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Update

Effect of non-payment of hire: After *The Astra* comes another twist in the tale

On 18 April 2013, Flaux J handed down a judgment in *Kuwait Rocks Co v AMN Bulkcarriers Inc. (The Astra)* that surprised many in the shipping community with its analysis that a charterers' failure to pay hire amounted to a breach of a condition, thereby entitling an owner not only to cancel the charter and escape future performance but also to claim damages for the unperformed part. The recent judgment of Popplewell J in *Spar Shipping AS v Grand China Logistics Holding (Group) Co., Ltd*, handed down on 18 March 2015, challenges that conclusion in a thorough and significant review of this important area of law.

Background

Clearly a refusal or failure to pay hire according to the terms of the charter, or a late payment, amounts to a breach of contract. The difficulty comes in determining whether that breach gives rise to a right to terminate the contract and claim damages. Although in most cases the charterparty will contain provisions that grant the owner a contractual right to withdraw the vessel in the event of non-payment, this will generally only provide the owner with the right to claim hire that is payable and earned up to that point. For the owner to establish a claim for damages for loss of the value of the rest of the contract, or the *"bargain"* - usually the difference between the market rate of hire and the charterparty rate for the remaining period of the charter – there must either be a breach of condition or some other breach that is deemed to be sufficiently serious to amount to a repudiation or renunciation of the charter.

If the payment provisions in the charterparty (for example, Clause 5 of the NYPE 1946 form) do not amount to a condition, then in practice the owner would need to show that the breach was sufficient to amount to an unambiguous representation that the charterers would not or could not perform their obligations under the charter. This will not always be easy for an owner and so the legal and commercial significance of whether or not the payment provisions are a condition of the contract entitling termination for even the slightest of breaches, together with a right to claim damages for the unexpired period, becomes immediately apparent.

The generally accepted position prior to *The Astra* was that although the owner may often have had a contractual right to withdraw the vessel for non-payment of hire, it would also have been necessary to establish a repudiatory breach by the charterers if the owner was also to recover additional damages. In other words, the payment provisions were not treated as a contractual condition but merely gave the owner a right to stop further performance in the event of unpaid hire, and claim the debt.

However, although it is correct to describe this as the *"generally accepted position"*, the issue had not been conclusively settled. Perhaps the clearest statement on the subject was provided in *The Brimnes* [1972] where Brandon J, considering whether Clause 5 of NYPE 1946 amounted to a condition, said:

> *"….. I have reached the conclusion that there is nothing in Clause 5 which shows clearly that the parties intended the obligation to pay hire punctually to be an essential term of the contract, as distinct from being a term for breach of which an express right to withdraw was given."*

Although this decision was approved in the Court of Appeal, in other cases a contrary view had been expressed, albeit in obiter comments. The authors of *Time Charters* perhaps provide the best summary of the pre-*Astra* position when noting:

> *"Despite these dicta, it is thought the better view is that the obligation to pay hire is by nature an intermediate term, so damages for the loss of the charter are recoverable only where the failure to pay hire by the due date can be shown to be repudiatory…. It may be that the judicial remarks [contrary to this view] should not be understood as meaning that Clause 5 [of NYPE] is a condition, but only that its draftsman, by adding an option to withdraw to the obligation to pay hire, had given to that obligation one characteristic of a condition, namely that any breach gives a right of termination. But uncertainty will remain until the House of Lords has shed more light on this important question."*

The Astra

It was against this background that Mr Justice Flaux came to examine the issue in *The Astra* and, contrary to the view of the Tribunal in that case and also that expressed in *Time Charters*, concluded that the obligation to make punctual payment of hire was a condition.

The Judge's view was:

- The fact that Clause 5 gave a right to withdraw the vessel was a strong indication that it was intended that a failure to pay hire promptly would go to the root of the contract
- As time was made of the essence, it was consistent with the requirement being a condition
- *The Brimnes* could be distinguished as it was a decision where there was no anti-technicality clause making time of the essence – however, the Judge stated that he would still have refused to follow the decision due to obiter dicta in subsequent decisions, and the fact that one of the authorities relied on in *The Brimnes* had been overruled; and, perhaps most importantly
- The importance to businessmen of certainty in commercial transactions – an owner would need to know whether he could withdraw the vessel and claim damages or whether he should persevere with his inconsistently performing charterers

Spar Shipping AS v Grand China Logistics

As in *The Astra*, the facts of the case before Popplewell J were such that the *"condition"* point in relation to the payment of hire proved not to be decisive because the charterers' conduct was found to be repudiatory. Nevertheless, the issue was fully argued and considered in great detail by the Judge.

The dispute arose in relation to three long term time charterparties on amended NYPE 1993 forms between Spar and CGL. Difficulties arose in relation to the payment of hire in respect of all three vessels, and eventually Spar withdrew the vessels and terminated the charterparties. After the charterers went into liquidation, claims were brought under guarantees that had been issued by charterers' parent company for the balance of unpaid hire before termination. In respect of the three vessels, this element of the claim totalled just over USD 561,000.

In addition, Spar claimed under the guarantees for damages for loss of bargain in respect of the unexpired term of the charters. The market for the vessels had deteriorated significantly with the result that this element of the claim, even allowing for owners' efforts to employ the vessels in mitigation totalled in excess of USD 23 million.

A significant part of the judgment dealt with issues relating to the validity of the parent company guarantees and whether (irrespective of the *"condition"* point) the charterers' failures to pay hire were sufficiently serious to amount to a renunciation of the charterparties. Spar were successful on both these issues which, in itself, was enough to ensure their entitlement to recover the full amounts claimed under the guarantees. However, just as in *The Astra*, and given the obvious significance of the point, the Judge embarked upon a detailed analysis of whether the failure to pay hire also amounted to a breach of condition.

In doing so, Popplewell J had the benefit of considering the extensive commentary within the shipping community following *The Astra* decision which indicated, as the Judge noted, *"that Flaux J's decision has not been universally welcomed or treated as settling the position."*

Popplewell J also had the benefit of being referred to the decision in *Financings Ltd v Baldock* [1963] which, it seems, may not have been considered in argument before Flaux J. This Court of Appeal decision concerning a hire purchase contract provided significant support for the

contention that a contractual right of termination conferred for any breach of a term, however trivial (for example, the right of withdrawal for non-payment of hire under NYPE 1993) could not of itself be relied on to provide a conclusive answer as to whether the term should be treated as a condition. The *"critical question"* as Popplewell J saw it remained as follows:

> *"'[W]hether the contractual right to terminate by withdrawal of the vessel for non-payment of hire conferred by clause 11 is to be construed as indicating that the parties intended that payment of hire was a condition, or whether it is to be construed simply as an option to cancel in circumstances where payment of hire is an innominate term and a breach will not give rise to a right to damages in the absence of a repudiatory breach or renunciation."*

Popplewell J was also unpersuaded by other key arguments relied upon by Flaux J in support of the contention that failure to pay hire amounted to a breach of condition. In particular, the Judge did not accept that considerations of commercial certainty pointed in that direction. The Judge noted that commercial certainty, though desirable, *"must be counterbalanced by the need not to impose liability for a trivial breach in undeserving cases"*. Furthermore, Popplewell J noted that a very considerable measure of certainty was provided anyway by the withdrawal clause because it provided an option to cancel. The additional question as to whether damages for loss of bargain could also be claimed undoubtedly raised issues of commercial risk. However, these were not unrealistic risks for the shipowner to bear in circumstances where it was not uncommon in the commercial world to rely on prompt payment in order to finance performance of a contract.

Popplewell J also did not feel that the existence of the anti-technicality clause was significant as it had been for Flaux J. Such a clause simply indicated that the strictness of the right to withdraw under the clause was to be tempered to avoid it being triggered by mere mishaps. Taken as a whole, the language of the clause was *"more naturally indicative of an option to cancel directed solely to future performance, not as something intended to impose new liabilities."*

It followed that Popplewell J's extensive review of the authorities and of the basis of Flaux J's conclusion in *The Astra* led him to reach a quite different conclusion, namely that the failure to pay hire in accordance with Clause 11 of NYPE 1993 did not amount to a breach of condition.

Comment

As in *The Astra*, the decision on the *"condition"* point in *Spar Shipping AS v Grand China Logistics* is, strictly speaking, obiter dicta, given that its determination did not affect the outcome of the case. However, given the detailed nature of both judgments and the arguably more complete review of the relevant authorities by Popplewell J, it must be considered highly unlikely that the Commercial Court or arbitration tribunals will now adopt a different approach to that of Popplewell J, at least until such time as the issue can be considered by the Court of Appeal.

So for now at least, the pre-*Astra* status quo has prevailed: although the owner may often have a contractual right to withdraw for non-payment of hire, it will remain necessary to establish a repudiatory breach or renunciation on the part of the charterers if the owner is also to be able to recover the often very substantial extra damages for loss of bargain.

Further information

If you would like further information on any issue raised in this update please contact:



Nick Austin
E: nick.austin@clydeco.com



Chris Moxon
E: chris.moxon@clydeco.com

Clyde & Co LLP
The St Botolph Building
138 Houndsditch
London EC3A 7AR

T: +44 (0)20 7876 5000
F: +44 (0)20 7876 5111

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