Damages for Loss of Fixture - The “Achilleas” and The “Sylvia”:

July 2010

Introduction

Sometimes, when a charterparty is breached, the innocent party will lose a fixture. For example, where, under a charter party, a vessel is re-delivered late by her charterer, she may have missed the laycan for her follow-on fixture. Similarly, where an owner breaches the charterparty (e.g. by failing to maintain the vessel during the charter period so that she breaks down or is detained), a charterer, acting as a disponent owner, may lose his sub-fixture.

Can the innocent party recover? On the current state of English law, the answer differs depending on whether the lost fixture is (i) a follow-on fixture lost by the vessel’s owner, or (ii) a sub-fixture lost by an intermediate charterer during the currency of the charter itself.

The explanation for this apparent inconsistency in approach lies in the way questions of remoteness of damage were approached by (i) the House of Lords in The “Achilleas” [2008] UKHL 48, and (ii) Mr Justice Hamblen in The “Sylvia” [2010] EWHC 542 (Comm).

The traditional English law on the remoteness of damages in contract is this: was the loss caused by the breach of contract a kind of loss which, at the time the contract was concluded, the parties would reasonably have contemplated as not unlikely to result from the breach? That was the test set out in Hadley v Baxendale (1854) 9 Ex 341, as explained and refined further in Czarnikow v Koulous (The “Heron II”) [1963] 1 AC 350.

Further, provided that the parties reasonably contemplated the kind or type of loss as a not unlikely result, it did not matter that the extent of the loss was greater than they could reasonably have foreseen: the innocent party was entitled to recover its full loss, even if foreseeably large. See, Jackson v Royal Bank of Scotland [2006] 1 WLR 371.

The “Achilleas”

The “Achilleas” was a “late redelivery” case. In breach of the time charter between the parties, the defendant charterers re-delivered the vessel 9 days late – on 11 May 2004 instead of 2 May 2004. The claimant owners had entered into a follow-on charter at a rate of US$39,500 per day, with a cancelling date of 8 May 2004. As a result of the charterers’ breach, the new charterers became entitled to cancel the new fixture. The owners were forced to reduce the new charter rate by US$6,000 per day to avoid cancellation.

They claimed the hire they had lost as a result of the charterers’ delayed redelivery. The arbitrators, by a majority, awarded the owners US$1,364,564.37 being the US$8,000 per day reduction multiplied by the duration of the follow-on fixture. The dissenting arbitrator ruled that the damages should be limited to US$158,301.17, being the difference between the market and charter rates for the 9-days of wrongful delay. The dissenting arbitrator’s decision was based on the general understanding in the shipping market, that liability for late redelivery was restricted to the difference between the market rate and the charter rate for the over-run period.

Applying the conventional analysis summarised above, Christopher Clarke J. at first instance ([2007] 1 Lloyd’s Rep. 19) and the Court of Appeal ([2007] 2 Lloyd’s Rep. 555) both dismissed the charterers’ appeal against the majority arbitrators’ award.

The House of Lords, however, disagreed. It allowed the charterers’ appeal and, agreeing with the dissenting arbitrator, held that the owners’ damages were limited to the difference between the market and charter rates for the 9-days over-ran.

In reaching their conclusion, each of the five Law Lords delivered a fully reasoned speech. The differences in reasoning set out in these 5 speeches makes determining the ratio of the “Achilleas” a matter of some difficulty. McGregor on Damages (16th Ed), para 4-173 takes the view that the ratio of The “Achilleas” lies in Lord Roger’s orthodox approach discussed below. Conversely, Civility on Contracts (30th Ed.), 26-100A treats the case as imposing the broader “assumption of responsibility” requirement as an “additional and probably separate requirement of the remoteness rule”.

The confusion arises because The “Achilleas” discloses two distinct approaches to remoteness of damages. Lord Hoffman articulated a “broader” approach, holding that “the extent of a party’s liability for damages is founded upon the interpretation of the particular contract … construed in its commercial setting” (para 11). In his view, in this kind of case, the fundamental question is: is the loss the “kind or type for which the contract-breaker ought fairly to be taken to have accepted responsibility” (para 15). However, Lord Hoffman conceded that “in the great majority of cases”, that question would be answered simply by applying “the ordinary foreseeability rule” explained in The “Heron II”. If the loss satisfied that test, it will prima facie be recoverable. Only in unusual cases would that presumption be rebutted. Applying that approach and relying on the general understanding in the shipping market found by all the arbitrators, Lord Hoffman held that “the charterer cannot reasonably be regarded as having assumed the risk of the owner’s loss of profit on the following charter” (para 26). Lord Hope adopted a similar analysis, ruling that foreseeability was not enough, and “the question is whether the loss was a type of loss for which the party can reasonably be assumed to have assumed responsibility” (para 32).

Lord Roger agreed with the reasons given by Lords Hoffman and Hope.

Lord Roger purported to adopt the “orthodox approach based on the Hadley v Baxendale/The “Heron II” “ordinary foreseeability rule”. He held that, contrary to the findings of the majority arbitrators, the parties would not reasonably have contemplated an overrun of nine days would “in the ordinary course of things” cause the owners the kind of loss claimed. He reached that decision because the loss claimed occurred “only because of the extremely volatile market conditions” (para 60), was more extensive that either party could quantify at the time of contracting (para 61) and arose from an “arrangement with a third party about which the charterers knew nothing” (para 62). Lord Roger agreed with the reasons given by Lord Hoffman. Baroness Hale reluctantly agreed to allow the appeal on those grounds.

It is, with respect, difficult to see how the result in The “Achilleas” can be supported under the “orthodox” approach, as Lord Roger sought to do. Firstly, as Lord Hoffman pointed out in paragraph 25 of his speech, the question of whether the kind of loss was foreseeable as a not unlikely result of the breach is a question of fact (Monarch Steamship Co Ltd v Karshamns Oljefabrikker (A/B) [1949] A.C. 196, 223 (per Lord Wright), The Heron II [1969] 1 AC 360, 397B-D (per Lord Morris)). Arbitrators’ findings of fact are final. As Steyn L.J. explained in The Balaores [1993] 1 Lloyd’s Rep. 218, 229, “the arbitrators are the masters of the facts” and “a court would never question the arbitrators’ findings of fact.” Since the majority...
Secondly, only a few years earlier, the House of Lords decided in *Jackson v Royal Bank of Scotland* [2005] 1 WLR 377 that the extent of the loss need not be foreseeable provided the “kind” or “type” of the loss was foreseeable. Thus, the result cannot be justified on the basis that the losses were unforeseeably large. Finally, knowledge of the terms of the third party contract from which the loss flows has never been a requirement. The defendants in *Victoria Laundry (Windsor) v Newman Industries* [1949] KB 528, 543 were held liable to compensate the claimants even though they did not know of the terms of the contracts lost by the claimant laundry; all that was required was that the losses be in respect of “contracts to be reasonably expected”. There was nothing to suggest that the follow-on charter in *The Achilleas* had been concluded on anything other than normal market terms. The fact that the market had been higher when it was concluded and then dropped did not make that contract out of the ordinary. Movement is the essence of a market.

The “Sylvia”

As discussed above, in *The Achilleas*, the House of Lords held that where a vessel on time charter is redelivered late by charterers, an owner’s damages are limited to the difference between the charter and market rates for the over-run period and that an owner cannot recover lost profits on a cancelled follow-on fixture. The issue in *The Sylvia* was whether a similar limit applied where the owner’s breach of charter caused his time-charterer to lose a sub-fixture. The arbitrators below and the Court on appeal both held that it did not.

The tribunal had found that the owners had been in breach of their due-diligence and maintenance obligations, as result of which *The Sylvia* had been detained by port state control. This in turn led to the charterers missing the cancelling date on their sub-fixture, which the sub-charterers then cancelled. The substitute employment which the charterers were able to find post-cancellation was less profitable than the cancelled fixture. Charterers claimed the difference from owners. The tribunal found in the charterers’ favour.

The owners appealed, contending, in reliance on *The Achilleas* that the charterer’s only recoverable loss was the difference between the charter and market rates for the period of the detention and that the profits lost on the cancelled sub-fixture were too remote to be recoverable.

In order to decide the appeal, Mr Justice Hamblen had to ascertain the *ratio decidenti* of *The Achilleas*. He noted the confusion on this point due to the disparity between the two approaches adopted by their Lordships. After reviewing their speeches and subsequent commentary on the case, Hamblen J concluded that:

“in my judgment, the decision in *The Achilleas* results in an amalgam of the orthodox and broader approach. The orthodox approach remains the general test of remoteness applicable in the great majority of cases. However, there may be “unusual” cases, such as *The Achilleas* itself, in which the context, surrounding circumstances or general understanding in the relevant market make it necessary specifically to consider whether there has been an assumption of responsibility. This is most likely to be in relatively rare cases where the application of the general test leads or may lead to an unquantifiable, unpredictable, uncontrollable or disproportionate liability or where there is clear evidence that such a liability would be contrary to market understanding and expectations.”

He added that “in the great majority of cases it will not be necessary specifically to address the issues of assumption of responsibility”, holding that this was consistent with the approach taken in other post-Achilleas decisions, most importantly, the recent decision of the Court of Appeal in the non-shipping case of *Supershield Ltd v Siemens Building Technologies* [2010] EWCA Civ 7.

In an important passage for practitioners, arbitrators and the commercial community generally, the Judge emphasised further that, “it is important that it be made clear that there is no new generally applicable legal test of remoteness in damages. It appears that in a number of cases, this is being argued and that decisions are being challenged for failing to recognise or apply the assumption of responsibility test. This results in confusion and uncertainty.”

Applying these principles to the Tribunal’s decision, Mr Justice Hamblen held that they had not erred in law by concluding that lost profits on a sub-fixture lost due to an owner’s breach of contract were not too remote. He relied on the fact that period charters often contain an express liberty to sub-let, and that there is both judicial and academic authority for the view that they are recoverable. In particular, in *The Derby* [1964] 1 Lloyd’s Rep 653, Hobhouse J had clearly recognised that such a claim could properly be made. He also pointed out that where a sub-fixture is lost, there will often be a loss regardless of market considerations because charterers will have to find substitute employment with the vessel in a distressed position.

There were in addition, important difference between *The Achilleas* and the facts of *The Sylvia*. In particular there was no market understanding or expectation that a charterers’ loss is limited to the difference between the charter and market rates for the period of the delay caused by the owner’s breach. On the contrary, the general understanding – supported by Hobhouse J’s judgment in *The Derby* – is that results in arbitral references and assumptions made in other court cases – was that damages could be recovered for loss of a sub-fixture. Also, it was less likely that an unquantifiable loss would arise because the lost sub-charterer could never be longer than the length of the head charter itself, and, in cases where the cancelled sub-fixture would be a voyage charter in any event.

On this basis, the owners’ appeal was dismissed. Leave to appeal was also refused.

The Present State of the Law

The judgment of Hamblen J in *The Sylvia* is the latest, word on this issue. Along with the dicta of the Court of Appeal in *Supershield Ltd v Siemens Building Technologies FE Ltd* [2010] EWCA Civ 7, para 43, it suggests that *The Achilleas* has added a gloss to the orthodox “foreseeability test” under which, in very unusual cases, losses satisfying that orthodox test will nevertheless be held to be unrecoverable because the circumstances demonstrate that the breaching party could not reasonably be taken to have assumed responsibility for such losses. Indeed, the Court of Appeal in *Supershield* has gone even further by suggesting that this additional gloss can operate not only to restrict recovery but to expand it. Losses that were not sufficiently foreseeable could nevertheless be recoverable if the contract construed in its commercial context demonstrated that the breaching party had assumed responsibility for such unforeseeable losses.

One thing is, however, clear from *The Sylvia* and the other judicial pronouncements on *The Achilleas*. The courts are strongly discouraging defendants from “flying their luck” by relying on *The Achilleas* to avoid or reduce their liability. Whatever principle that case establishes it is likely to be applied only in the rarest of cases.

By David Semark and Chirag Karia of Quadrant Chambers.