LAW OF CONTRACT

- Measure of damages for breach of contract which is terminable in certain circumstances.
- What losses may be compensated.

REPUBLIC OF KENYA

IN THE HIGH COURT OF KENYA AT NAIROBI

MILIMANI COMMERCIAL COURTS

CIVIL CASE NO. 704 OF 2000

KENYA BREWERIES LIMITED ..... PLAINTIFF

VERSUS

NATEX DISRIBUTORS LIMITED ..... DEFENDANT

JUDGEMENT

This suit revolves around a beer distributorship agreement entered into on 30.5.97 between Kenya Breweries Ltd, the plaintiff (defendant in the counterclaim) and Natex Distributors Ltd, the defendant (Plaintiff in the counterclaim) and which agreement was terminated on 28.7.1999. Natex Distributors Ltd (Natex) conceded Kenya Breweries Ltd (KBL) case against it in respect of dishonoured cheques and suffered judgment in the sum of Kshs.4, 951,326.28 on 5.6.03. It also abandoned its claim that the said contract was obtained by misrepresentations. What now remains for trial is NATEX'S counterclaim against KBL. The essence of that claim is that the distributorship agreement was illegally terminated and as a consequence of the said termination the company has suffered the loss and damage pleaded. Thus the principal issues for trial in the counterclaim are (i) whether the termination of the contract between KBL and Natex by KBL on 28.7.99 was unlawful, (ii) if the answer to (i) is in the affirmative, what loss, if any, Natex has suffered, and (iii) whether KBL is liable to compensate Natex for any such loss.

This case does not turn on the credibility of witnesses. Indeed I would say that all witnesses who testified on both sides were forthcoming and sincere in their evidence. I believed their presentation of facts and treated their opinions as no more than that. The case turns largely on the interpretation of the distribution agreement (D exh. 3) and the termination letter (D exh. 6). The said letter of 28th July, 1999 is a short one and may be read in full. It was in the following terms -

"28th July, 1999
Managing Director
Natex Distributors Limited
P. 0. Box 61405
NAIROBI

Dear Sir, TERMINATION

Our letter of 25th June, 1999 and yours of 30th June refers. Among other things. To date you are yet to pay Kshs.5.7 million after your cheques bounced on 24th despite your promise of 26th July.
You have been out of operation since 25th June, 1999. This cannot continue further as KBL business is suffering heavily.
The Distribution Agreement is very explicit on these and in view of the foregoing, we are compelled to invoke clause 19 (b) (iii) and terminate your Distributorship forthwith.
Thanks for the period we have had to do business with you.
Yours faithfully,
For: KENYA BREWERIES LIMITED
J. ICHOROH
CUSTOMER SERVICE DIRECTOR"

From the evidence and submissions made, I understood Natex's case to be that there was no clause 19 (b) (iii) in the contract and accordingly, the termination of the contract was illegal. KBL conceded in evidence, quite properly if I may say so, that indeed there was no such clause and the reference thereto was a mistake. The intention was to invoke clause 17 (c) (iii) as there was a fundamental breach of the contract. That fundamental breach arose from the circumstances that the contract was one for beer distributorship and the defendant was in breach thereof as it had bounced cheques worth Kshs.5.7 million and could not therefore be supplied with stock to distribute and it had indeed been out of operations since 25th June 1999. To assist their assertion of a fundamental breach of the terms of the contract, the plaintiff also invoked clause 3 of the said contract. At this stage I should read in full the provisions of the said clauses.

"3. You will pay for all your purchases in cash, bankers cheques, bank guaranteed cheques, or as specified by KBL from time to time.
17 (c). Your appointment as KBL's distributor may also be terminated, forthwith upon service on you of notice in writing from KBL to that effect, in the event of your:- ……
(iii) Committing any other breach of the terms and conditions hereof and not remedying the same to KBL's satisfaction within (7) days of the date of any written notice from KBL drawing attention to such breach."

Natex argued that clause 3 of the contract only specified the mode of payment for purchases and had nothing to do with termination on grounds of dishonoured cheques. It also argued that for clause 17 (c) (iii) to be invoked successfully, it had to be shown that there had been a written notice from KBL drawing the distributor's attention to alleged breaches of contract and calling on it to remedy the same within 7 days, a condition which was not satisfied in this case. Moreover, it was argued, dishonouring cheques could not be a ground for termination as Natex had previously dishonoured its cheques and been allowed to make them good without the agreement being terminated and accordingly the KBL had waived its right to rely on dishonour of cheques as a ground for termination or it was estopped from relying on that ground by its conduct. To those arguments, KBL argued that a fundamental breach of the contract by Natex went to the root of the contract and could not be cured by a ninety days notice provided in clause 17 (a) [which provided that the contract may be terminated by either party giving to the other ninety (90) days notice] and that even the 7 days notice contemplated by clause 17 (c) (iii) was unnecessary as the breach had continued for over 30 days. It also argued that its accommodation of past dishonour of cheques by Natex was discretionary and the same could not be regarded as a waiver of its rights.

I have carefully considered the evidence and the submissions on the issue of KBL's liability to Natex. Having done so I make the following findings. Parties to a written contract are bound by its terms. KBL terminated Natex contract by invoking a non existent clause. That was not legitimate. However, the written contract had a termination clause, i.e. clause 17. The same could lawfully be invoked. If the plaintiff's intention was to invoke clause 17 (c) (iii), and I accept the evidence that such was the case, a condition precedent thereto was service of a 7 days notice drawing the distributor's attention to the breaches complained of and calling for their remedy. That condition was not satisfied, there was no such letter and it is not an adequate answer to say that the distributor was in breach for 30 days before the letter

of termination. In my opinion, there could not be a breach without default in complying with the terms of a 7 days notice contemplated by the clause. And of course clause 3 of the contract does not assist the plaintiff at all as it had nothing to do with termination of the contract. As regards Natex claim that KBL had waived its rights or was estopped by conduct from relying on the fact of dishonour of cheques to terminate the contract, I reject the same. Waiver is contractual and must be express and duly supported by consideration. And there cannot be an estoppel unless there was a representation intended to be acted on and actually acted on that dishonour of cheques was inconsequential. Those elements of waiver and estoppel are absent here and the indulgences granted to Natex do not amount to waiver or estoppel as understood in law. Be that as it may, and while I am with much sympathy for KBL's contention that Natex was in fundamental breach of the distribution contract by virtue of the two reasons given in the letter of termination, I am constrained to agree with the arguments advanced on behalf of Natex that the termination was not in accordance with the written contract and it was accordingly illegal. However much a party resents the behaviour of another party to the contract, it cannot terminate it without following the laid down procedure. The matter would have been entirely different if Natex was trying to enforce its rights to be supplied with purchases under the contract. In that event KBL's refusal to make further supplies could have been justified on the ground that the company was in fundamental breach of the contract and accordingly KBL had been released thereby from its obligations to perform its part of the said contract. I now turn to the issues of loss and whether KBL is liable therefore to Natex.

The general principle of compensation in both contract and tort is that subject to the doctrine of mitigation of loss, the claimant is to be put as far as possible in the same position as he would have been if the breach complained of had not occurred: ***restitutio in integrum.*** Accordingly the claimant is entitled to gains prevented by the breach, expenses caused by the breach, and expenses rendered futile by the breach. In the instant case the defendant claims to have spent Kshs.1,844,356.20 on capital development of Kinoo and Uthiru premises which he had rented to service the beer distribution business. In its view those expenses are now thrown away expenses and they are recoverable. It also claimed that it had purchased two motor vehicles KAE 740C and KAG 128B on hire purchase terms from Southern Credit Finance Ltd on hire purchase terms exclusively for the beer distributorship business. The hire purchase charges were properly serviced until the beginning of July 1999 when the distribution contract was terminated. The vehicles were then repossessed by the Financier and sold to other parties. The outstanding balances on the hire purchase accounts at the end of June 1999 was Kshs.4, 565,519. The defendant submits that that amount may be regarded as the value of the said lorries as it had spent far in excess of Kshs. 5 million in servicing the hire purchase agreement during the period it was in business. It maintains that this is another thrown away expense for which KBL should be held liable. The defendant also contends that it had an overdraft facility with Giro Bank for the purpose of the beer distributorship business which was secured by a charge over L.R. No.209/4401/731. That account had a debit balance of Kshs.2, 575,023.90 as at the end of June 1999. The account was not serviced after July 1999 when the agreement was terminated and accordingly the charged property was sold sometime in year 2002 to recover the outstanding balance of Kshs.4, 020,448.80. The defendant claims that loss of its charged property was as a result of breach of contract by the plaintiff and the same should be recoverable as an expense incurred as a result of the breach.

In response, the plaintiff argues that the damages claimed are not a consequence of its terminating the contract. It contends that the person in breach is responsible only for the result and damage which he ought to have foreseen or contemplated when the contract was made as not being unlikely. In that vein it argues that restitution of capital expenditure costs would not have been a foreseeable consequence of termination of the contract. It is also argued that the effect of the exit clauses in the contract as relates to wasted expenditure should be considered and that, in that regard, the defendant had not demonstrated that had notice been given it would have avoided the alleged loss and damage. Further more, in the case of sale of the charged property, it is argued that the defendant failed to act reasonably and mitigate its loss in that had the property been sold at the earliest opportunity after the termination of the contract in July 1999 when the overdraft account had a debit of Kshs.2,525,972.25, the accrual of interest in the sum of Kshs.2,039,777.00 would have been avoided and accordingly, the plaintiff is not entitled to that amount. As regards the Lorries, the plaintiff contends that the defendant did not show that the financiers could not have obtained a better price in the market other than have the loan taken over by new customers and accordingly the amount of Kshs.4,565,519/= claims becomes uncertain.

Having considered the arguments and evidence pertaining to the losses claimed by Natex I am of the following view. The capital expenditure in the sum of Kshs.1, 844,356.20 for the exclusive purpose of facilitating the performance of the beer distributorship contract is prima facie an, expenditure rendered futile by the breach. However the Company did have the use of those facilities for a period of about two years before the contract was terminated. Therefore think a discount ought to be made for that use. In the absence of expert guidance on devaluation thereof I will assume a discount of 20%. That would leave the compensable loss at Kshs.1, 475,484.96. As regards the amount outstanding in the hire purchase accounts of the two motor vehicles in the sum of Kshs.4,565,519, I am unable to accept that the same may be regarded as the value of the said vehicles and for which the defendant should be compensated either as a gain prevented by the breach of contract or a loss caused by such breach or even an expense rendered futile. If the defendant's claim is that it lost the said vehicles, the proper measure of damages would have been a valuation of its interest in the said vehicles. And if that be so, it would be difficult to discern what its interest in the said vehicles was considering that it had possession of them as a hire purchaser and the title thereto was still vested in the finance company. I think this aspect of the claim is misconceived. As regards the quantum for the loss of the defendant's charged property as a result of the breach, I am unable to accept that the same should be pegged to the amount outstanding on the overdraft account in year 2002 in the sum of Kshs.4,565,519/=. I agree with the plaintiff's counsel that the defendant should have taken action to mitigate its loss by having the charged property sold in July 1999 or soon thereafter when the overdraft stood at Kshs.2,525,972.25 as at 6.7.99 . If that had been done and assuming the said property had a market value of Kshs.5 million (which is the price it fetched at the auction), the defendant's loss would have been the difference between the value of the said property and the amount of the overdraft he was obliged to pay as at the moment of the termination of the contract. That loss would have been Kshs.2, 474,027.75. In those premises, I would assess the defendant's losses in the sum of Kshs.3, 949,512.71.

The next question is whether the plaintiff should in the circumstances of this case be condemned to compensate the defendant for those losses. In that regard, I am of the opinion that where a claim is predicated on breach of a contract which provides for its own termination, the principle of ***restitutio in integrum*** would require that the proper measure of damages should be the loss suffered by the claimant which could not otherwise have been suffered had the contract been lawfully brought to an end. For example, in cases of damages for breach of contract of employment, it is established that where the employment is terminable by notice, the measure of damages is the loss suffered in default of serving the claimant with the appropriate notice. In similar vein, in the instant case, the beer distribution contract could have been brought to an end by a 90 days notice for no reason under clause 17 (a) or forthwith upon failure to comply with a 7 days notice to remedy any alleged breaches of contract under the provisions of clause 17 (c) (iii). The wrong that KBL committed was not therefore to terminate the agreement but to do so without following the provisions of the said agreement. That is the breach that was committed. The question therefore of whether the defendant could have avoided the losses in respect of which the claim is made had the plaintiff followed the correct procedure in terminating the contract cannot be avoided. And so the Court must ask whether, if KBL had given Natex 90 days notice of termination of the contract in accordance with clause 17 (a) or a seven days notice to remedy the breach of dishonoured cheques in the sum of Kshs.5.7 million and resume business operations followed by a termination letter in default, Natex could have avoided the repossession of the two motor vehicles or the sale of its charged property over an overdraft standing in the sum of Kshs.2,525,972.25 or avoided the loss of capital expenditure in respect of the Kinoo and Uthiru premises? There was no evidence from Natex to that effect. And seeing that the company had been making losses almost from inception and that it was out of business for about a month before the contract was formally terminated, it is more probable than not that the losses recited could not have been avoided for the Company's continuation with the beer distributorship business and hence the service of its commercial obligations was not probable in the circumstances. In those premises, to compensate the defendant for the alleged losses would be perilously close to injecting it with a dose of unjust enrichment. In short, I find that the plaintiff is not liable to compensate the defendant for the losses claimed.

In the result, I find that whereas KBL is guilty of breach of contract, it is not liable to compensate Natex for the losses claimed. However a breach of contract should not count for nothing. In my judgment the defendant is entitled to nominal damages for breach of contract which I assess in the sum of Kshs.50,000/=. And it is also entitled to the costs of the counterclaim.

It is so ordered.

DATED at **NAIROBI** this 19th day of January 2004.

A.G RINGERA

JUDGE