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LEGAL INSIGHT
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CONTRACT BREACH: ENFORCE YOUR ENTITLEMENTS UNDER THE LAWS AND IMMEDIATE LEGAL ACTION

By: Sakinah Hayati Binti Sukri
Legal Associate

Did you know you can walk away from a contract?

The answer is yes — but only under certain conditions. You can terminate a contract if there is a material breach, meaning a serious violation that goes to the heart of the agreement.

A material breach in contract laws means a serious violation of the terms of the contract that substantially impaired the values of the non-breaching party.

For example, Party A is appointed as a contractor to build a house within a specified timeframe. However, if Party A fails to complete the construction entirely, this constitutes a material breach, as the core obligation of building the house has not been fulfilled, thereby violating the essential terms of the contract.

This differs from a partial or immaterial breach, such as where Party A completes the house but with minor deviations—like using the wrong door color. In such cases, although there is a breach, the contract remains enforceable because the core purpose of the agreement has still been met.

Partners

Atiqah Binti Abdul Razak
Partner
atiqah@legalasa.com

Syafiqah Binti Abdul Razak
Partner
syafiqah@legalasa.com

Areas of Practice

Corporate & Commercial
Real Estate, Property& Finance
Litigation & Dispute Resolution
Probate & Estate Administration
Shariah
Taxation Law
Legal Advisory

Contact Us:

No.559-A,Jalan Samudera Utara 1,
Taman Samudera,
68100 Batu Caves, Selangor

03-6178 6831/014-923 8785

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Material breach is illustrated well in the case of Ban Hong Joo Mines Ltd V Chen & Yap Ltd [1969] 2 MLJ 83 where it was held that:

"In the present case, as was stated by the learned trial judge, the appellants were in breach of their obligation to make fortnightly payments. Their deliberate refusal to pay what was already due by way of fortnightly payments was an important element on the question of their repudiation of the contract. Furthermore, they ordered the respondents to stop work. This stoppage of work by them clearly went to the root of the contract. In the circumstances, the respondents had no option but to treat the contract as at an end and to sue for payment for the work which they had already done. In our judgment they were entitled to recover the amount claimed either on the basis of work done by them at the appellants' request or by way of damages on the basis of quantum meruit."[1]

Simply said, the party who was supposed to make payments (the appellants) stopped paying and even told the workers (the respondents) to stop their work. These actions were serious and broke the main terms of the contract.

Because of that, the workers had the right to treat the contract as cancelled and ask for payment for the work they already completed. The court agreed that they deserved to be paid, either for the work they did or as fair compensation.

[1] [1969] 2 MLJ 83

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Thus, in this situation you are entitled to:

i. **Terminate the contract, and**
ii. **Sue for damages caused by the breach.**

Sue/Claim for Damages

A. What is damages under contract laws?

The law provides for monetary compensation to the aggrieved party in the event of a breach of contract, provided that the loss arises directly from the breach caused by the defaulting party.
Simply said, money that one person has to pay another because they did something wrong—usually by breaking a contract or causing harm.

It's like saying:
"You messed up, and now you owe me for the trouble you caused."
Damages is stipulated under Section 74 of Contracts Act 1950:

"*(1) When a contract has been broken, the party who suffers by the 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 the breach, or which the parties knew, when they made the contract, to be likely to result from the breach of it.***

(2) Such compensation ***is not to be given for any remote and indirect loss or damage sustained by reason of the breach."***

The general rule is stated in the case of **East Asiatic Co Ltd V Othman [1966] 2 MLJ 38** where clearly defined how the court evaluate the loss suffered by the aggrieved party.

[1] [1966] 2 MLJ 38

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*"The general purpose of the law is to give compensation, that is to put the plaintiff in **as good a position as he would have been had the defendant performed the contract and the law speaks of compensation and not damages.** Therefore the plaintiffs must show that they have suffered some loss or damage before compensation can be awarded."*[1]

The main goal of the law is to compensate the injured party — **to put them in the same position they would have been in if the contract had been properly followed**. But to get this compensation, the person suing must prove that they actually suffered a loss or damage.

B. Measure quantum of damages[2]

There are two measure quantum of damages may be claimed by the aggrieved party:

i.General damages: loss of profits
ii.Special damages: loss in preparation of performance of the contract, wasted expenditure – that already incurred by the aggrieved party

- **General damages: loss of profits**

Loss of profits normally occurs when there is a difference between the market price and contract price.

As an example; Party A agreed to sign a contract with Party B to deliver fresh pastries every morning at 6 AM. Party A agreed that to pay Party B weekly, and in return, Party A got exclusive rights to their popular croissants.

However, Party B failed to deliver for a whole one week and it affected the sale of Party A. Party A lost their regular customers. Party A then lost their profits.

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Hence, in this situation, Party A has the right to sue Party B for the loss of profits.

- **Special damages: loss in preparation of performance of the contract, wasted expenditure**

For instance, Party A engaged Party B to construct a coffee shop with a stage-payment arrangement. Party B proceeded with the works and achieved 30% completion, incurring RM100,000.00 in expenditure towards fulfilment of the contract.

Subsequently, Party A unilaterally terminated the contract without just cause. In this circumstance, Party B may initiate a claim for special damages against Party A, specifically seeking compensation for the wasted expenditure of RM100,000.00, as the loss directly resulted from the premature and wrongful termination of the contractual agreement.

C. Presumed Loss vs Special Knowledge of the Damages

In deciding whether the defaulting party indeed caused the losses suffered by the aggrieved party, the court will examine the material facts surrounding the breach of contract.

If the losses arise in the ordinary course of events, the law will presume that the defaulting party had knowledge of such potential consequences.

Alternatively, liability may arise where the defaulting party possessed special knowledge that made the specific losses foreseeable.

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These principles are illustrated under the two limbs of Section 74 of the Contracts Act 1950.

Under **Section 74(1) of the Contracts Act 1950,** the loss you claim must be something that would normally happen when a contract is broken. It is assumed that the party who broke the contract knew such a loss could happen.

The examples under **Section 74(1) of the Contracts Act 1950** show situations where losses can naturally happen if a contract is broken, such as:

i.Market prices for goods or items can go up or down.
ii.When a contract is broken, the affected party may take other actions that lead to more losses.
iii.Selling goods or offering services usually brings in profit — so losing that chance is a real loss.[1]

As decided in the case of ***Koufus v C Czarnikow Ltd (The Heron II) [1969] 1 AC 350[2]The House of Lords held that a ship owner must be presumed to know that prices in the commodity market are subject to fluctuation, and that any delay could naturally and probably result in financial loss arising from such fluctuations.***

- **Section 74(2) of the Contracts Act 1950**

However, the application under Section 74(2) of the Contracts Act 1950 differs, as the aggrieved party must prove that the defaulting party possessed special knowledge and could foresee the specific losses resulting from the breach.

In the case of ***Tham Cheow Toh v Associated Metal Smelters Ltd [1972] 1 MLJ 171 FC[3], the appellant agreed to sell a melting furnace with a required temperature specification of not less than 2600°F.***

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However, the appellant failed to meet this specification. The respondent subsequently claimed that the appellant had breached a fundamental condition of the contract.

The Federal Court held that the appellant, as a reasonable person, could have foreseen the resulting loss from the delay. Accordingly, damages were awarded to the respondent under **Section 74(2) of the Contracts Act 1950.**

In conclusion, a claim for damages is more likely to succeed when the aggrieved party can provide sufficient evidence that the breach of contract was caused by the defaulting party.

Step-by-Step Guide to Responding to a Breach of Contract and Safeguarding Your Business

1. Review the Contract

- **Check the terms**: Read the contract carefully to see what the other party agreed to do and whether they've broken those terms.
- **Look for specific clauses:** Some contracts have provisions on how to handle breaches, including notice periods, dispute resolution steps, and penalties for non-performance.
- **Jot down timeline:** The factual matrix is crucial in understanding how the breach occurred. Record the events in chronological order, starting from pre-contract discussions, through the performance of the contract, and finally to the point of breach. This timeline helps identify key moments that contributed to the breach and supports your legal position.

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2. Document Everything

- **Keep records:** Collect all emails, texts, letters, and any correspondence that shows the breach (e.g., missed deadlines, faulty delivery).

- **Track your losses:** If the breach caused financial harm (lost profits, extra costs), make a record of that too. Advisable to keep all the receipts, invoices and any other supporting documents to support your case.

3. Notify the Breaching Party

- **Send a formal notice**: If you believe a breach has occurred, notify the other party in writing. Be clear about the breach and what remedy or compensation you expect.

- **Stay professional:** Even if you are upset, keep it polite and professional. The goal is to resolve things, not escalate the situation.

- **Provide time frame:** In your notice regarding the breach, specify a clear time frame within which the defaulting party must respond or take corrective action. It is generally advisable to allow 7 to 14 days for the other party to address the issue. This gives them a reasonable period to resolve the matter before further legal action may be pursued.

4. Try to Resolve the Issue (Negotiate)

- **Talk to the other party:** Sometimes breaches happen due to misunderstandings or unforeseen problems. See if you can work it out without going to court. This is the best route in settling the matter.

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- **Offer a solution:** If they're willing to fix things, suggest a reasonable way forward. For example, you might agree to an extended deadline or partial payment.

- **Consider alternative solutions:** You may want to offer them a chance to correct the breach (e.g., a new delivery date) or a discount on future services instead of outright cancelling.

5. Assess the Impact of the Breach

- **Material vs. Minor Breach:** If the breach is material, it's more serious, and you may want to consider cancelling the contract. If it's minor, you may still be able to go ahead with the agreement, potentially reducing the amount owed or requiring fixes.

- **Loss of profits:** Calculate whether the breach has caused actual losses—whether financial (like loss of business) or other tangible harm.

- **Wasted expenditure:** Calculate all the costs that you have incurred in fulfilling the performance of the contract.

6. Consider Legal Action

- **Mediation or arbitration:** Some contracts have clauses that require you to resolve disputes through mediation or arbitration rather than going to court. This could save time and legal costs.

- **Filing a lawsuit:** If negotiations fail and you've suffered significant harm, you may decide to take legal action. You'd likely want to consult an attorney to determine the strength of your case.

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Conclusion

In the event of a breach of contract, selecting the appropriate legal remedy is critical—not only for recovering losses but also for preserving business relationships and minimizing disruption. Whether through damages, specific performance, or termination, the remedy must align with the severity of the breach and the strategic interests of the organization.

By proactively incorporating clear contractual terms, dispute resolution mechanisms, and risk mitigation strategies, businesses can position themselves to respond effectively and decisively when a breach occurs. Legal counsel plays a key role in guiding these decisions and ensuring the chosen remedy upholds the company's legal and commercial objectives.

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