is late, the contract is voidable if time is of the essence of the contract. What this means is that if performance on time is something which was fundamentally important, and that the intention of the parties was that being late, even a little late, would justify the innocent party in ending, terminating, rescinding, the contract.

19. To my mind, in the case of the driver coming to bring me to the airport, time is crucial, essential. Because it was not, and the law required me to wait until the contract had been well and truly broken, it may be too late for me to arrange an alternative (the traffic will have got worse, and the time for the journey will have got less); and if I miss my flight, the idea that I can sue the driver, and obtain full compensation for all the losses which flow from the breach (if anyone really wants to see why, see Illustration (r) to Section 73).

20. This kind of example tells us three really important things.

21. First, there are some breaches of contract which allow an innocent party to put an end to the contract, and there are others which do not. Always remember that, as a matter of Myanmar law (and as in the common law world generally) it is not the breach of contract which puts an end to the contract. It is the promisee who may choose – and who may not choose – to put an end to the contract. The party who breaks his contract is not usually the party who puts an end to the contract. Section 39 is very clear about that.

22. The second point is going to take more time to explain, but here it comes. The test used by Section 55, and, as I would say, usable for other terms as well, is whether the term which

has been broken is ‘essential’ to the contract. What this really means is that the term is so important, its performance is so important, that any breach of that term is understood by the parties as a sufficient justification for the immediate ending of the contract. In common law systems outside Myanmar we have the same idea but we do not have a statute, and we now call such terms ‘conditions’. But this language is not helpful, because it is not used in the Contract Act. I mention it only to make the point that all common law systems ask the same question, and they answer it the same way: is the term which has been broken one whose performance was so important that any breach of it would allow the innocent party to end, terminate, rescind, avoid the contract. Some are; some aren’t.

23. Where the singer is concerned, if on night she does not appear, what is the manager to do ? Hope that she will come tomorrow or next week ? Or rescind the contract immediately and start to look for a replacement performer ? I think it is the second: the manager does not have to wait and see how many audiences are going to be disappointed and demand their money back. But suppose a different case. Suppose you are a professional musician who gives lessons to talented young musicians. Suppose that you make a contract with the parents of an aspiring young violinist, according to which you will give her twenty lessons, every Tuesday at 5pm, for twenty weeks. Suppose that on the third Tuesday you are delayed by the traffic and do not arrive until 5.15: can the parents terminate the contract ? Surely the answer is not; time is not of the essence of the contract; being strictly on time is not crucial for the performance of the contract; and if being late causes any problems, damages can put it right.

24. Now suppose that instead of being late, on one Tuesday you do not appear at all. Can the parents now terminate the contract ? It is more difficult to say for sure, but in my opinion the answer is no. It is certainly a breach when the teacher does not come to give the lesson, and it is infuriating if this was done with no excuse. Although damages should be paid for the loss – the refund of the fee for one lesson, if the fees have been paid in advance – it does not seem to me that the breach has struck at the heart of the contract and robbed it of its purpose.

25. It is not like the case of the singer. The reason why is that if there is a week’s gap in the schedule of violin lessons, the contract still works. We all wait for a week, and it will not do any harm. But in the case of the singer, the theatre manager has an audience to worry about; and later this week he will have another audience to worry about; and he cannot afford to wait and see what happens. That is why the theatre manager can terminate the contract after one failure by the singer; and it is also why the parents of the gifted child cannot terminate the contract to give violin lessons after one lesson is missed by the teacher.

26. (I should say at this point that I had originally intended to use the example of a contract of employment, such as your contract of employment with the firms or companies for whom you work. But I decided not to, because the law which applies to employment contracts tends to be a little different from the law which applies to contracts generally. I should also say that things may look a little different today from the way they did in 1872. For example, if the singer is ill, she can telephone and explain what has gone wrong; if my driver is a little late he can send a text message. But in 1872, if the singer did not appear, or the driver did not come,

what am I supposed to do ? Wait until things get worse and then try to figure it out ? That is why the Illustrations given in the Act may look a little strange today.)

27. We now come to our third point. It may be important to the contracting parties to know whether it is or is not permitted to terminate the contract if this should happen or if that happen. Suppose we have a contact for the sale of goods or for the provision of services. Suppose we have a contract to construct a building or to undertake essential repairs to the roof of a house. What is the customer allowed to do if, one day, the builder arrives late, or does not come at all ? Can he terminate the contract and get someone else in to do the work, or must he just keep a record of the loss which this causes and claim compensation ? The best answer I can give – the best answer than anyone can give – is that it all depends. And that is a really unsatisfactory answer. What should we do about it ?

28. The answer is obvious, really. If the contract had said that 'if X happens, the customer may not terminate the contract, but if Y happens then the customer may put an end to the contract' everyone will know where they stand. If the contract says that 'if on a particular day the builder does come to the building site, the customer may not put an end to the contract; but on the third occasion on which the builder does not come to the site the customer may terminate the contract for breach', everyone will be able to answer this important question. A contract which says what you want it to say will provide the answers to the question. The law favours those who draft their contracts properly.

29. Now suppose you ask me this: where in the Contract Act does it say that the parties can put in their contract a term which says that the contract may be terminated, put to an end, rescinded, if this happens (when this would not otherwise be the case) or that the contract may not be terminated, &c, if that happens (when it would otherwise be lawful to put an end to the contract) ? My answer is in fact another question: where in the Contract Act does it say that you cannot do it ? If the parties agree to say in their contract that a particular term is essential, or that any failure to perform any one or more of these terms is a basis for one of the parties to terminate the contract, I can see no reason why their expression of intention would not be decisive. Section 55 provides the model; the principle of autonomy – that the parties may make contracts on the terms they wish within the limits of the law – provides the justification.

30. The conclusion which follows from this is that if the parties wish to know in advance which are the failures of performance by one party will entitle the other to terminate the contract, they should say so. If they do not, then when something happens, and one party wishes to know whether he may terminate the contract, or must persist and simply claim compensation for loss, it will be necessary to go back to Section 39 and try to predict what a court would say. That does not seem to be a very good plan.

31. Now I said just now that the parties, who wish to make their positions clear, may state in their contract that breach of a particular term does, or will not, entitle the other to terminate the contract. What I had in mind was the sensible arrangement by which the breach of a term which might or might not justify termination was made clear.

32. What I want to ask now is a little different: whether is it possible to draft something more one-sided or extreme. For example, what about this:

> 'The buyer may terminate the contract whenever the seller has failed to perform an obligation of the contract.'

33. This term says that as soon as there is a breach, no matter how small, the other party can terminate the contract. Is this acceptable a term of a contract of sale, or does it cross an invisible line ? We should approach the question as one of principle.

34. If the parties genuinely agree – that is, with no coercion or undue influence, for example – that the contract may be terminated as soon as there is any breach by one of the parties, it is hard to see why the law would want to stop them. It may be a rather strange contract to make, but if the parties agree to it, well, why would the law stop them ? There appears to be nothing illegal or contrary to public policy if the contract is made in such a way. It might be unwise, but I cannot see that it would be illegal. And if it is not illegal, it should not be ineffective.

35. And consider this. A contract between the parties may be of indefinite duration. For example, a contract for the sale of goods, between buyer and seller, may be of indefinite duration. A contract of distributorship may also be agreed and made to go on without a time limit. It may contain a term which says this:

> 'Either party may at any time terminate the contract'

or

> 'Either party may on one month's notice terminate the contract'

36. If this is what the contract says – and it would be a perfectly sensible term to include in a contract when the parties were not able to decide at the outset how long the contractual relationship should go on – it will be given legal effect. It means that either side can put an end to the contract whenever he or it wishes, for any reason or for no reason at all. And if that is so, it follows that a term which allows a party to a contract to terminate it at any time after there has been a breach by the other must also be given legal effect. Looked at from this point of view, it is a more limited version of a contract term which with which we saw no problem. It follows from that that a contract term which allows the contract to be terminated as soon as there is a breach – any breach – of the contract will be accepted by the courts if it has been agreed to by the parties.

37. Let us go to the other extreme. What about a contract which says something like this:

> ‘Without prejudice to his right to claim compensation for loss caused by the seller’s breach of contract, the buyer shall not be entitled in any circumstances to terminate the contract.’

or

> ‘Without prejudice to his right to claim compensation for loss caused by the distributor’s breach of contract, the manufacturer shall not be entitled in any circumstances to terminate the contract.’

38. This term says that even though there may have been breaches, of real importance and great effect, the innocent party cannot terminate the contract but must content himself with a claim for compensation. Will a clause like that be effective ?

39. You might think that the answer here is the same as before: that if the parties want it, they can agree to it and the court will be prepared to enforce it. But this time that may not be quite right. Certainly the parties can agree to it, and if they want it, they can include it in their contract. But when would a court ever get involved ? The answer presumably is that the court will be involved if the party who is said to have had no right to terminate the contract does terminate it, or acts as though he had terminated it. Suppose that the buyer pretends to terminate the contract and refuses to take delivery of the goods, or that the manufacturer refuses to supply good to the distributor for distribution. And suppose that in each case this means that the buyer and the manufacturer have broken their contractual promise. What will happen is that the innocent party will take the other to court: what can the court do ? It can order compensation for loss caused by the unjustified termination, but it cannot un-terminate the contract. It could, possibly, order specific performance, ordering the parties to do what they had promised to do. But the terms of the Specific Relief Act 1877 mean that that will rarely happen; and by the time the parties get to court it will be far too late to even think of specific performance as a solution. This contract term, therefore, may be one which has no effect at all.

40. It is just the same as if the contract contains a term which says that

> ‘The parties agree not to break this contract.’

41. If one of them does break the contract, what difference does it make that they had promised not to break the contract ? Surely the answer is: none at all. The conclusion to which this points is that a contract term which provides that even if there is a breach the contract cannot be terminated by the innocent party will be broken if the contract is terminated; and if that happens the court will simply have to order compensation. In short, the term will not change anything.

42. Still, the conclusion is that the position of the parties will be far clearer, and less costly to deal with, if the contract spells out, in as much detail as possible, the circumstances in which one party may, and may not, terminate the contract on account of a failure in performance.

(B) Writing or rewriting the terms relating to compensation for non-performance or breach

43. In this Section we shall be looking at the rules, and then at clauses in contracts, which deal with sums payable (or not payable) when a contract has not been performed and one party is shown to have broken the contract. These clauses can take many forms, for example: agreed compensation clauses, penalty clauses, limitation clauses, payment-of-profit clauses. We can look at only a few of these, but they will illustrate a general point of some importance.

44. Let us start with the statute. On this occasion it is necessary to include the Illustrations which explain what the provisions, especially Section 73, are intended to mean.

> **73. Compensation for loss or damage caused by breach of contract.** When a contract has been broken, the party who suffers by such breach is entitled to receive, from the party who has broken the contract, compensation for any loss or damage caused to him thereby, which naturally arose in the usual course of things from such breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.
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> Such compensation is not to be given for any remote and indirect loss or damage sustained by reason of the breach.
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> **Compensation for failure to discharge obligation resembling those created by contract.** When an obligation resembling those created by contract has been incurred and has not been discharged, any person injured by the failure to discharge it is entitled to receive the same compensation from the party in default as if such person had contracted to discharge it and had broken his contract.
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> *Explanation*.- In estimating the loss or damage arising from a breach of contract, the means which existed of remedying the inconvenience caused by the non-performance of the contract must be taken into account.
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> *Illustrations*
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> (a) A contracts to sell and deliver 50 maunds of saltpetre to B, at a certain price to be paid on delivery. A breaks his promise. B is entitled to receive from A, by way of compensation, the sum, if any, by which the contract price falls short of the price for which B might have obtained 50 maunds of saltpetre of like quality at the time when the saltpetre ought to have been delivered.
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> (b) A hires B's ship to go to Bombay, and there take on board, on the first of January a cargo which A is to provide and to bring it to Rangoon, the freight to be paid when earned. B's ship does not go to Bombay, but A has opportunities of procuring suitable conveyance for the cargo upon terms as advantageous as those on which he had chartered the ship. A avails himself of those opportunities, but is put to trouble and expense in doing so. A is entitled to receive compensation from B in respect of such trouble and expense.
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> (c) A contracts to buy of B, at a stated price, 50 maunds of rice, no time being fixed for delivery. A afterwards informs B that he will not accept the rice if tendered to him. B is entitled

to receive from A, by way of compensation, the amount, if any, which the contract price exceeds that which B can obtain for the rice at the time when A informs B that he will not accept it.

(d) A contracts to buy B's ship for 60,000 rupees, but breaks his promise. A must pay to B, by way of compensation, the excess, if any, of the contract price over the price which B can obtain for the ship at the time of the breach of promise.

(e) A, the owner of a boat, contracts with B to take a cargo of paddy to Rangoon, for sale at that place, starting on a specified day. The boat, owing to some avoidable cause, does not start at the time appointed, whereby the arrival of the cargo at Rangoon is delayed beyond the time when it would have arrived if the boat had sailed according to the contract. After that date, and before the arrival of the cargo, the price of paddy falls. The measure of the compensation payable to B by A is the difference between the price which B could have obtained for the cargo at Rangoon at the time when it would have arrived if forwarded in due course, and its market price at the time when it actually arrived.

(f) A contracts to repair B's house in a certain manner, and receives payment in advance. A repairs the house, but not according to contract. B is entitled to recover from A the cost of making the repairs conform to the contract.

(g) A contracts to let his ship to B for a year, from the first of January, for a certain price. Freights rise, and on the first of January the hire obtainable for the ship is higher than the contract price. A breaks his promise. He must pay to B, by way of compensation, a sum equal to the difference between the contract price and the price for which B could hire a similar ship for a year on and from the first of January.

(h) A contracts to supply B with a certain quantity of iron at a fixed price, being a higher price than that for which A could procure and deliver the iron. B wrongfully refuses to receive the iron. B must pay to A, by way of compensation, the difference between the contract price of the iron and the sum for which A could have obtained and delivered it.

(i) A delivers to B, a common carrier, a machine, to be conveyed without delay to A's mill, informing B that A's mill is stopped for want of the machine. B unreasonably delays the delivery of the machine, and A in consequence loses a profitable contract with the Government. A is entitled to receive from B by way of compensation the average amount of profit which would have been made by the working of the mill during the time that delivery of it was delayed, but not the loss sustained through the loss of the Government contract.

(j) A, having contracted with B to supply B with 1,000 tons of iron at 100 rupees a ton, to be delivered at a stated time, contracts with C for the purchase of 1,000 tons of iron at 80 rupees a ton, telling C that he does so for the purpose of performing his contract with B. C fails to perform his contract with A, who cannot procure other iron, and B, in consequence, rescinds the contract. C must pay to A 20,000 rupees, being the profit which A would have made by the performance of his contract with B.

(k) A contracts with B to make and deliver to B, by a fixed day, for a specified price, a certain piece of machinery. A does not deliver the piece of machinery at the time specified, and in consequence of this B is obliged to procure another at a higher price than that which he was to have paid to A, and is prevented from performing a contract which B had made with a third person at the time of his contract with A (but which had not been then communicated to A), and is compelled to make compensation for breach of that contract. A must pay to B, by way of compensation, the difference between the contract price of the piece of machinery and the sum paid by B for another, but not the sum paid by B to the third person by way of compensation.

(l) A, a builder, contracts to erect and finish a house by the first of January, in order that B may give possession of it at that time to C, to whom B has contracted to let it. A is informed of

the contract between B and C. A builds the house so badly that, before the first of January, it falls down and has to be rebuilt by B, who in consequence loses the rent which he was to have received from C, and is obliged to make compensation to C for the breach of his contract. A must make compensation to B for the cost of rebuilding the house, for the rent lost, and for the compensation made to C.

(m) A sells certain merchandise to B, warranting it to be of a particular quality, and B, in reliance upon this warranty, sells it to C with a similar warranty. The goods prove to be not according to the warranty, and B becomes liable to pay C a sum of money by way of compensation. B is entitled to be reimbursed this sum by A.

(n) A contracts to pay a sum of money to B on a day specified. A does not pay the money on that day. B in consequence of not receiving the money on that day is unable to pay his debts, and is totally ruined. A is not liable to make good to B anything except the principal sum he contracted to pay, together with interest up to the day of payment.

(o) A contracts to deliver 50 maunds of saltpetre to B on the first of January, at a certain price. B afterwards, before the first of January, contracts to sell the saltpetre to C at a price higher than the market price of the first of January. A breaks his promise. In estimating the compensation payable by A to B, the market price of the first of January, and not the profit which would have arisen to B from the sale to C, is to be taken into account.

(p) A contracts to sell and deliver 500 bales of cotton to B on a fixed day. A knows nothing of B's mode of conducting his business. A breaks his promise, and B, having no cotton, is obliged to close his mill. A is not responsible to B for the loss caused to B by the closing of the mill.

(q) A contracts to sell and deliver to B, on the first of January, certain cloth which B intends to manufacture into caps of a particular kind, for which there is no demand except at that season. The cloth is not delivered till after the appointed time, and too late to be used that year in making caps. B is entitled to receive from A, by way of compensation, the difference between the contract price of the cloth and its market price at the time of delivery, but not the profits which he expected to obtain by making caps, nor the expenses which he has been put to in making preparation for the manufacture.

(r) A, a ship-owner, contracts with B to convey him from Rangoon to Sydney in A's ship, sailing on the first of January, and B pays to A, by way of deposit, one-half of his passage money. The ship does not sail on the first of January, and B, after being in consequence detained in Rangoon for some time and thereby put to some expense, proceeds to Sydney in another vessel, and in consequence, arriving too late in Sydney, loses a sum of money. A is liable to repay to B his deposit, with interest, and the expense to which he is put by his detention in Rangoon, and the excess, if any, of the passage-money paid for the second ship over that agreed upon for the first, but not the sum of money which B lost by arriving in Sydney too late.

74. Compensation for breach of contract where penalty stipulated for. When a contract has been broken, if a sum is named in the contract as the amount to be paid in case of such breach, or if the contract contains any other stipulation by way of penalty, the party complaining of the breach is entitled, whether or not actual damage or loss is proved to have been caused thereby, to receive from the party who has broken the contract reasonable compensation not exceeding the amount so named or, as the case may be, the penalty stipulated for.

Explanation.- A stipulation for increased interest from the date of default may be a stipulation by way of penalty…

Illustrations

(a) A contracts with B to pay B Rs. 1,000 if he fails to pay B Rs. 500 on a given day. A fails to pay B Rs. 500 on that day. B is entitled to recover from A such compensation, not exceeding Rs. 1,000, as the Court considers reasonable.

(b) A contracts with B that if A practises as a surgeon within Rangoon he will pay B Rs. 5,000. A practises as a surgeon in Rangoon. B is entitled to such compensation, not exceeding Rs. 5,000, as the Court considers reasonable.

(c) A gives a recognizance binding him in a penalty of Rs. 500 to appear in Court on a certain day. He forfeits his recognizance. He is liable to pay the whole penalty.

(d) A gives B a bond for the repayment of Rs. 1,000 with interest at 12 per cent. At the end of six months, with a stipulation that in case of default interest shall be payable at the rate of 75 per cent from the date of default. This is a stipulation by way of penalty, and B is only entitled to recover from A such compensation as the Court considers reasonable.

(e) A, who owes money to B, a money-lender, undertakes to repay him by delivering to him 10 maunds of grain on a certain date, and stipulates that, in the event of his not delivering the stipulated amount by the stipulated date, he shall be liable to deliver 20 maunds. This is a stipulation by way of penalty, and B is only entitled to reasonable compensation in case of breach.

(f) A undertakes to repay B a loan of Rs. 1,000 by five equal monthly instalments with a stipulation that, in default of payment of any instalment, the whole shall become due. This stipulation is not by way of penalty, and the contract may be enforced according to its terms.

(g) A borrows Rs. 100 from B and gives him a bond for Rs. 200 payable by five yearly instalments of Rs. 40, with a stipulation that, in default of payment of any instalment, the whole shall become due. This is a stipulation by way of penalty.

75. Party rightfully rescinding contract entitled to compensation. A person who rightly rescinds a contract is entitled to compensation for any damage which he has sustained through the non fulfilment of the contract.

Illustration

A, a singer, contracts with B, the manager of a theatre, to sing at his theatre for two nights in every week during the next two months, and B engages to pay her 100 rupees for each night's performance. On the sixth night A wilfully absents herself from the theatre, and B, in consequence, rescinds the contract. B is entitled to claim compensation for the damage which he has sustained through the non-fulfilment of the contract.

45. Let me just say two things about Section 75 before we go any further. First, it clearly reinforces the idea, which we mentioned in paragraphs 12 and 13, that the reliable performance of the artist was essential to the contract, which is why the manager of the theatre can end, terminate, or rescind the contract as soon as she misses a performance. Second, the right to claim compensation is given, but has to be created, by Section 75. This is because, if the contract, when ended, is treated as though it had ceased to exist, there has to be some other justification for a court to award damages; and Section 75 is it.

46. Now we go back to Section 73. It shows how the Act decides what will and will not be recoverable when the contract is broken. It is pretty clear that it is not enough, or not always

enough, to say that the sums claimed represents something which, according to the plaintiff, the defendant knew, or suspected, would result if the contract was broken. I say it is clear: from the statutory exclusion of loss which is 'remote and indirect', even if that remote and indirect loss was something which the defendant realised was likely to result from the breach: everything turns on what the Act means by 'remote and indirect'. I say it also in the light of Illustrations (n), (o) and (q) in particular. These Illustrations allow us to draw some tentative conclusions.

47. If, and to the extent that, the plaintiff has had to make payments, paying out of his own pocket sums which he would not have had to pay if the contract had not been broken, he will have a good chance of recovering compensation in respect of them. If a supplier, of goods or services, fails to do what he contracted do to, the plaintiff can recover any difference in value between what he received and should have received. He can recover what he has to pay to go into the market to obtain a substitute or a replacement. The plaintiff may also be able to recover sums which he has had to pay to a third party, out of his own pocket, if the other party knew that the plaintiff would have to do this if he let the plaintiff down.

48. It is quite different if the plaintiff's complaint is not that he has had to hand over his own money, but that he has been prevented from receiving sums which would otherwise have come his way. The plaintiff may be able to recover sums in respect of the further profits he would have made, but was prevented from making, if it can be seen that the other party assumed responsibility for these (Illustration (j)). But the plaintiff will not be able to recover sums in respect of further profits he would have made, but was prevented from making, if the most that can be said that the other party probably knew this but had not been told about it and had not agreed to deal on the basis that he would be liable for the sums lost. The fact that non-delivery of the goods meant that the buyer could not sell them on, and so lost the profit which he would have gained from selling them on, will not be enough to make these sums recoverable from the party who broke his contract. The fact that the seller knew that the goods were going to be sold on at a profit (the buyer in Illustration (o) was obviously not buying 50 maunds of saltpetre for private consumption: it is nearly two tons of the stuff, so it is obvious that he was going to trade it, yet he cannot recover compensation for the profits he did not receive; the buyer in Illustration (q) was obviously going to use the material to make caps and sell them on) is not enough to make the lost profits recoverable.

49. Now this may be deliberate. Well, as it is in legislation it obviously is deliberate. The purpose of the law may be reasonably generous to a plaintiff who is seeking to recover losses, in the sense of replenishing sums which were paid out; but to be rather more restrictive to a plaintiff who wants the defendant to go further and reimburse him for gains which were anticipated but which were not realised. Why would the law want to do this ?

50. One answer would be that when the Act was drafted, English law contained the same restrictions. But as time goes by, courts will often try to loosen laws which made perfect sense at the time but which now appear to be rather too limiting. And after all, if you ask the simple

question whether the person who broke his contract caused the profits to be lost, only one answer is possible: he did. So, one may ask, why should he not pay damages to put it right ?

51. If the answer is that he did not know about the profits which the plaintiff was planning to make, and if this is true, then of course he should not pay. Section 73 is right to say this is the general rule, and it does not just apply to lost profits, but to all unknown losses. But if the defendant did know, either because he was told or because he did not need to be told, as he already knew the business of the plaintiff, then there is a good reason for saying that he should pay if his wrongful act has prevented the inflow of money to the plaintiff. If the law nevertheless says that he need not pay, it is presumably because it wishes to protect the defendant from being exposed to risks of having to pay a lot of money. After all, if your business is in selling, or supplying, or repairing, would you really want to make contracts which, if they go a little wrong, could ruin you ? Perhaps this is the real point: Myanmar law aims to put some limit on the risk, on the size of the risk, which a person who makes a contact is exposed to. And if that is correct, it may be that Section 73 reflects an important principle of Myanmar contract law.

52. And if that is correct, one should ask whether the parties may put in their contract a term which alters the answer, or redefines the financial consequences of a breach of contract. For example:

> 'If either party should break the contract the party in breach shall, notwithstanding anything said in Section 73 of the Contract Act, pay to the other party such sum as represents the whole of the financial loss, whether direct or indirect, resulting from the breach of contract.'

53. Would this courts give effect to such a provision ? We do not know the answer. When the Act was drafted, it is quite likely that questions like this had never crossed anybody's mind; the Act does not, therefore, give us a clear and reliable answer. There will be cases in which the parties to a contract are commercial and are able to look after themselves as they wish; such parties do not necessarily need the protection of Section 73 when the contract is broken: if they wish to stipulate for greater liability they should probably be allowed to: unless public policy is involved, what interest does the law have to intervene in the contract the parties chose to make ?

54. In other cases, in which the parties are not so powerful and strong, it is much easier to see Section 73 as having a sensible protective function, helping to ensure that a party who breaks his contract is not necessarily brought to ruin by something which may not really be his fault. All of that makes it difficult to see what the right answer ought to be. It cannot really be 'sometimes it is effective; other times it is not'. It has to be yes in every case, or not ever, in any case.

55. The question is the one which we have been asking for some time: can the parties contract out of – agree upon something which contradicts – the provisions of the Contract Act,

and in particular Section 73 ? Can the parties to a contract, by clear, deliberate, and express words, agree that there will be an assessment of compensation for breach of contract which is not a fixed sum (to which Section 74 would apply) but which is much more generous to the plaintiff, and much more painful for the defendant, than Section 73 would otherwise have provided for ?

56. One possible answer might be to say that such a contract term is a penalty, which is enforceable, but that the sum actually recoverable on breach may be scaled down, as is allowed for by Section 74. However, the sum to be paid is not a fixed or liquidated sum; and even if that is not a problem, is a promise to pay the sums which represent the losses resulting from the breach really a penalty ? A calculation of actual loss, which is not then increased or multiplied, or whatever, does not look all that much like a penalty, though if a judge was to want a reason to deprive it of effect, this might do the job. We will come back to Section 74 in a moment.

57. If this suggested term is not regarded as a penalty, the question is whether Section 73 imposes a rule about compensation which the parties cannot vary, even if they wish to, and whether upwards or downwards; or whether Section 73 is a default rule which will apply if the parties do not make a different agreement, but which will not apply if the parties chooses to assess compensation by a different calculation. One might ask: why ever not ? If it is the agreement the parties wanted, and if consent was free, why should the law override it ? One might also say that Section 73 is worded as it is so that the cost of making a contract which might be broken is not so ruinously high that it puts people off contracting in the first place. The honest answer is that we just do not know. However, it seems unlikely that parties can contract out of Section 74 by saying, for example, that the scaling down part of Section 74 shall not be applied to their contract; and that may mean that contracting out of Section 73 is not allowed, either.

58. Let us now move to Section 74 and the law of fixed sums and penalties. What about this, for example ?

> ‘The agreed hiring fee for the items is calculated as follows. For the first 7 days, the fee is $10 per day. For the next 7 days the fee is $50 per day. For every day after the 14th day the fee is $100 per day; and the total sum payable for the hire is to be paid on the date on which the items are returned.’

59. Or this ?

> ‘All items must be returned to us within 14 days from the date of posting/delivery/ collection. A fee of $100 per day will be charged for each item which is retained by you longer than the said period of 14 days except where we agree a longer period in writing with you.’

60. Or this ?

> ‘During the period of this contract A promises B Co that he will perform his services exclusively for B Co; if in spite of this A performs services for anyone other than B Co he will pay to B Co all sums received or receivable by him for such performance.’

61. There are several reasons to think about the use of such terms. The most obvious one would be that the provisions of the Contract Act concerning compensation for loss or damage caused by a breach of contract are rather restrictive in the relief which they allow a plaintiff to claim. It extends only to loss directly incurred, and it is clear from the Illustrations given, and from what we have just said, that only some of the adverse consequences of a breach of contract count as a loss. There may therefore be some advantage in drafting a contract term which tries to secure for the plaintiff more than would be recovered if Section 73 of the Act were to be applied. We should ask whether they are likely to be effective.

62. The first question to ask is whether these are to be seen as terms which come into effect when there is a breach of contract. If they are, their effect will depend on Sections 73 and 74 of the Act; but if they are not terms which operate when there has been a breach, they will be unaffected by these provisions. On the face of it, a fee which is agreed to be paid for hiring another person’s property is a fee for hiring, and is not compensation for loss resulting from a breach of contract. However, if one takes the view that a massive increase which comes into effect after a stipulated date has passed is really a punishment for failure to return the property on a particular day, then it may be seen as a penalty for breach which has been disguised as something else; and if that is really the way to look at it, the disguise should be removed and Section 74 applied to it.

63. In the case of the hire fee, it seems pretty clear that if increase in payment is seen as something which happens when there has been a default, it will count as a penalty, because it so closely resembles the increase in interest which must be paid, set out in the Explanation to Section 74, that it should be treated in the same way. In other words, it can be included in the contract, but it will not be fully enforceable: all that will be recovered is reasonable compensation. If, on the other hand, this is seen as the price – the variable – price which is payable for the hire, which is a large sum but which is reduced or kept small if the property is returned by a particular date, there is no problem with enforcing it, and Section 74 will not apply to it.

64. This distinction follows, first, from the decision of the Supreme Court in *AKRMMK Chidambaram Chettyar v Khoo Hwa Lam* (1950) BLR 98 (SC), in which the Chief Justice adopted a distinction which has been drawn in an earlier (Indian) case. For convenience, the judgment to which the he referred, and which he approved, had put the point this way:

> The law on the subject is not, I think, open to any serious question. If there is an agreement to pay a sum of money by a particular date with a condition that if the money is not paid on that date a larger sum shall be paid, that condition is in the nature of a penalty against which a Court of equity can grant relief and award to the party seeking

> payment only such damage as he has suffered by the non-performance of the contract. But if, on the other hand, there is an agreement to pay a particular sum followed by a condition allowing to the debtor a concession, for example, the payment of a lesser sum, or payment by instalments, by a particular date or dates, then the party seeking to take advantage of that concession must carry out strictly the conditions on which it was granted, and there is no power in the Court to relieve him from the obligation of so doing (58 Bom. 610, 618).

65. The core question is therefore whether these are provisions which set out the price which the customer has agreed to pay, that price being a variable price, or are provisions which set out to penalise, to punish, for breach of a promise to return the goods by a date which has been agreed. If it is the former, the Contract Act gives no power to the court to reduce the sums which have been agreed to be paid; if it is the latter, then Section 74 would allow the court to reduce this figure. The courts have no general power to alter the terms of contracts just because they consider the price which was agreed to be far too high, or to be unconscionable. In the one reported case in which a judge at first instance did think he had this power, *Nabin Chandra Deb v Mi Robeya* AIR 1928 Ran 7, the appellate court described the judgment from which the appeal was brought, and which it reversed, as being 'sentimental rather than judicial'. That may be rather unkind to the judge, but there it is: the Contract Act is clear enough.

66. What is not so clear is whether these really are payment provisions, or are sums agreed to be paid when there is a breach of contract. The answer must be found by treating the question as one of the true construction of the contract. On issues like this, the parties have considerable freedom to structure their relationship as they wish; on the other hand, they cannot, surely, disguise what is in substance a provision which works in the case of a contractual failure to perform, a breach, as something which it actually is not. The best way to ensure that 'Section 74 of the Contract Act would not apply for the the purpose of scaling down the amount of compensation agreed upon', as the Chief Justice put it, is to frame the duty to pay the sums of money as payments not as sums due as penalties for breach.

67. What about the third of these payment provisions ? The same reasoning must be applied. If it looks as though it is designed to punish or penalize the party against whom it is to be enforced, who is considered to have broken the contract, it will be a penalty, and the sum to be paid as reasonable compensation may be scaled down from what is provided for in the contract itself. If, instead, it is read as though it makes it entirely legitimate for the party concerned to offer his services to someone else, but the price to paid for doing so is that the gains made have to paid over as the cost of this freedom, then Section 74 will not apply to it. Suppose the term had said this:

> 'During the period of this contract in which A promises that he will perform his services for B Co, A may perform services for someone other than B Co on condition that A pays to B Co the sums which he receives from that other person for the services which he provides to that other person.'

68. If that was how it was put, it would be very hard to argue that A had broken his contract with B Co by working for someone else, and if A were to do this, a claim by B Co for the money would be a good claim; it would not be 'scaled down' by reference to Section 74. Once again, it is a question of how the terms of the contract are construed. The more they can be made to look like price or payment provisions, the greater the likelihood that the court will enforce them according to their letter (or their number).

(C) Conclusions

69. What do I invite you to take away from the lecture ? I think there are four important points. First, that the law on when a contract can be terminated, ended, rescinded in response to the other party's non-performance, depends on the term broken being essential to the contract. Not all terms are; but the power of the parties to specify in advance which terms are essential in the sense that this may be the result of not performing them, is considerable, and if that power is exercised, it will save a lot of arguing later.

70. Second, that the rules governing compensation may be the rules of Myanmar law which apply in every case to which Myanmar law applies; or they may be the default rules of Myanmar law which will apply if, but only if, the parties have not spelled out in their contract the rules governing compensation. We do not know, or do not know with sufficient certainty, which view is the correct one.

71. Third, the rules on penalties – and in particular the scaling rule – apply when there is a breach. If the contract can be written so that the sum in question is part of the payment, and not something which arises after and because of the breach, it will be much more likely to be upheld.

72. And fourth, in the current state of Myanmar law, which is pretty good but which is also, in one or two places, more uncertain than one would like, it makes sense for contracts to be detailed and to set out clearly what the parties would like the rules of their relationship to be. If the parties do not so that, it is too late, and simply wrong, to complain that the law does not produce the result they wanted. The law does not make contracts; parties do. The law is not to be blamed if there is something wrong with the contract which it is asked to deal with.