

BETWEEN: **SHEM CONSTRUCTION**
Appellant

AND: **THE REPUBLIC OF VANUATU**
Respondent

Date of Hearing: 5th August 2025

Coram: *Hon. Chief Justice Vincent Lunabek*
Hon. Justice Mark O'Regan
Hon. Justice Anthony J Besanko
Hon. Justice Dudley Aru
Hon. Justice Viran M Trief
Hon. Justice Edwin P Goldsbrough

Counsel: *Kent T Tari for the Appellant*
Mr Sammy Aron for the Respondent

Date of Decision: 14th August 2025

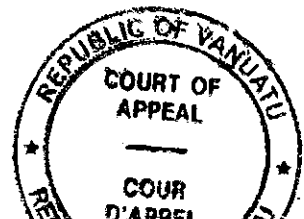
JUDGMENT OF THE COURT

Introduction

1. This is an appeal from a decision of a Judge of the Supreme Court. The appellant is Shem Construction (Shem) and the respondent is the Republic of Vanuatu. Shem brought an action against the respondent claiming damages for breach of contract. The primary judge held that the claim failed and dismissed the action. Shem appeals against the order of dismissal.

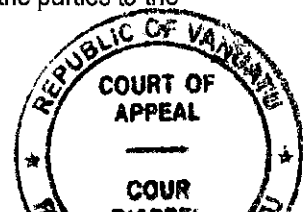
Background

2. On the 2nd of March 2022, Shem entered into a contract with the Ministry of Agriculture, Livestock, Forestry, Fisheries and Biosecurity ("MALFFB") to construct the tissue culture laboratory at the Vanuatu Agricultural Research and Technical Centre ("VARTC") in Santo. We will refer to this contract as the Building Contract.
3. The start date in the contract was 14th of March 2022. Due to the nationwide Covid-19 lockdown, work under the contract did not start until 11th of May 2022. Interim payments were to be made



under the contract and one particular interim payment is important. It is the second interim payment. Under the procedure set out in the Building Contract, Shem was to submit at the intervals stated in the Building Contract an interim payment statement to the Construction Supervisor. Assuming all was in order, the Construction Supervisor had seven days to certify the interim payment and thereafter the other party to the Building Contract had 30 days to make the payment due. The second interim payment was for an amount VT1,926,000 and related to the supply and construction of the foundation and floor slab. We will refer to this liability as the second interim payment. There had been a prior interim payment of VT2,000,000 for the completion of preliminaries and general. That progress payment was paid to Shem Construction in full and without any deduction.

4. There is another contract which was relevant in the circumstances of this case. It is dated 9th September 2021 and is between Shem and the Department of Customs and Inland Revenue ("DCIR"). Shem was significantly in arrears in the payment of Value Added Tax ("VAT"). Under this contract there was a repayment plan. The agreement was that 20% of all payments made to Shem pursuant to government contracts would be deducted for VAT arrears. The primary judge found that this contract enabled Shem to be issued with a tax clearance certificate which was issued on 10th October 2021 and had an expiry date of 9th of September 2022. The tax clearance certificate was provided to MALFFB. The primary judge said that Mr Shem accepted that MALFFB was not aware of the VAT arrears agreement when the contract with MALFFB was signed. We will refer to the contract with DCIR as the Repayment Contract.
5. As we have said there was no deduction of 20% in relation to the first interim payment of VT2 million under the Building Contract.
6. With respect to the second interim payment, Shem submitted an interim payment statement to MALFFB for the amount of VT1,926,000. On the 15th of October 2022, the Department of Finance issued cheque number 2400883 to Shem for VT481,500. In other words, Shem Construction did not receive a cheque for the full amount of the payment request in the amount of VT1,926,000 which was payable under the Building Contract. That came about because the Department of Finance deducted the sum of VT1,444,500 for VAT arrears purportedly pursuant to the Repayment Contract. There was no dispute at the trial that the deduction was a good deal more than the permitted deduction of 20% referred to in the Repayment Contract. We will refer to the deduction above 20% as the excessive deduction. The primary judge found that the reason for the amount of the deduction was because a 20% deduction was not made in relation to four prior payments. Shem was not given notice that such a large deduction would be made. It is clear that the excessive deduction was not contemplated under the Repayment Contract.
7. Shem commenced this action on the 11th of December 2023. In December 2024 DCIR paid VT1,051,000 to Shem. That amount represented the excessive deduction.
8. One further matter should be noted before we leave this section of our reasons. We have referred to the Building Contract as a contract between MALFFB and Shem and the Repayment Contract as a contract between DCIR and Shem. Shem disputes this characterisation of the parties to the



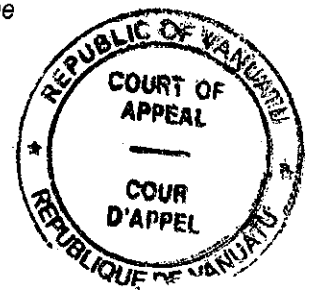
respective contracts. It submits that MALFFB and DCIR are not legal entities and that the other party in the case of each contract was the respondent. We will come back to consider this argument.

The Reasons of the Primary Judge

9. The primary Judge said that the principal issue before her was whether or not the Building Contract had been unlawfully terminated by MALFFB. That is undoubtedly correct. The issue had been identified in that way by counsel in the agreed and disputed facts and issues filed on 28th March 2025. As the primary Judge noted, if the answer to that question is in the affirmative then further questions arose as to whether Shem was entitled to damages and if so, what the quantum of these damages should be.
10. The primary Judge found that on the 30th of June 2022 Shem submitted a request for payment VT1,926,000 and that there was a progress certificate signed by the Project Engineer. Her Honour found that on the 4th of July 2022 a Local Purchase Order (LPO 470-019108) was issued for VT1,926,000. This procedure for interim payments is set out in clause 5.9.4(1) and (2) in the Building Contract. That clause is the following terms:

5.9.4. Interim Payments

- (1) *The Contractor shall submit, at the intervals stated in the SCC, an Interim Payment Statement to the Construction Supervisor, in the form approved by the Construction Supervisor, showing;*
 - (a) *The value of the Works executed on Site, including any materials and goods delivered to the Site for incorporation in the Works, for the period covered by the Statement;*
 - (b) *Any other sums to which the Contractor considers himself to be entitled under the Contract (if applicable);*
 - (c) *Less the total of interim progress payments made by the Employer;*
 - (d) *Less the amount to be deducted for Retention, at the rate stated in Clause 5.9.6;*
 - (e) *Less the amount, if any, to be recovered from the Contractor due to an advance payment having been made to the Contractor.*
- (2) *The Construction Supervisor shall satisfy himself that the works accomplished for the respective period have been completed without the defects in pursuance of the Contract, and any statutory Acts regulating construction Works in Vanuatu, and within 7 days shall certify the interim payment which he considers due and payable to the Contractor in respect of the above-mentioned items. The Employer shall pay to the Contractor the amount so certified within 30 days of the date of the Payment Certificate issued by the Construction Supervisor. The basis of calculation of payments shall be that specified in the Bill of Quantities / Schedule of Activities [Employer to delete whichever is not appropriate, depending on the type of contract in question].*



11. The primary Judge found that there had been a breach by MALFFB of the Clause 5.9.4(2) of the Building Contract in that MALFFB had not paid the amount due within 30 days of the date of the payment certificate issued by the construction supervisor. Her Honour did not find that the excessive deduction from the second interim payment was a breach of the Building Contract. We will return to this point.
12. Shem argued before the primary Judge that the Building Contract had been "verbally" terminated by MALFFB. Shem argued that it had never received a notice of termination of the contract or a letter of termination and that in those circumstances the termination of the Building Contract was unlawful because it had not been carried out in accordance with the terms of the contract. Shem advanced a further argument. It was that MALFFB's actions in terminating the Building Contract were unlawful because the requirement in Clause 5.13.1(1)(a) was not fully met before the contract could be terminated.
13. Clause 5.13 of the Building Contract deals with the termination and suspension of the contract. In so far as it is relevant, it is in the following terms:

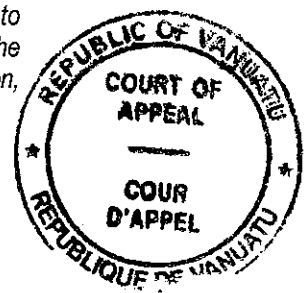
5.13 TERMINATION AND SUSPENSION

5.13.1. Termination for Default

- (1) *The Employer may, without prejudice to any other remedy for breach of Contract or written notice of default sent to the Contractor, terminate the Contract in whole or in part if the Contractor:*
 - (a) *Abandons the works, refuses or fails to comply with a valid instruction of the Employer or fails to proceed expeditiously and without delay; or;*
 - (b) *Persistently or repeatedly refuses or fails to supply sufficient properly skilled workers or proper materials; or*
 - (c) *Persistently disregards laws, ordinance, or rules, regulations or orders, or a public authority having jurisdiction; or*
 - (d) *Otherwise is guilty of substantial breach of a provision of the Contract; or*
 - (e) *Has engaged in corrupt, fraudulent, coercive or obstructive practices on competing for or in executing the Contract. Termination for insolvency*
- (2) *The Employer may at any time terminate the Contract by giving notice to the Contractor if the Contractor becomes bankrupt or otherwise insolvent. In such event, the Contractor shall be compensated for the Works completed and materials supplied up to the date of termination only, provided that such termination will not be prejudice or affect any right of action or remedy that has accrued or will accrue thereafter to the Employer*

5.13.2. Termination for Convenience

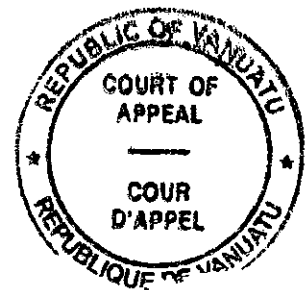
- (1) *The Employer may, without cause, by written notice order the Contractor to terminate its engagement under the Contract. Upon such termination, the Contractor shall be paid for the Works performed up to the date of termination,*



provided that any such uncompleted Works were not late or otherwise overdue for completion at the date of termination. The Contractor shall promptly make every reasonable effort to procure cancelation upon terms acceptable to the Employer of all outstanding subcontracts.

5.13.3. Termination by the Contractor

- (2) *In the event the Employer fails to comply with the requirements under Clause 5.9.3 and 5.9.4 within a period of 30 days after the payments became due, the Contractor may after 7 days serve a notice to the Employer to terminate this Contract and any costs shall be determined in accordance with the provisions of Clause 5.9.4.*
14. The primary Judge noted that the respondent's argument was that Shem had abandoned the contract and did not give notice of termination. The respondent argued that the Building Contract was lawfully terminated pursuant to 5.13.1.
15. The primary Judge referred to the terms of Clause 5.13.3 and said that Shem could have terminated the Building Contract under that Clause on the ground was that it had not been paid within a period of 30 days after the second interim payment became due. The procedure would involve Shem Construction 7 days after the non-payment serving a notice on MALFFB to terminate the contract. The primary judge said that there was no evidence that Shem had done that.
16. An issue before the primary Judge was whether Mr Shem's assertion that a staff member at MALFFB had told him that the Building Contract had been terminated was correct. The primary Judge considered the evidence given by Mr Shem and evidence given by Ms Gwendoline Kalsev. Ms Kalsev was the procurement officer at MALFFB who facilitated the procurement process for the Building Contract. We do not need to outline that evidence because there was no challenge to the finding made by the primary judge that she was unable to accept Mr Shem's evidence that an unspecified person had told him on the 18th of August 2022 that the Building Contract had been terminated. Even if there was a challenge it must be rejected. The primary Judge saw and heard the witnesses and made findings of fact. There is no basis to interfere with Her Honour's findings.
17. The primary Judge found that Shem did not carry out any work under the Building Contract after completing the supply and construction of the foundations and floor slab.
18. The primary Judge said that she considered that Shem ceased work under the contract due to the financial difficulties it encountered when the excessive deduction was made and Mr Shem was not advised that such a large amount would be deducted. Her Honour said that in that sense Shem abandoned the works which could then give rise to MALFFB terminating the contract pursuant to Clause 5.13.1(1).



19. The primary Judge said that the evidence did not support a finding on the balance of probabilities that MALFFB terminated the contract unlawfully. Her Honour reached that conclusion for three reasons. First, Shem was not fulfilling the terms of the contract as it had ceased work. Her Honour said that, in other words, Shem had abandoned the works. Secondly, the primary Judge said that she found Mr Shem's evidence that an unidentified staff member had verbally terminated the contract implausible. Thirdly, Her Honour said that even if Shem had been verbally advised that the contract was terminated, it was clear on Mr Shem's own evidence that Shem did abandon the works due to financial difficulties. The abandonment of the works gave MALFFB the right to terminate the Building Contract and MALFFB was not required to give any notice to Shem that the termination had taken place. That was in contrast to Clauses 5.13.1 and 5.13.2 where notice of termination was required.
20. In the result her Honour concluded that the claim had not been proved on the balance of probabilities. Her Honour said that she was unable to say that it was more likely than not that MALFFB terminated the contract unlawfully.
21. Before leaving this summary of the primary Judge's reasons we set out two paragraphs in her Honour's reasons which are important in our consideration of the first issue identified below.

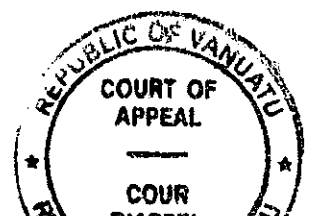
(14) *Under clause 5.9.4(1) of the contract, on 30 June 2022, Shem Construction submitted a request for payment of VT 1,926,000 for the supply and construction of the foundation and floor slab once the work was completed. There was a progress certificate signed by the project engineer. On 4 July 2022, LPO ("local purchase order") 470-019108 was issued for VT 1,926,000 being for the supply and construction of the foundation and floor slab.¹ But as already noted, the Department of Finance issued a cheque to Shem Construction for VT 481,500 on 15 October 2022 because a deduction had been made for VAT arrears.*

...
(17) *I consider that MALFFB fulfilled its obligation under the contract to pay Shem Construction the interim progress payment of VT 1,926,000 due under the contract. That is because Tony Sewen's evidence establishes that on 4 July 2022, LPO 470-019108 was issued for the sum of VT 1,926,000, being an interim payment for works done under the contract. The Department of Finance eventually issued a cheque to Shem Construction but did not pay the company the full amount of the interim payment because of the over deduction for VAT arrears pursuant to Shem Construction's agreement with DCIR. This was done by way of a credit note against the VAT arrears, as per Tony Sewen's sworn statement, annexure TS 7. That was a separate issue which did not form part of the contract between Shem Construction and MALFFB. DCIR was not a party to that contract.² The VAT deduction was made pursuant to a statutory power, and a separate agreement between Shem Construction and DCIR.³*

¹ As per Tony Sewen's sworn statement, annexure TS 7

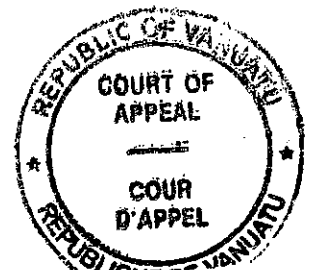
² See the discussion about privity of contract in *Pipite v Republic of Vanuatu* [2025] VUSC 9

³ The deductions were made pursuant to s 35 of the Tax Administration Act No 37 of 2018 as detailed in Collins Gesa's sworn statement filed on 26 November 2024

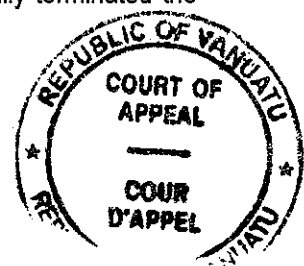


Analysis

22. There are two issues in the case.
23. The first issue is as follows. Shem was entitled to the amount of VT1,926,000 minus 20% by way of the second interim payment. Shem does not dispute the legality of the deduction of 20%. Shem's entitlement arose under the Building Contract. As we understand her Honour's reasons, she held that MALFFB has discharged its obligations to pay under the Building Contract upon the issue of the Local Purchase Order 478-019108 for VT1,926,000 being for the supply and construction of the foundation and floor. The Local Purchase Order is an internal government document.
24. If the primary Judge is correct and MALFFB met its obligation to make the second interim payment upon the issuance of the Local Purchase Order, then the only breach of the Building Contract committed by MALFFB is in failing to pay within 30 days. Even that proposition might be questioned as the certificate which provided on 30th June 2022 and the Local Purchase Order was issued on 4th July 2022. In any event, the failure to pay within 30 days was not the focus of Shem's case.
25. With respect, we do not consider that Her Honour's analysis is correct. There were undoubtedly two contracts. However, MALFFB and DCIR are not legal entities, and they are not separate legal entities. They are emanations or organs of the Republic of Vanuatu. The other party to the two contracts was the Republic of Vanuatu. That means that the respondent was bound to pay Shem VT1,926,000 with a deduction of 20% and no more than 20%. The excessive deduction was a breach of the Building Contract. There is a further point which was not argued on the appeal and which we do no more than flag. Even assuming that MALFFB is a separate legal entity, there may be a real question as to whether the issuance of the Local Purchase Order was sufficient to fulfil MALFFB's obligation to pay Shem under the Building Contract.
26. The second question is whether the respondent unlawfully terminated the Building Contract. Two matters must be borne in mind when considering this issue. First, breach of a contract and termination of a contract are two different legal concepts. One party to a contract may be in breach of the contract, but the other may decide not to terminate the contract. Secondly, termination by one party or abandonment by the other, are not the only means whereby a contract may come to an end. It may come to an end because both parties acquiesce in that state of affairs. We only mention this point because Shem's submissions seem to proceed on the basis that if it could be established that it did not abandon the Building Contract, then it followed as a matter of course that the respondent had unlawfully terminated the contract.
27. As it happens, we are of the view that the respondent had not unlawfully terminated the Building Contract. We are of the view that Shem abandoned the works within clause 5.13.1(1)(a) and that gave rise to a right in the respondent to lawfully terminate the contract. Alternatively, it could accept without more that the contract had come to an end.



28. The failure to pay the amount due under the Building Contract (including the excessive deductions) and to do so within 30 days were both breaches of the Building Contract which gave Shem the right under clause 5.13.3 to terminate the contract by notice. Shem did not serve a notice to terminate the contract. Those acts by the respondents are breaches of the Building Contract but they do not constitute without more, a termination of the contract. Those acts gave Shem the right to terminate the Building Contract by notice, but it did not exercise that right.
29. The only act that might be seen as termination of the contract by the respondent was the alleged advice Mr Shem said he was given by an unspecified person on 18th August 2022 that the Building Contract had been terminated. That evidence was rejected by the primary Judge and, as we have said, we see no reason to interfere with the judge's conclusion. There was no provision in the Building Contract permitting Shem to cease work under the contract until an interim payment was received. Mr Shem acknowledged that he did not carry out any work under the contract after the completing the supply and construction of the foundation and floor slab. It seems to us that the primary Judge in fact found that Shem had abandoned the works, although unsurprisingly in light of the issue before her Honour, she confined herself to the conclusion that Shem had not established on the balance of probabilities that the respondent had unlawfully terminated the contract.
30. We consider that the acts and conduct of Shem warrant the conclusion that it abandoned the works within the ordinary meaning of that term.
31. Shem submitted that the ordinary and natural meaning of "*abandonment*" did not apply when there was prior breach by the other party which had any significant effect on the financial ability of the innocent party to continue with the work. The primary Judge noted the submission by Shem that it was unable to continue with the work required under the Building Contract due to financial difficulties.
32. However, her Honour did not deal with this issue because of her conclusion that the only breach of contract by MALFFB was the non-payment of the amount due within 30 days. Shem's argument fails, even if, as we have found, the breach of the Building Contract included the non-payment of the excessive deductions. First, there is no warrant for giving the word "*abandonment*" a meaning other than its ordinary and natural meaning. Secondly, it is not the case that Shem's only option was to cease work under the Building Contract. Shem could have advised the respondent that it would terminate the Building Contract if payment of the amount due was not made. Shem could have terminated the Building Contract and claimed damages if payment was not made. In any event, as we have said, even if Shem did not abandon the works it does not follow as a matter of course that the respondent had unlawfully terminated the Building Contract.
33. We do not consider that there was an error in her Honour's conclusion that Shem had not established on the balance of probabilities that the respondent had unlawfully terminated the Building Contract.



Conclusion

34. For these reasons, the appeal must be dismissed. The appellant must pay the respondent's costs fixed in the amount of VT50,000 within 28 days.

DATED at Port Vila, this 14th day of August, 2025

BY THE COURT

.....
Hon. Justice Vincent Lunabek

