Shipping

ReedSmith

The business of relationships.

House of Lords restricts charterers' liability for late redelivery

In ***The Achilleas, Transfield Shipping Inc of Panama v Mercator Shipping Inc of Monrovia*** the House of Lords had to decide whether Time Charterers, who had redelivered the vessel 9 days late, were liable to pay US$1.3 million to Owners (on the basis that the follow-on fixture had to be renegotiated because the laycan was missed) or only US$158,301.17 (the difference between the charter and market rate for the 9 day overlap). The House of Lords has today ruled unanimously in Charterers' favour, overturning the Court of Appeal, the Court of first instance and the decision of the majority arbitrators.

The facts

The charter period expired on 2nd May 2004. The first notice of redelivery was given on 8th April 2004 when Charterers gave 20 days notice between 30th April and 2nd May. On the basis of that redelivery notice, Owners fixed a period charter (4 to 6 months) at US$39,500 a day (the 'Cargill charter'). Laycan was 28th April to 8th May. When the vessel was not redelivered in accordance with the redelivery notice, Owners sought an extension of the laycan under the Cargill charter. This was agreed at 11th May, but the hire rate reduced from US$39,500 to US$31,500. The vessel was finally delivered at 08.15 on 11th May.

In any claim for breach of contract, the general rule of damages is that the innocent party is entitled to be placed in the position he would have been in if the breach had not occurred. Two limitations control the effect of this rule:

1. the innocent party's duty to mitigate (not at issue here); and
2. foreseeability of the damage. Traditionally, damages have been regarded as 'foreseeable' (and therefore recoverable) if the parties would have regarded them as being 'not unlikely' to occur in the event of breach.

The tribunal's decision

The arbitrators, by a majority decision, awarded damages in the sum of US$1.3 million. This award was calculated on the basis of the reduction in the hire rate agreed with Cargill of US$8,000 per day, multiplied by the duration of the Cargill fixture, on the basis that Charterers would be assumed to know that one of the hazards of late delivery might be the loss by Owners of a follow-on fixture concluded in a volatile market. They dismissed Charterers' argument that they did not assume responsibility for a loss of any particular fixture, on the basis that, as the type of loss was foreseeable, the length of the follow-on fixture was irrelevant.

Court of first instance and Court of Appeal

This decision was upheld at first instance and in the Court of Appeal.

House of Lords

The House of Lords has adopted a fresh approach to the issue of foreseeability, requiring the parties to consider whether the loss for which compensation is sought is of a 'kind' or 'type' for which the contract breaker ought fairly to be taken to have accepted responsibility even if it was 'not unlikely' to occur if the contract was breached.

The question of whether a given type of loss is one for which a party assumed contractual responsibility involves the interpretation of the contract as a whole against its commercial background and, like all questions of interpretation, is a question of law. In cases such as this, therefore, one has to consider what the charterers would have reasonably considered to be the extent of their liability when entering into the charterparty in September 2003. At that time it would have been within their contemplation that at some stage during the charter the Owners would enter into a follow on fixture and also that the market rate may fluctuate. What they would not have been able to contemplate would be the terms on which any future fixture was made, either as to its length or other terms, such as what was to happen should the previous charter overrun and the owner be unable to meet the new commencement date.

If you have questions or would like additional information on the material covered in this Bulletin, please contact the Reed Smith lawyer with whom you regularly work, or any of the following lawyers in our **Shipping Group**:

David Semark (London)
ddi: +44 (0)20 7772 5784
dsemark@reedsmith.com

Sally-Ann Underhill (London)
ddi: +44 (0)20 7772 5857
sunderhill@reedsmith.com

July 2008

Shipping 

The House of Lords appears to endorse the view that a charterer cannot be expected to assume responsibility for something that he can neither control nor, therefore, quantify.

The majority of their Lordships appear to have specifically endorsed the 'market rule' for assessing damages for late redelivery: namely that where a vessel is redelivered late, Owners are only entitled to damages for any difference between the market and charter rate over the length of the overrun period.

According to Lord Rodger, however, this endorsement is subject to two caveats: (1) that there may be cases where, when entering into a charterparty, a charterer could reasonably contemplate that late redelivery would mean there was no market for the vessel and so the owner might have a claim for some general sum for loss of business; and (2) the position might be different if, when entering into the charter, the owners told the charterers of the existence of a forward fixture including its terms, in which case the second limb of ***Hadley v Baxendale (1854) 9 Exch 341***, and whether the loss could *"reasonably be supposed to have been in the contemplation of both parties at the time they made the contract as the probable result of a breach of it"* may well be relevant.

The future

The House of Lords' decision will be welcomed by charterers. The market rule is clear, certain, and easy to calculate and apply. The prospect for disputes would be enhanced if parties were left to deal with uncapped loss of profit claims, based on unknown contracts of unknown lengths made at unknown times, especially when owners are able to protect themselves to a certain extent by (i) refusing illegitimate last voyage orders and (ii) ensuring that the laycan for any follow on fixture is fixed bearing the risk of a short overrun in mind.