

THE CONTRACT PREVAILS: SUPREME COURT CONFIRMS THERE IS NO PRINCIPLE OF DEEMED FULFILMENT OF CONDITIONS PRECEDENT UNDER ENGLISH LAW

The Supreme Court in **King Crude Carriers & Ors v Ridgebury November & Ors** has unanimously overturned the Court of Appeal and settled a long-debated point in English contract law, holding that the principle of ‘deemed fulfilment’ of conditions precedent (also known as the *Mackay v Dick* principle) is not part of English law.

Key takeaways

- There is no *Mackay v Dick* principle of ‘deemed fulfilment’ of conditions precedent in English law.
- As a result, where a debtor breaches a contract and wrongfully prevents the fulfilment of a condition precedent to a debt, the innocent party cannot treat the condition as having been waived or fulfilled to pursue a debt claim.
- Instead, usual English law contractual principles apply. English law focuses on the terms of the contract, and their proper interpretation, to determine whether a debt has accrued.
- Unless the parties have agreed otherwise, the appropriate remedy will be damages for breach of contract (subject to usual principles of causation, mitigation and remoteness).
- Where contracting parties wish to prevent a party in breach from benefiting from its own wrong, parties should consider express drafting to this effect.

Background

The appeal arose in relation to the sale of three second-hand oil tankers. The sale contracts (which were materially identical and used amended 2012 Norwegian Salesform standard form terms) provided that the buyers would pay deposits of 10% of the purchase price into third-party escrow accounts shortly after the accounts were opened and they would provide all necessary ‘know your client’ documentation for this purpose. The buyers breached the contracts by failing to provide the documentation, meaning that the accounts could not be opened and the deposits were not paid.

The sellers terminated the contracts and claimed the deposit amounts in debt. The sellers relied on a principle derived from a House of Lords decision in the Scottish

case of *Mackay v Dick*, which provides that where a debtor’s breach of contract results in the non-fulfilment of a condition precedent to a debt, the condition is deemed to be waived or satisfied on the basis that a wrongdoer should not be able to take advantage from their own breach. In contrast, the buyers argued that the sellers were entitled only to compensatory damages for breach of contract.

Damages versus debt claims

The difference between debt claims and damages claims is important: it comes down to the ease of recoverability and enforcement. A debt claim is for a specific sum that has become due and payable under a contract but is unpaid. The creditor can recover the full amount of the debt without needing to prove its loss. A damages claim, on the other hand, aims to compensate an innocent party for losses it has suffered due to a breach of a primary obligation in a contract. However, the innocent party must prove its loss, and the amount of damages payable will depend on the principles of causation, mitigation and remoteness of loss, for example. If an innocent party is unable to prove much/any loss resulting from the breach of contract, it will recover no/limited damages.

This was the case here. Based on assumed facts, a subsequent increase in the market price of the tankers versus their purchase price meant no loss had been suffered and, therefore, (absent a claim in debt) only nominal damages would be payable to the sellers.

The decisions

In a pendulum of decisions, the dispute was initially referred to arbitration, resulting in the sellers obtaining awards in their favour. The buyers successfully appealed the awards to the Commercial Court under section 69 of the Arbitration Act 1996, but the Court of Appeal unanimously reversed that decision in favour of the sellers. The buyers appealed to the Supreme Court which unanimously allowed their appeal, reinstating the High Court’s decision.

The *Mackay v Dick* principle is not part of English law

In reaching its decision that the *Mackay v Dick* principle is not part of English law, the Supreme Court reasoned that:

1. The *Mackay v Dick* principle was drawn from civil law rather than English case law.
2. English authorities are inconsistent and “do not speak with one voice” on whether the principle exists.
3. The principle would fundamentally undermine the English law on contracts for the sale of goods (among others) and limiting its ambit by way of exceptions would lead to uncertainty in a way that does not make for a robust principle of law.
4. The principle is based on a legal fiction of deeming a condition precedent as fulfilled or waived which obscures transparency in legal reasoning and should be avoided where possible.
5. English contract law proceeds on the basis of the terms of the contract (express and implied) and their proper interpretation, rather than relying on fictional fulfilment of conditions precedent. The Supreme Court considered this approach to be consistent with the importance English law attaches to freedom of contract and that it promotes certainty and predictability.
6. No injustice results from rejecting the principle – where a condition precedent has not been fulfilled because of the debtor’s breach of contract, the Supreme Court held that the breach is appropriately and adequately dealt with through a remedy in damages.

Contractual interpretation and implied terms: a party may benefit from its wrong

Having rejected the *Mackay v Dick* principle, the Supreme Court turned to the contracts in issue and held that, on a proper construction of their terms, the deposits had not accrued.

The sellers’ interpretation arguments failed. The Supreme Court held that there is no “universal principle” of interpretation that a contract should be interpreted in such a way not to permit a party to take advantage of their own wrong. To the contrary, the Supreme Court considered that there are many contractual circumstances in which a party may do so: an obvious example being that damages for breach of contract aim to compensate the claimant rather than to punish the defendant.

As the buyers were not relying on their breach to treat the contracts as being at an end or to claim a benefit or invoke a right under them, the interpretative principle did not apply. Applying the modern objective and contextual approach to contractual interpretation (*Investors Compensation Scheme v West Bromwich Building Society*; *Arnold v Britton*; *Wood v Capita*), the

Supreme Court found that the correct interpretation of the express preconditions in the contracts was that they did not need to be satisfied where the buyers had defaulted. The Court considered that the interpretation proposed by the sellers would rewrite the contracts.

The sellers’ proposed implied terms were also found to be flawed. The Supreme Court considered that they would render performance impossible (as they would lead to a situation where the accounts might not exist, meaning the buyers would never be able to pay the deposits) or would rewrite the contracts and contradict the express terms of the contracts (as would be the case if a term were implied that the deposits instead be paid directly to the sellers).

Preconditions for payments not merely “machinery for payment”

The Supreme Court also dismissed the sellers’ alternative argument that the deposits had accrued at the time the contracts were concluded and the contract terms for setting up the escrow accounts were merely “machinery for payment”. In doing so, the Supreme Court approved an earlier Court of Appeal decision in *The ‘Blankenstein’* concerning terms similar to those in the present case.

Comment

The Supreme Court’s decision provides helpful clarification on a longstanding area of uncertainty in English contract law by rejecting the *Mackay v Dick* principle under English law. In doing so, the Supreme Court has restated core principles of English law, namely freedom of contract, certainty and predictability. In this case, the sellers had (in the words of the Court of Appeal) been “messed around” by the buyers and were entitled to compensatory damages for their loss of bargain, even though the direction of the market meant that those damages would be nominal.

The decision also highlights the risks for commercial parties, with the Supreme Court noting that “[c]ontract law permits efficient breach and the defendant may therefore profit from its wrong”. The decision is an important reminder for commercial parties to ensure they consider the potential risks when negotiating conditions precedent. This is particularly important where those conditions depend on preconditions, non-fulfilment of which may enable a party to sidestep their contractual obligations, in some cases with limited repercussions.

It remains open to contract parties to determine how a condition precedent operates. If the parties intend that breach of contract should result in a condition precedent to a debt obligation falling away, express drafting should be used. Doing so may allow the creditor to bring a claim in debt and recover the full amount without needing to prove its loss.

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