

THE “AQUAFAITH” – OWNERS’ ALTERNATIVE RIGHT TO REFUSE EARLY REDELIVERY

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In the recent High Court judgment in the *Aquafaith*¹, the Court considered the alternative remedy available to owners when charterers repudiate the charterparty by prematurely redelivering the vessel. The judgment is noteworthy as it illustrates that the general rule is that owners will be entitled to reject redelivery of the vessel by affirming the charterparty and claiming hire for the balance of the minimum period of the charterparty as opposed to accepting charterers’ repudiatory breach and claiming damages. In holding defaulting charterers to the contract, owners’ need not act reasonably.

Further, the judgment is a welcomed clarification of the two qualifications established by the House of Lords in *White and Carter*² on an innocent party’s otherwise unfettered right to affirm a contract and claim the contract price following repudiation of the contract by a counterparty. An innocent party’s otherwise unfettered right to affirm the contract is subject to: a) whether the innocent party is able to continue to perform the contract without the cooperation of the party in breach of the contract; and b) whether the innocent party has a legitimate interest, whether financial or otherwise, in continuing to perform the contract rather than accepting the repudiation and claiming damages.

Facts

The *Aquafaith* was chartered on amended NYPE terms for minimum 59 to maximum 61 months. The charterparty included a warranty “that the vessel will not be redelivered before the minimum period of 59 months”. The expiration of the agreed minimum period of 59 months was in the event 10 November 2011.

On 6 July 2011 the Charterers notified the Owners of their intention to redeliver the vessel on dropping the last outward sea pilot after completion of discharge operations in China. It was accepted that the Charterers’ notice constituted an anticipatory repudiatory breach of the charterparty. The vessel was eventually redelivered on 9 August 2011.

The Owners refused to accept redelivery of the vessel and sought to affirm the charterparty. Accordingly, the Owners commenced arbitration proceedings on 25 July 2011 seeking a partial final award declaring that the Owners were entitled to refuse redelivery and to affirm the charterparty and, as a result, that they were entitled to hire for the balance of the minimum period of the charterparty, being 94 days. The Charterers argued that the Owners were not

¹ *Isabella Shipowner Sa v Shagang Shipping Co Ltd* [2012] EWHC 1077 (Comm).

² [1961] UKHL 5 House of Lords

entitled to affirm the charterparty on the basis that the Owners could not continue to perform the contract without the Charterers' cooperation and that the Owners had no legitimate interest in performing the contract.

Arbitration award

The arbitrator found for the Charterers and held that the dispute fell outside the *White and Carter* general principle that the Owners had an unfettered right to affirm the contract on the basis that a time charterparty was a contract the continuing performance of which required charterers' cooperation, namely by way of provision of bunkers to the vessel.

In considering the second qualification of the Owners' otherwise unfettered right to affirm the contract, namely whether the Owners had a legitimate interest in the continued performance of the charterparty, the arbitrator asked whether an adequate remedy was to keep the vessel at the Charterers' service for the remaining three and a half months of the contract.

Having reviewed the judgments in the *Dynamic*³ and the *Alaskan Trader (No 2)*⁴, the arbitrator held that the Owners were in a position to accept the repudiation of the charterparty and mitigate losses by fixing the vessel on the spot market for the balance of the minimum period of the charterparty and to claim damages based on the difference between the charterparty hire rate and the vessel's earnings during the balance of the charter period. As the Owners could mitigate losses and claim damages, they had no legitimate interest in the performance of the contract and ought not to be allowed to saddle the Charterers with an additional burden without benefit to themselves. Accordingly, the Owners' claim failed on both the qualifications set out in *White and Carter*.

High Court judgment

The Owners appealed the arbitration award on two grounds. The first ground of the appeal was under section 69 of the Arbitration Act 1996 in that the arbitrator had erred in law. The question before the High Court was: "*Whether, as a matter of law, owners were entitled to refuse early redelivery of the Aquafaitth (the vessel) at Jintang on 9 August 2011 and affirm the charter, or whether they were bound in law to accept early re-delivery and merely entitled to sue for damages*". The second ground of appeal was serious irregularity pursuant to section 68 of the Arbitration Act, because the arbitrator had failed to give any, or any sufficient weight, to the Owners' submissions when deciding the issues that arose between the parties.

In considering the first ground of appeal, Mr Justice Cooke considered the principle set out in *White and Carter* and subsequent shipping authorities. He first considered the judgment in the *Puerto Buitrago*⁵, a Court of Appeal judgment, which considered the *White and Carter* principle in relation to redelivery of a vessel under a bareboat charter where the Court held

³ [2003] 2 Lloyd's Rep 693

⁴ [1983] 2 Lloyd's Rep 645

⁵ [1976] 1 Lloyd's Rep 250

that the case fell outside the *White and Carter* principle because a bareboat charter could not be performed without the charterers' cooperation and that the owners there had no legitimate interest in affirming the contract rather than seeking damages.

The Court went on to consider the judgment in the *Oldenfeld*⁶ where the Court accepted the generality of the *White and Carter* principle that owners had an otherwise unfettered right to elect to affirm the charter. The Court held that any fetter on an owners' right to affirm the contract would only apply in extreme cases where damages would be an adequate remedy and where an election to keep the contract alive would be wholly unreasonable. The Court further held that charterparties differed to general services contracts and could continue to be performed without the cooperation of a repudiating charterer. The Court, however, accepted that the passage of time might in itself alter the position because a continued insistence on performing the contract despite charterers' repudiation might in time become unrealistic, unreasonable and untenable.

Mr Justice Cooke then considered the judgment in the *Alaskan Trader* where the Court upheld the innocent party's unfettered right to elect to affirm the contract and found that while there may be some fetter it applies in extreme cases only.

Next, Mr Justice Cooke considered the judgment in *Stoczia v Latvian Shipping*⁷ where the Court held that for the innocent party to have a legitimate interest, there must be reasonable grounds for keeping the contract open, bearing in mind the interests of the party in breach.

Finally, Cooke J. considered the judgment in the *Dynamic* where it was held that the *White and Carter* rule was general and that the exceptions applied in extreme cases. The burden of proof is on the party in breach to show that the innocent party had no legitimate interest in affirming the contract rather than claiming damages. Further, the burden is not discharged by showing that the innocent party's benefit from affirmation of the contract is small compared to the loss that may be suffered by the party in breach. Lastly, that the exception to the general rule that an innocent party has an unfettered right to elect to affirm the contract applies only in extreme cases where damages would be an adequate remedy and the option to keep the contract alive would be unreasonable.

In his judgment Mr Justice Cooke considered, firstly, whether a time charter is subject to the rule in *White and Carter* and found that the question was simple. Could owners claim hire from charterers pursuant to a time charter without charterers' cooperation? The judge found that the answer was affirmative. The Owners were entitled to refuse to accept redelivery of the vessel and could continue to hold the vessel at the Charterers' disposal even in the absence of any orders. The vessel would simply stay where she was at the time of the repudiation of the contract and continue to earn hire. The fact that the Charterers were liable pursuant to the terms of the charterparty to supply bunkers to the vessel was not held to be material as the

⁶ [1978] 2 Lloyd's Rep 357

⁷ [1995] 2 Lloyd's Rep 592

Owners could bunker the vessel themselves in the absence of the Charterers' cooperation and charge the price of bunkers stemmed to the Charterers. In order for the Owners to continue to perform the charterparty it was not required that the Charterers need do anything. Accordingly, the first qualification of the *White and Carter* rule was not triggered and the arbitrator had erred in law by finding to the contrary.

Secondly, Mr Justice Cooke then considered whether the second qualification of the *White and Carter* rule had been triggered, namely whether the Owners had a legitimate interest in affirming the contract rather than seeking damages. He found that the arbitrator had erred in law by applying the wrong test in considering whether the Owners had a legitimate interest in affirming the charter or not for the remaining 94 days of the contract period. The arbitrator had not asked the question as enunciated in *White and Carter* and the subsequent shipping authorities whether it would be "wholly unreasonable" for the Owners to affirm the contract rather than claim damages. The authorities which were considered by Mr Justice Cooke established that an innocent party will have no legitimate interest in affirming the contract when the continued performance of the contract can be described as "wholly unreasonable" or "perverse". Had the arbitrator asked that question he would have found that the Charterers had not discharged the burden of proof in showing that the Owners' election to affirm was beyond unreasonable. Had he asked that question the arbitrator would have considered whether there was any benefit to be had by the Owners, however small, in the affirmation of the charterparty compared to a claim in damages. The arbitrator had instead ignored the fact that the innocent party's general right to elect to affirm a contract would only be displaced in extreme cases. Accordingly, the arbitrator had erred in law.

Accordingly the Court held that the award should be varied to declare that the Owners were entitled to refuse redelivery of the vessel and were entitled to affirm the contract and claim hire for the balance of the minimum charter period.

Comment

The judgment is noteworthy as it has clarified that an innocent party will be entitled to affirm a contract and claim the contract price against the party in breach rather than accept the repudiation and claim damages. So long as the contract can continue to be performed by the innocent party without the cooperation of the party in breach and damages are an inadequate remedy under the circumstances and the innocent party's insistence on performing the contract is not wholly unreasonable or perverse, affirmation of the contract can be sought.

In a falling market owners may consider to elect to affirm the charterparty rather than accept a repudiatory breach and claim damages. Affirmation of the contract provides owners with a secure route by which to recoup losses arising from charterers' breach. Were owners to claim in damages they would have to wait until the end of the minimum charter period before their losses could be quantified and claim against charterers. At that time, charterers may have become insolvent or seek to settle at a discount of any losses claimed based on arguments regarding whether owners mitigated losses successfully or not and whether owners' losses

were properly quantified in light of the market available to the vessel during the balance of the minimum charter period. By exercising the option to affirm the charterparty, owners continue to perform the contract and earn hire in advance without having to grapple with arguments regarding mitigation of loss and quantification of damages.

The court applied a commercial approach in determining whether a claim in damages or affirmation of the contract was the correct remedy under the circumstances. The determining factor in the Court's ruling was that the Charterers were in effect seeking to benefit from their own breach by leaving the Owners to mitigate losses in a difficult market when they themselves could have traded the vessel in the same market if the Owners sought to affirm the contract. Upon fixing the charter, charterers bear the risk of trading the vessel in fluctuating markets. On that basis, Cooke J. found that the Charterers were attempting to get out of the difficulties faced in trading the vessel in a difficult market while at the same time imposing the same burden on the Owners and subsequently seeking to gain credit by settling a prospective damages claim at a discount.