When An Innocent Party Is Disallowed From Rejecting Repudiation (In The Context Of Time Charters)

Introduction

It is a basic principle that, when faced with the repudiation of a contract, the innocent party can choose to accept the repudiation and sue for damages, or reject the repudiation and continue the contract. However, the innocent party’s right to reject repudiation is not absolute, and is subject to the concept of ‘legitimate interest’.

Nonetheless, English case law in the context of repudiating long-term time charters has consistently adopted a pro-Owner/Plaintiff approach. This approach is exemplified by the very recent English High Court decision Isabella Shipowner SA v Shagang Shipping Co Ltd ("The Aquafait") [2012] EWHC 1077 (Comm) where the High Court examined existing authorities and affirmed that, save for exceptional circumstances, it is generally prepared to allow Owners to affirm continuation of the Charter and claim for hire in the face of Charterers’ default.

The choice to continue to with the charterparty contract is important. If the Plaintiff Owners continue with the contract, they can simply sue for hire due as they fall due. If the contract is terminated, the Plaintiff Owners have to sue for damages from that point onwards, and their damages is calculated based on the difference between the market price and contract price. There may be circumstances where it is more attractive for the Plaintiff Owners to continue with the contract, for example it may be difficult to prove the difference between market price and contract price and where a contract is terminated, issues of mitigation will arise.

The Decision in Summary

The dispute in The Aquafait concerned the scope of the principle in White and Carter (Councils) Limited v McGregor [1962] AC 413 ("White and Carter"), where Lord Reid set out two exceptional circumstances where the Plaintiff shipowner is limited to a remedy in
damages rather than to continue the contract: first, where the Defendant’s co-operation is required before the Plaintiff can complete performance, and second, where the Plaintiff has no legitimate interest, financial or otherwise, in performing the contract rather than claiming damages.

Therefore, where the Defendant’s co-operation is required for the Plaintiff Owners’ performance of their contractual obligations, the Plaintiff Owners will not be able to insist on continuing the contract. Instead the Plaintiff Owners is compelled to end the contract, and to sue for damages. Where no such co-operation is required, the Plaintiffs’ claim can also be limited to one of damages if he has no ‘legitimate interest’ in rejecting repudiation and affirming the contract.

White and Carter is not a charterparty case, it was about placement of advertisement on Council litter bins. The Aquafait is but one of the many charterparty disputes which turned on an interpretation of the two exceptions enunciated by Lord Reid. Even in the context of early redelivery of the vessel for time charters, the facts of the case are not novel.

However, this case is distinctive for several reasons. First, in The Aquafait, Cooke J explicitly separates time charter cases from the demise charter cases because of the degree of co-operation between Owners and Charterers in both cases. While it can be said that the Owners’ performance of their contractual obligations for a time charter is not contingent on co-operation from the Charterers, the same cannot be said for the case of demise charters. Second, it has been said that Cooke J’s interpretation of the previous authorities and restatement of the test for ‘legitimate interest’ has widened the scope of the White and Carter principle, thereby imposing a heavier burden on the Charterers before the Plaintiff Owners’ claim can be limited to one of damages only.

The Co-Operation Requirement

The first exception laid down in White and Carter is that the innocent party’s right to affirm the contract will be restricted where he is incapable of fulfilling his contractual obligations without the co-operation of the contract breaker.

In the general context of time charters, The Aquafait confirms that that Owners do not need the co-operation of the Charterers to earn the hire in question. Therefore, cases involving the anticipatory breach of contract due to the early redelivery of the time chartered vessel are unlikely to fail on this point.
Accordingly, what constitutes a ‘legitimate interest’ to affirm the contract and claim for hire is likely to be of more interest to shipowners.

‘Legitimate Interest’

The second exception laid down by Lord Reid in White and Carter is that the contract-breaker bears the burden of showing that the innocent party has no ‘legitimate interest’ in affirming the contract. There is no authority defining exactly what a ‘legitimate interest’ in the context of time charters would be. However, The Aquafairth and the authorities considered do confirm that a lack of ‘legitimate interest’ will only be found in a handful of extraordinary cases, where damages would be an adequate remedy, and keeping the contract alive would be “wholly unreasonable”, “extremely unreasonable” or “perverse”. Some of the factors which were considered as relevant to determining the existence of a ‘legitimate interest’ are set out below.

First, whether the Owner’s conduct is in fact ‘wholly unreasonable’ is likely to be judged in a commercial light. Cases such as The Alaskan Trader and The Dynamic show that where the appointed commercial arbitrator finds that the Owners do not have a legitimate interest in maintaining the charter instead of suing for damages, the Court will only interfere with his decision if he has made an ostensible error of law, as in The Aquafairth. Therefore, where it can be shown that Owners have no financial interest in maintaining the charter, this uncommercial decision would necessarily be prima facie evidence of unreasonable behaviour to the arbitrator. However, this would be taken in light of all other evidence made available to the arbitrator.

Second, the financial viability of the contract-breaking Charterers was considered a relevant factor in The Aquafairth. The judge held that the regular advance payment of charter-hire functioned as a security to the Owners for the amounts due to them. It reduces the possibility of the Charterers directing their limited funds to meet other financial obligations and putting off payment to the Owners till the end of the relevant period before seeking to pay the amount due in ‘damages’, subject to the Owners’ fulfilment of their duty to mitigate. Furthermore, he also considered that the Charterers might have become insolvent by the end of the charterparty. Thus, the more financially unstable the Charterers, the more it would be justified for the Owners to insist on claiming for hire, as opposed to damages.

Third, the availability of alternative employment is also a relevant factor for consideration. This factor is especially pertinent where market conditions for the period are difficult such
that it is not possible to obtain alternative employment. In such cases, there is no reason for foisting the unnecessary burden of obtaining alternative employment on the Owners as both Owners and Charterers have the same ability to sub-let the vessel in the market.

Fourth, relevant bank requirements are also relevant. However, it is probable that for this to be a legitimate factor, the contract-breaker must have notice of the bank’s involvement as a third party. This factor was explained in The Odenfeld as being relevant because one way in which Owners can pay off outstanding loans to the bank is by assigning the charter hire in a long-term charterparty to the bank. This was the case in The Odenfeld, but the Charterers in that case had notice of the agreement and assignment of charter hire.

Lastly, the difficulty in assessing damages was also pointed out as being a relevant factor in The Odenfeld. In practice, where the charter still has many years to run, variables such as fluctuations in the market rate and performance of the vessel often make it very difficult to assess damages. It was noted that the position of the shipowner when he is entitled to damages and when he is entitled to hire is very different. Thus, where damages are difficult to assess, this factor would likely weigh in favour of a claim for hire.

The Singapore Context

The rule in White and Carter has not been followed in any Singapore decision. In fact, it only received consideration in one High Court case in 1999 involving a developer and purchaser of a property. Even though White and Carter was not applicable on the facts, the Court’s hesitance in accepting the application of the principle was evident.

However, both White and Carter and The Aquafait are still persuasive English authorities, albeit the burden of proof which the Charterers must discharge before these principles will apply will arguably be heavier. In the absence of a highly persuasive factual matrix, it is unlikely that the Courts will allow the innocent party’s right to be limited as a result of the other party’s breach of contract. Furthermore, this would introduce uncertainty into the area of commercial law where certainty is paramount.

Concluding Words

The case of The Aquafait does not set down any new legal doctrines. It does, however, confirm the following: (1) that time charters are unlike ordinary service contracts and that the principle of White and Carter may apply in the context of time charters; and (2) that the law leans in favour of protecting the innocent party’s right of choosing the remedies
available to him in the event of a breach of contract. Thus, in the absence of extraordinary facts, it will be unlikely for contract-breaking charterers to prove that the circumstances warrant the finding of no ‘legitimate interest’ which would justify limiting the innocent party’s contractual right to affirm the charter.

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