

AVOIDING COSTLY PITFALLS WHEN ENDING A BUSINESS RELATIONSHIP

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IN BRIEF

Business relationships and dealings should be set out in writing. Having a written contract which clearly articulates the circumstances in which the business relationship can end ensures that everyone is aware of their rights and minimises uncertainty between the businesses.

BUSINESS RELATIONSHIPS SHOULD BE RECORDED IN A WRITTEN CONTRACT

At the heart of most business relationships is a contract which governs the parties' rights and obligations, including their right to end their relationship. A business contract can be in writing, oral, by conduct or a combination of the three. Whereas a written contract will ordinarily set out all of the parties' rights and obligations, an oral contract or contract by conduct will rarely contemplate all aspects of the business relationship.

As a result, businesses that enter into an oral contract or contract by conduct are often unsure of the circumstances in which they can bring the contract to an end and the process for doing so. This often leads to a business which is seeking to bring a business relationship to an end being threatened with claims that it has acted unlawfully. To prevent this, business relationships should be recorded in a written contract.

CONTRACTUAL RIGHT TO TERMINATE

A contract governing a business relationship can ordinarily be brought to an end:

- Automatically at the expiry of the term of the contract.
- By one party giving the other party reasonable notice.

Having a written contract which clearly articulates the circumstances in which the business relationship can end ensures that everyone is aware of their rights and minimises uncertainty between the businesses.

- By a party electing to terminate the contract when the other party has breached a fundamental term of the contract.

AUTOMATIC EXPIRY OF A CONTRACT

Some business contracts are for a fixed period and will expire at the end of the period unless the parties agree to continue the business relationship, in which case it will be governed by the terms of the original contract unless a new contract is entered into. In these circumstances, the relationship can be ended by one of the parties giving the other reasonable notice of its decision to terminate the contract.

ENDING CONTRACTS PURSUANT TO THEIR TERMS

In situations where contracts are not for a fixed term, the parties' right to terminate the contract will be governed either by the conditions of the contract or the common law. If the contract contains a procedure for ending the contract, it is essential that the procedure is followed. Failure to comply with the specified termination procedure could expose the party seeking to terminate the contract to claims for damages.

ENDING CONTRACTS WITH REASONABLE NOTICE

If the contract is not for a fixed term and is silent on the circumstances in which a party can end the contract, either party may terminate the contract by giving the other party reasonable notice. Reasonable notice will depend upon the nature of the business relationship.

For example, a motor dealership which has sold a particular brand of vehicle for 15 years could expect the supplier of that brand of vehicle to give the dealership

at least six months' notice of its intention to terminate the contract, whereas a homeowner may only need to give the local newsagency that delivers the weekend newspaper 24 hours' notice of his or her decision to terminate the service.

TERMINATION FOLLOWING A BREACH OF AN ESSENTIAL TERM OF THE CONTRACT

Written contracts often contain clauses which stipulate the circumstances in which the parties can terminate the contract. In most cases, it is when a party has failed to fulfil a condition which goes to the heart of the contract, e.g. the motor dealership refuses to pay the manufacturer for the cars that it has supplied to the dealership.

If the contract is silent on what constitutes a terminable event, the right to terminate the contract will be governed by the common law (law developed through court cases). At common law, the right to terminate a contract will arise where a fundamental condition of the contract has been breached, or the other party has demonstrated that it does not intend to fulfil its obligations.

Again, the innocent party needs to be satisfied that the other party has breached a fundamental condition of the contract or repudiated the contract before it terminates the contract and ends the business relationship. Notice of the breach or repudiation should be given to the other party to terminate the relationship officially.

PUT IT IN WRITING

It is in a business's best interests to ensure that its relationships and dealings are set out in writing. This ensures that everyone is aware of their rights and obligations and minimises uncertainty between the businesses.

Ideally, the contract should clearly articulate the circumstances in which a party can end the business relationship.

Finally, you should always follow any process set out in the contract for ending the relationship. If in doubt, always give the other party reasonable notice of your decision to do so.

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