

Update

What “delay” counts towards cancellation?

With tumbling oil prices and projects being mothballed or cancelled, knock-on effects are to be expected. Offshore contractors with vessels or rigs under construction in yards are less likely to be tolerant of construction delays than they would otherwise be, and may consider cancellation. The recent Commercial Court decision in *Zhoushan Jinhaiwan Shipyard Co Ltd v Golden Exquisite Inc & Others* [2014] EWHC 4050 provides a timely look at cancellation rights in the context of delay.

Facts

In *Zhoushan*, the buyer had purported to exercise its right to cancel under a series of materially identical shipbuilding contracts, on account of periods of accumulated delay in delivery. Article VIII.3 of the contract permitted the buyer to cancel if the total accumulated delay exceeded a certain number of days, but certain categories of delay could not be included in the calculation. One of the excluded categories was for delays “...due to default in performance by the buyer”. The court recognised that, in each case, the cancellation of the contract by the buyer followed a similar pattern:

- The delivery of the vessel was delayed beyond the “delivery date” (as defined in Article VII of the contract)
- The buyer gave notice of cancellation of the contract on a date which was more than 270 days after the delivery date (being the relevant period of accumulated delay giving rise to a right to cancel under Article III of the contract)
- Before such notice of cancellation was given, the yard had not given notice to the buyer of any delay which the yard claimed had been caused by a breach of contract by the buyer (or any other cause for which the yard was not responsible)

- After notice of cancellation had been given, however, the yard did make such a claim and alleged that breaches of contract by the buyer had resulted in delays in the construction of the vessel totalling, variously, not less than 90 days or 100 days depending on the case

The yard argued that the cancellation was wrongful because part of the delay was, on its case, caused by the buyer’s own breach of the contract, namely that during construction, the buyer had breached its obligations relating to the inspection of the ship by the buyer’s supervisor (under Article IV). Essentially, the yard complained that the supervisor worked too slowly and sought to impose unreasonable requirements on the build.

If the cancellations were lawful, the buyer would be entitled, under Article X, to a refund of all instalments of the contract price which had been paid before the cancellation, together (potentially) with interest on those instalments, from the date of payment to the date of repayment. If the cancellations were unlawful, the yard would be entitled to keep the instalments and re-sell the vessels, crediting the buyer only with the balance of the proceeds of any such sale, after the yard has recouped its expenses.

Further information

If you would like further information on any of the issues raised in this update, please do not hesitate to speak to your usual Clyde & Co contact or the authors of this update:



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Decision

The court (Leggatt J) held, on an appeal from previous arbitral awards, that the exception under Article VIII.3 for delays “*due to default in performance by the buyer*” had to be understood, in context and as a matter of contractual interpretation, as a reference only to those types of default by the buyer in respect of which the contract expressly provided for an extension of the delivery date. (An example of a specific provision to this effect was Article XI of the contract, which covered (amongst other things) failure by the buyer to make payments on time, and had the effect of postponing the delivery date so long as that default continued).

The court considered that the overall contractual scheme indicated that breaches of the kind of which the yard complained were not ones which were intended to entitle the yard to make late delivery, whatever other remedies the yard might have. In coming to this view, the court observed that for other breaches by the buyer, the contract provided for a formal extension of the delivery date, and required notice by the yard of its intention to rely upon such breaches to extend this date, but this was not so in relation to breach of Article IV.

The court concluded that the parties were unlikely to have intended for the yard to be able to rely on a period of delay without it having to give notice of this to the buyer, and observed that this interpretation would avoid an undesirable situation in which the parties might be unsure, at any given point, whether the contract could or could not properly be cancelled. The yard’s interpretation, if accepted, would cut across this scheme. As the judge put it:

“The parties could no doubt have made a contract which left them each to perform their own calculation and then argue about the causes of delay after a cancellation has occurred. However, they have tried to avoid such an anarchic situation. Instead, they have adopted a scheme which provides for notices to be given and agreement reached, or

any dispute resolved by arbitration if necessary, whenever an event occurs which the Yard wishes to say justifies an extension of the time for delivery.”

It followed that the shipyard’s arguments had failed, and the court upheld the findings under the arbitration awards to the effect that the buyer’s cancellation of the contracts was justified, and the yard was obliged to repay the full amount of the instalments advanced by the buyer.

Comment

Although the decision turned on the particular wording of the contract in question, it may provide some guidance as to the interpretation of other shipbuilding contracts, particularly those, as appears to be the case here, based on the widely used SAJ (Shipbuilders’ Association of Japan) form. Some key points to note are:

- Standard provisions relating to termination and delay are frequently subject to extensive amendment by the parties. This decision highlights the potential significance of any ambiguity around which categories of delay do, and which do not, count towards the accumulated period permitting the buyer to cancel
- The decision suggests that buyers should, perhaps, hesitate to take at face value assertions by a yard that particular periods of delay are to be disregarded for the purposes of establishing buyers’ cancellation rights. It would seem that the court/tribunal may be slow to accept such arguments unless the wording is clear, particularly if the result would be that the yard would not have to give any notice of its intention to rely on the relevant delay
- In a similar vein, the case recognises the importance of contractual notice regimes where they appear. The court showed hostility to interpretations of the contract that would allow the yard to exclude periods of delay for the purposes of calculating buyer’s cancellation rights without first giving notice of its intention, and only after the buyer had purported to terminate for excessive delay