PENNINGTONS MANCHES COOPER

PERFORMANCE AND CANCELLATION OF CHARTERPARTIES

SUSPENSION / WITHDRAWAL / TERMINATION

Notices, damages and potential pitfalls

A. INTRODUCTION

The minds of owners and charterers alike are presently focused (as they should) on the Covid19 outbreak and how they can either utilise existing clauses or put together new clauses dealing with Covid19 in an attempt to refuse to perform or get out of a charter or prevent their contractual counterparty from doing so.

Penningtons Manches Cooper has already issued a number of articles and circulars (as well as a contractual tool kit) in respect of the effect of Covid19, the business interruption aspects of it as well as the way forward.

But what happens in circumstances where an existing contract is no longer desirable (or indeed financially viable) and one of the contractual counterparties wishes to no longer be bound it, either because of, for example, the state of the market or because the other party are not performing their end of the deal, whether as a result of Covid19 or otherwise?

A number of other considerations will of course be relevant (amongst others, the parties' commercial relationships, the state of the market, the ability to enforce against the non-performing party) but the purpose of this article is to act as a reminder of the various options available to an owner and charterer in the context of refusing to perform or getting out of a charterparty.

The above will be considered against a background of seeking to resolve disputes before they even arise, with a view to limiting (to the extent feasible) the costs and delays incurred where the parties engage in arbitration/ litigation proceedings.

B. SUSPENSION OF SERVICE

Suspension of service is only a right expressly afforded by the contract; that is, it requires an express provision in the charter in order to exist [1]. As such, a mere failure by the charterer to pay hire does not entitle the owner to suspend the services of the vessel temporarily [2].

Unless the charterparty provides otherwise, there is no need for the owner to give notice of his intention to suspend performance before doing so [3] and hire continues to accrue during temporary suspension of service.

Indeed, the charterer may have to indemnify the owner for the consequences of the suspension, including (depending on the clause) in respect of liability to third parties.

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[1] See, for example, clause 11(a) of NYPE 1993, clause 11(c) of NYPE 2015, clause 8.4 of BPTime 3, clause 8(b) of GenTime, clause 10(e) of SupplyTime 1989

[2] ***The Agios Giorgis*** **[1976] 2 Lloyd's Rep. 192** at 202, ***The Aegnoussiotis*** **[1977] 1 Lloyd's Rep 268** at 276, ***The Mihalios Xilas*** **[1978] 2 Lloyd's Rep 186** at 191.

[3] ***The Greatship Dhriti*** **[2012] EWHC 3468 (Comm)**

C. WITHDRAWAL

The right of an owner to withdraw his vessel from the charter service is a separate and different remedy to suspension and termination.

It is not a temporary remedy but a permanent one and causes the charterparty to be cancelled.

Like suspension, withdrawal is a contractual right [4].

An owner that wishes to withdraw is not required to prove deliberate non-performance or negligence on the part of the charterer. However, hire must be due [5].

A notice of withdrawal is normally required in order to withdraw. The notice:

- need not have a particular form of words [6]
- cannot be conditional
- must contain an unequivocal statement by the owner that he is exercising his right to withdraw [7]
- must comply with any anti-technicality clause in the charterparty (e.g. giving the charterer 48 or 72 hours to make full payment)
- must be given within a reasonable time after the default [8].

If the charterer has made deductions, the owner will have a reasonable time to consider whether such deductions were lawful or wrongful.

- In ***The Mihalios Xilas*** [9] the court held that 5 days to consider the deductions was reasonable, otherwise the owners may be taken to have waived their right to withdraw the vessel.
- The reasonableness of a 5-day period of consideration was confirmed in ***The Fortune Plum*** [10].
- The question of what amounts to a "reasonable" time depends on the particular facts of the case.

A mere late payment of hire does not cure a charterer's default and the owner can still withdraw [11].

However, acceptance by the owner of a late payment without protest and without reservation will normally amount to a waiver of the owner's right to withdraw [12]. The owner has the choice either to accept the late payment or to give it back.

Finally, the owner may not both withdraw the vessel and accept an advance payment of hire [13].

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[4] See clause 5 of NYPE 1946 and clause 9 of ShellTime 4.
[5] Unless provided otherwise, a charterer normally has until midnight on the due date to make payment.
[6] ***The Aegnousiotis*** **[1977] 1 LLR 268**
[7] ***The Georgios C*** **[1971] 1 LLR 7**
[8] ***The Laconia*** **[1977] AC 850**
[9] **[1978] 2 LLR 397**
[10] **[2013] EWHC 1355 (Comm)**
[11] *Ibid*
[12] ***The Brimnes*** **[1974] 2 LLR 241**
[13] However, the decision in ***The Brimnes*** indicates that the owner can retain hire as security for cross-claims without the court inferring a common intention of the parties to enter a fresh agreement on the same terms, or treating the owner's withdrawal as if it had not been made.

Remedies for withdrawal

The owner will only be entitled to hire up to the date of withdrawal, rather than damages for any losses he may have for the rest of the charterparty period [14].

The owner may seek damages for the remainder of the charter period only if the charterer's conduct also amounted to a repudiatory breach of the charter [15].

If the vessel had cargo on board and continues with the voyage, the owner will normally also be allowed to claim expenses from the charterers on a quantum meruit basis [16], although the position has yet to be properly judicially determined.

Following withdrawal, the owner will be a non-contractual bailee of the cargo and will be entitled to remuneration for the use of his vessel in any event [17].

Opportunities / risks of withdrawal

If the market is rising, an owner may wish to find reasons to withdraw. However, if the charterer is later found to have properly exercised a contractual or equitable right to make deductions from hire, the owner may be found to have unlawfully withdrawn.

D. TERMINATION

A party will be in repudiatory breach of a charter if it *"shows an intention no longer to be bound by the charter or an inability to perform such that the threatened non-performance would deprive* [the innocent party] *of substantially the whole benefit of the charter"* [18].

Damages for repudiatory breach

According to the "minimum performance rule", where the contract allows for alternative methods of performance by the guilty party, damages are to be calculated by reference to the minimum level of performance consistent with the terms of the contract, that is, the performance which is *"least burdensome"* to the guilty party [19].

In assessing damages, the court can take into account facts that became known following the breach [20].

The availability of an available market is important in measuring an innocent party's loss. An available market is defined as a market on which the vessel could be re-chartered for the balance of the charter period on terms (other than the hire rate) generally similar / equivalent to those of the repudiated charter.

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[14] ***Wehner v Dene SS Co* [1905] 2 KB 92**
[15] ***Leslie Shipping Co v Welstead* [1921] 3 KB 420**
[16] ***London Arbitration 12/11***
[17] ***The Kos* [2012] UKSC 17**
[18] ***The Afovos* [1983] 1 WLR 195** at 202; see also ***The Gregos* [1995] 1 Lloyd's Rep 1**
[19] ***Withers v General Theatre Corp Ltd* [1933] 2 KB 536**, ***Lavarack v Woods* [1967] 1 QB 278** at 294, ***Abrahams v Reiach (Herbert) Ltd* [1922] 1 KB 477**
[20] In ***The Golden Victory* [2007] 2 Lloyd's Rep. 164 (H.L.)** a war incident (subsequent to the termination) which under the charter would have brought it to an end was taken into account.

In particular:

- **Where an available market exists:**

  - The measure of the innocent party's loss will be the difference between the market rate and the charterparty rate of hire for the remainder of the charter.
  - This measure of loss applies irrespective of what the innocent party did in fact do following the termination.
  - The actual earnings of the vessel post-termination are not taken into account [21].

- **Where there is no available market**

  - Calculating the measure of loss becomes a difficult exercise.
  - The exercise involves an assessment of the actual losses suffered by the owner (on the basis that the charterparty had been performed) to the date of the relevant assessment and then a projection of future losses [22].
  - A charterer can challenge whether the owner properly mitigated his losses every time he chartered the vessel.
  - Deductions will be applicable in respect of:

    - commissions that would have been payable in any event;
    - off-hire days (based on, amongst other things, the vessel's previous off-hire record);
    - a discount for accelerated receipt [23];
    - a discount for catastrophic contingencies (e.g. total loss, bankruptcy etc) [24].

[21] ***The Elena D'Amico*** **[1980] 1 Lloyd's Rep. 75**, reconfirmed in ***The New Flamenco*** **[2017] UKSC 43** where a subsequent sale of the vessel at a profit was held to be irrelevant.
[22] ***The Kildare*** **[2011] 2 LLR 360**, ***The Wren*** **[2011] 2 LLR 370**
[23] In ***The Kildare*** **[2011] 2 LLR 360** a discount of 1.5% for accelerated receipt was found to be reasonable.
[24] In ***The Kildare*** **[2011] 2 LLR 360** a discount of 1.5% for catastrophic contingencies was found to be reasonable.

Examples of repudiatory breach

- **Failure to pay hire:**

Failure to pay hire is not a condition but an innominate term [25]. Following some doubt that was initially cast on this characterisation [26], the position has now been confirmed in a case that this firm [27] was involved [28].

Failure to pay hire is a breach that gives rise to damages only, unless the breach is sufficiently serious so as to go to the root of the contract, in which case it constitutes a repudiatory breach entitling the innocent party to terminate the charter.

A rule of thumb is a failure to pay 3 hires in a row [29].

In ***The Pro Victor*** [30] it was held that:

- When ascertaining whether a party has renounced a contract, the question to be considered is whether, by its word or conduct, the party has evinced an intention not to perform the contract, which a reasonable person in the position of the other party would regard as clear and absolute.
- The question is to be judged at the time when the contract was terminated, having regard to all the circumstances including the history of the contractual relationship.
- This will include repeated failure to respond clearly, or at all, to reasonable questions from the owners about when the charterers expect to resume payment of hire.

It is of course open to the parties to agree that payment of hire is a condition of the charter. In ***The Mahakan*** [31] the charter provided that punctual payment of hire "shall be of the essence". Eder J held that this made payment of hire a condition.

- **Duration of the charterparty / early-late redelivery**

In order to see whether a vessel is redelivered early or late, the minimum or maximum duration of the charter needs to be identified.

In the absence of an agreement to the contrary, the date of redelivery should be considered as an approximate one [32], although it will all depend on the particular clause.

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[25] ***The Brimnes*** **[1972] 2 LLR 465**
[26] ***The Astra*** **[2013] EWHC 865** per Flaux J.
[27] As Thomas Cooper, prior to the merger that led to the formation of Penningtons Manches Cooper.
[28] ***Grand China Logistics Holding (Group) Co Ltd v Spar Shipping*** **AS [2016] EWCA Civ 982**)
[29] ***London Arbitration 17/02***
[30] **[2010] 2 Lloyd's Rep. 158**
[31] **[2011] EWHC 2917**
[32] ***The Peonia*** **[1991] 1 Lloyd's Rep 100**

Most clauses nowadays provide for a specific minimum / maximum duration of a charter on "about" terms. There is no single rigid rule as to what "about" may refer to and it all depends on the clause, the overall circumstances and the length of the charter in hand. For example:

- In ***The Democritos*** [33], a ship was chartered for "about 4 to 6 months". The arbitrators allowed a margin of 5 days of overrun.
- In ***Meyer v Sanderson*** [34], a ship was chartered for "about 6 months". The ship was redelivered 12 days after the end of the sixth months. Atkin, J. held that this was beyond the tolerance allowed by "about".

- **Early redelivery**

Provided that the duration is set out in an express provision, early redelivery constitutes a repudiatory breach of the charterparty [35].

An owner has the option to:

- accept such breach which would bring the contract to an end; or
- refuse redelivery and continue to claim hire.

It is trite law that an owner may refuse a charterer's early redelivery if he has a "*legitimate interest*" in continuing the charterparty **[36]**. In practice, only in exceptional circumstances will an owner be seen as not having a "legitimate interest" to continue performing the charterparty [37].

As seen above, the measure of the owner's loss:

- where there is a market, is the difference between the charter rate and the current market rate [38].
- where there is no market, is the owner's actual loss [39] and consideration should be had of:
  - The owner's failure to mitigate his loss; and
  - The potential revival of the market subsequently.

[33] **[1976] 2 Lloyd's Rep. 149**
[34] **(1916) 32 TLR 428**
[35] ***The Aquafaith*** **[2012] EWHC 1077**
[36] In ***The Aquafaith*** **[2012] EWHC 1077** an owner was found to have had a legitimate interest to refuse redelivery where the charterer purported to redeliver 94 days before the minimum duration had expired in a 5-year charter.
[37] To be noted that in ***The Puerto Buitrago*** **[1976] 1 LLR 250,** the owner was found to not have a legitimate interest to continue a demise charter.
[38] ***The Elena D'Amico*** **[1980] 1 Lloyd's Rep. 75**
[39] ***The Wren*** **[2011] EWHC 1819**

- **Late redelivery**

  The obligation to redeliver at the end of the charter period is an innominate term, so delay in redelivery will not (of its own) justify termination of the charter [40].

  If the owner proceeds on a voyage, completion of which is expected to mean that the vessel will be redelivered late (on reservation of his rights), hire at the charterparty rate will be payable up to the end of the charter period and at the then market rate for the excess period thereafter [41]; that is, the owner's measure of loss is the difference between what the owner was paid for the overrun period and what he would have been paid if he had employed the vessel in the market.

  In line with the "minimum performance rule" (referred to above), damages would be calculated from the latest possible redelivery time.

  In most circumstances, an owner's damages for late redelivery will be restricted to the normal measure (i.e. the difference between charter and market rates for the overrun).

  In order for a different type of loss to be recovered, foreseeability of the loss is not sufficient and such loss will be recoverable if it:

  - is held to be within the reasonable contemplation of the parties;
  - is not too remote;
  - has been assumed as a responsibility from the charterer; alternatively, if the risk for the additional loss was specifically drawn to the charterer's attention and the charterer insisted on an illegitimate last voyage order [42].

A note on notices of redelivery

Approximate / definite notices of redelivery are given by the charterer to the owner as an indication of redelivery so that the owner can start looking into the future employment of the vessel.

Although it is trite law that the giving of a notice of redelivery is not a condition precedent to an effective redelivery (which is a matter of fact), where the charterer fails to follow the charterparty provisions concerning notices, the owner will be entitled to recover damages.

In ***The Great Creation*** [43] a 20-day approximate notice of redelivery was given on 19 April, just 6 days prior to the vessel being redelivered (on 13 April), the question arose of whether the charterer was in breach:

- because he redelivered only 6 days after giving a 20-day approximate notice; or

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[40] ***The Gregos*** **[1995] 1 Lloyd's Rep. 1**
[41] ***The Dione*** **[1975] 1 Lloyd's Rep 115**
[42] ***The Achilleas*** **[2008] 2 Lloyd's Rep 275, *The Sylvia* [2010] EWHC 542**
[43] **[2014] EWHC 3978**

- because he did not give the required notice approximately 20 days before the actual date of redelivery.

Cooke J held that it was the former, so the owner was able to recover hire for the balance of the approximate (20-day) period (allowing a 2-day margin in light of the notice being an "approximate" one) with credit to be given for any earnings achieved by the owner in mitigation.

Opportunities / risks of charter termination

It is worth for any party, if anything in the interest of certainty, to seek to include language in the charterparty dealing expressly with repudiatory breach, for example:

- making time of the essence
- making a term expressly a condition

However, there are risks involved too. In particular:

- It is a generally precarious situation to be without receipt of hire from the charterer and there may not be certainty as to whether a charterer's failure to pay hire gives rise to a successful claim for damages for repudiatory breach of contract.
- There is always the risk of getting it wrong which will in itself constitute a repudiatory breach which the other party may seek to accept and itself bring the charter to an end.

It would be best practice for a party to:

- Allow sufficient time before terminating;
- Send messages asking the other party to confirm if / when he is going to perform (e.g. make payment of outstanding hire);
- Continue to reserve its position;
- Involve lawyers to assist.

E. WITHDRAWAL OR TERMINATION?

In a falling market, the owner will most likely want to keep the charterer tied in to the charterparty for as long as possible and the decision to withdraw the vessel from the charterer's service will also depend on whether there is any chance of recovery from the charterer [44].

In a rising market, the owner will withdraw at the first available opportunity, let alone if the charterer's conduct can be stated to also give rise to a repudiatory breach (which would entitle the owner to damages referable to the remainder of the charter period).

[44] Indeed, the ability to enforce against a party is a crucial factor to consider and it has been seen all too often for a charterer to "disappear" and re-emerge under a new name / corporate structure.

There may also be issues in relation to the cargo on board, and there may be no advantage to the owner in withdrawing the vessel before the cargo is delivered, given the owner's (contractual and/or physical) carrier's duties.

Another factor to take into account is whether the vessel is still trading. A relevant consideration is that it is much easier for an owner to obtain security if the vessel is still trading by way of exercising liens (e.g. a lien over her cargo, suspending performance, refusing to discharge the cargo unless and until hire is paid or a "lien" over any freight/sub-freight or hire / sub-hire by requesting that any such freight/sub-freight hire / sub-hire be paid to the owner directly by the parties down the chain). If the vessel is simply sitting idle in ballast, no assets of the charterer can be found and/or the charterer is not a substantial trading entity, it is probably better for the owner simply to cut its losses and withdraw the vessel.

There is also the question of whether there is an available market. If not, the owner may be better off holding out for repudiatory breach as opposed to withdrawing.

F. CONCLUSION – COMMERCIAL CONSIDERATIONS

When a charterer fails to comply with its obligations under the charterparty regarding re-delivery of the vessel or payment of hire, the owner generally has the simple and quick option of withdrawal which will normally result in no damages being claimable, or the lengthier and less certain option of waiting until the charterer is in repudiatory breach before terminating the charter and claiming damages. The hire market should be taken into account as should also the general financial well-being of the charterer. The option of suspension of service, where available, often leads to a quick resolution of disputes that could otherwise lead to the charter being cancelled.

The above points will hardly sound new to an owner or a charterer; however, it is always important to keep the legal position in mind, together with the usual commercial considerations, in considering one's position when it comes to performance and/or cancelling of a charter.

Overall, when it comes to the performance or cancellation of a charter, a party should be extremely cautious and ensure that they have examined their options before acting. As a general rule, a party should negotiate wherever possible and not rush into decisions. A risk assessment should always be undertaken before taking big steps.

Many of the above considerations will bring back vivid memories to those in the shipping community that experienced the post-September 2008 era. Indeed, the impact that the Covid19 outbreak may have on shipping in 2020 may not be dissimilar to the post-Lehman Brothers era where the market collapsed creating havoc but careful business planning and appropriate legal advice can still secure the best possible outcome in the circumstances.

FIND OUT MORE

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