ANALYSIS AND COMMENT

SPAR SHIPPING, THE ASTRA AND THE STATUS OF THE OBLIGATION TO PAY HIRE PUNCTUALLY: WATCHING A FALLING STAR

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Grand China Logistics Holding (Group) Co Ltd v Spar Shipping AS
[2016] EWCA Civ 982

Introduction

In *Grand China Logistics Holding (Group) Co Ltd v Spar Shipping AS*,[1] the Court of Appeal has handed down an eagerly awaited decision that resolves the vexed question of whether a charterer's failure to pay an instalment of hire punctually under a time charterparty is, in and of itself, a breach of condition with the consequence that the shipowner may claim damages for loss of its bargain, or else whether such a failure merely entitles the shipowner to withdraw the vessel from service in accordance with the express provisions of the withdrawal clause, with no such automatic entitlement to substantial damages. The Court of Appeal decided unanimously in favour of the latter interpretation, affirming the decision of Popplewell J at first instance.[2]

The decision therefore provides much needed clarity upon the true status of the obligation to pay hire punctually, an issue upon which – most unusually – opposing views had been expressed by highly experienced judges of the Commercial Court. In *The Astra*,[3] Flaux J had held[4] that the obligation was a condition but in reaching his decision, Popplewell J expressly declined to follow that decision.

Although it won the argument on the classification of the obligation, the charterer did not win the day. This is because the Court of Appeal saw no ground for interfering with the further decision of Popplewell J that, through evincing an intention not to pay in advance but only in arrears – a manner of performance found to be so substantially different from that which had been agreed as to go to the root of the contract – the charterer had committed an anticipatory breach of the charterparty, which the shipowner could, and did, accept as terminating the contract, and which entitled it to damages for loss of its bargain.

Facts

Spar Shipping AS (Spar) was the registered owner of three bulk carriers, the *Spar Capella*, the *Spar Vega* and the *Spar Draco*. Grand China Shipping (Hong) Kong Co Ltd (GCS) chartered the vessels from Spar by time charters on the NYPE '93 form. These were of relatively long durations: 35–37 months for the *Spar Draco*, and 59–62 months for the two other vessels. The charterparties provided for payment of hire to be guaranteed by GCS's parent company, GCL. Letters of guarantee were duly issued.

The *Spar Draco* was delivered into charter service on 31 May 2010, the *Spar Capella* on 6 January 2010 and the *Spar Vega* on 12 January 2011.

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[1] [2016] EWCA Civ 982.

[2] [2015] EWHC 718 (Comm), [2015] 1 All ER (Comm) 879.

[3] *Kuwait Rocks Co v AMN Bulkcarriers Inc (The Astra)* [2013] EWHC 865 (Comm), [2013] 2 All ER (Comm) 689.

[4] In view of Flaux J's primary conclusion that the charterer was in repudiatory breach of the charterparty in any event, it is difficult to avoid the conclusion that his decision on this point was *obiter*. Gross LJ's view at [39] that it was not is accordingly somewhat mystifying.

The charterparties each contained a 'hire payment' clause (clause 11) which, in the ordinary way, required that payment of hire be received by the shipowner on the due date, which was 15 days in advance. There was then a withdrawal clause, which provided that: 'Failing the punctual and regular payment of the hire … the Owners shall be at liberty to withdraw the Vessel from the service of the Charterers without prejudice to any claims which they (the Owners) may otherwise have on the Charterers'. As is common, the withdrawal clause was coupled with an anti-technicality clause, which laid down a 'grace period'. It required that, in case of failure to make payment by reason of oversight etc, the charterers be given three days' notice to rectify the failure, absent which the shipowners would be entitled to withdraw the vessel in accordance with the withdrawal clause.

From April 2011 (ie relatively early in the charterparty periods), GCS was in arrears as regards payment of hire. Spar recouped some of the arrears by exercising its lien on sub-freights, but there remained substantial outstanding hire on all three vessels throughout the summer of 2011, and a catalogue of missed or delayed payments. On 16 September 2011, Spar called on GCL for payment under the letters of guarantee. On 23 September 2011, Spar withdrew the *Spar Capella* and terminated that charterparty. A week later, Spar withdrew the *Spar Vega* and the *Spar Draco* and terminated those charterparties.

Upon bringing proceedings against GCL under the guarantees, Spar claimed both the balance of hire accrued due prior to termination and damages for loss of bargain in respect of the unexpired term of the charterparties. The total amount of damages awarded by the Commercial Court for loss of bargain, ie the difference between the agreed rate of hire and the rate obtainable in the market for replacement charterparties, was approximately US$24 million over all three vessels.

Decisions of Flaux J in *The Astra* and of Popplewell J in *Spar Shipping*

Since the Court of Appeal was in effect faced with a choice between the opposing judgments of Flaux J and Popplewell J on the breach of condition point, it is convenient to outline the key elements in the reasoning of each.

It is a peculiar feature of the debate that both arguments could be supported by copious *obiter dicta*. This was so, notwithstanding it having been the received opinion, at least on the strength of the views expressed in the leading textbooks, that the obligation was *not* a condition. *Dicta* could be marshalled from such eminent judges as Lords Diplock and Denning (in favour of it being a condition) and of Lords Mance and Sumption (against it being a condition). In only one prior case had the point been decided, namely in *The Brimnes*.[5] In that case, Brandon J (as he then was) decided that the obligation was not a condition. But the authority of that decision was arguably in doubt, owing to the reliance placed on another case, *The Georgios C*,[6] which had been overruled.[7] Given that background, it is unsurprising that both Flaux J and Popplewell J undertook lengthy and painstaking exegeses of the available authorities, before setting out their preferred approaches to the problem.

The approach taken by Flaux J in *The Astra* was a robust one. First and foremost, he derived particular support from the express entitlement of the shipowner to withdraw the vessel whenever there was a failure to make payment: the fact that the contract treated this as sufficiently serious to entitle the shipowner to withdraw the vessel irrespective of whether the breach was otherwise repudiatory was, he considered, a 'strong indication' that the parties regarded the failure to pay hire promptly as going to the root of the contract, and thus that the provision was a condition. Secondly, reliance was placed on there being a 'general rule' in mercantile contracts that where there is a provision requiring something to be done by a certain time, time is considered to be of the essence. In this connection, Flaux J considered that the anti-technicality clause, whereby the shipowner was entitled to bring the contract to an end upon the expiry of the stipulated grace period, had the effect of making the obligation to pay hire a condition. But even if there were no anti-technicality clause, he would still, albeit with some hesitation, have concluded that the obligation was a condition. Thirdly, the need for

[5] *Tenax Steamship Co v Owners of the Motor Vessel Brimnes (The Brimnes)* [1973] 1 WLR 386.

[6] *Empresa Cubana de Fletes v Lagonisti Shipping Co Ltd (The Georgios C)* [1971] 1 QB 488.

[7] By *Mardorf Peach & Co Ltd v Attica Sea Carriers Corp of Liberia (The Laconia)* [1977] AC 850. Ultimately, the Court of Appeal in *Spar Shipping* took the view that the relevant *dicta* in *The Georgios C* had been left unaffected by that overruling: see para 25 (Gross LJ).

certainty in commercial transactions could, he felt, only properly be served by categorising the term as a condition. Otherwise the shipowner might be left in a position of uncertainty whether to 'withdraw the vessel or to soldier on with a recalcitrant charterer until such time as the owners were in a position to say that the charterers were in repudiatory breach'.

The approach taken by Popplewell J was more measured. Unlike Flaux J, he had the benefit of being referred to *Financings Ltd v Baldock*,[8] a case concerning a hire purchase agreement in which the financing company terminated the contract pursuant to a withdrawal clause after the hirer failed to pay the first two instalments. Dismissing the financing company's claim for loss of bargain damages, the Court of Appeal held that the hirer had not repudiated the agreement. As such, the decision neatly demonstrated that a 'mere' contractual right of cancellation could take effect with no anterior breach of condition. The case thus supported the proposition that a contractual termination clause should be treated as a mere contractual option to cancel, which does not confer greater rights to damages at common law than would exist apart from the clause *unless there is clear language to that effect.*

Fortified by this decision, Popplewell J declined to follow the robust interpretation accorded by Flaux J to the withdrawal clause. As he explained: 'Once it is recognised that a clause providing for termination on any breach of a term, however trivial, may constitute an option to cancel, the fact that the clause is triggered by such a breach tells one nothing about whether the term breached is to be characterised as a condition'. Rather, the critical question is whether payment of hire would be treated as a condition in the absence of the withdrawal clause. In the view of Popplewell J there were a number of reasons why it should not. First, the very inclusion of a contractual right of termination by withdrawal suggested that in its absence there would be no such right. Secondly, there was a presumption in mercantile contracts that stipulations as to the time of payment were not to be treated as conditions absent a contrary indication in the contract. Thirdly, predicated breaches of the term might range from the trivial to the serious. For instance, there may be a delay in payment falling outside the scope of the anti-technicality clause, of only a few minutes, causing no loss to the owners. Unless considerations of commercial certainty dictated a different result, this was the classic *indicium* of an innominate term. In the situation at hand, commercial certainty did not point to a different conclusion, since certainty was a *desideratum* which was to be balanced against the need not to impose liability for a trivial breach in undeserving cases.

However, Popplewell J went on to hold that, even though GCS' actual breaches in failing to pay hire were not themselves repudiatory, they nevertheless constituted conduct that would lead the reasonable observer to conclude that GCS intended not to perform the contract in the agreed manner in future, but instead in a manner that was so different (ie in arrears, rather than in advance) as to deprive Spar of substantially the whole benefit of the contract. In this regard, it was telling that GCS had stated in antecedent arbitration proceedings brought by Spar that it was 'willing to pay hire at the agreed rate, albeit not in advance due to the temporary cash flow problems and the internal restructuring'. There having been an anticipatory breach by renunciation, Spar was not required to wait until the repeated failures had become repudiatory, but could take GCS at its word and sue for loss of bargain damages, just as though the repudiatory breach had already occurred.

The decision of the Court of Appeal

The leading judgment was given by Gross LJ, with whom the other Lords Justice of Appeal (Sir Terence Etherton MR and Hamblen LJ) agreed, each giving additional reasons.

Gross LJ explained that for both historical and analytical reasons he was not persuaded that the inclusion of the express withdrawal clause provided a strong or, indeed, any indication that clause 11 was a condition. In his view, the historical reason for the development of withdrawal clauses was to put beyond argument shipowners' entitlement to terminate the charterparty where charterers had failed to make a timely payment of hire. In the circumstances, it was a 'leap too far' to argue from the mere presence of an express withdrawal clause that the obligation to make punctual payment of hire was a condition. He too distanced himself from the view of Flaux J that the resolutive nature of the

[8] [1963] 2 QB 104.

withdrawal clause pointed towards its being a condition. As he observed: 'The simple and important point to keep in mind is that all conditions entitle the innocent party to terminate the contract – but not all contractual termination clauses are conferred for breaches of condition alone'. With respect, this is plainly right. Indeed, it could be said that a right of withdrawal, far from indicating that the obligation to make due payment is a condition of the contract, is equally (if not more) consistent with a recognition that default does not in principle give rise to a right of termination. If it did, then the contractual right would be otiose.

Secondly, Gross, LJ referred to and applied a principle derived from speeches of the House of Lords in *Bunge Corp v Tradax SA*[9] that, 'unless the contract made it clear that a particular stipulation was a condition or only a warranty, it was to be treated as an innominate term; the courts should not be too ready to interpret contractual clauses as conditions'. In the present case, the charterparties did not make it clear that clause 11 was to be categorised as a condition.

Thirdly, whereas certainty was plainly a consideration of major importance when construing commercial contracts such as charterparties, the real question lay not in choosing between certainty and uncertainty but in striking the right balance. Significant certainty was already achieved by construing clause 11 as a contractual termination option, *simpliciter*. While greater certainty might be achieved by categorising clause 11 as a condition, it was significant that breaches of clause 11 could range from the trivial to the grave. The cost of greater certainty was thus the possibility of disproportionate consequences flowing from trivial breaches. This, in the opinion of Gross LJ, resulted in an unsatisfactory balance.

Fourthly, Gross LJ did not regard as significant the arguments advanced on the basis of a general presumption that time is of the essence in mercantile contracts. In the specific, detailed and specialised context of hire payment under time charterparties, there could only be limited scope for general presumptions. In addition, any presumption that time is generally of the essence in mercantile contracts did not, in his view, routinely apply to the time of payment, unless a different intention appeared from the terms of the contract.

Fifthly, Gross, LJ remarked that he was 'wholly unable to accept' the submission that the anti-technicality clause strengthened the case for timely payment of hire being a condition of the charterparties. Such clauses were developed to protect charterers from the serious consequences of a withdrawal, not to make time for payment of the essence. Finally, Gross LJ drew reassurance from his perception that market reaction generally supported the decision of Popplewell J.

The reasoning of the other Lords Justice of Appeal on this issue was similar, Hamblen LJ adding that: 'in circumstances where, as here, the law had apparently been settled by an existing decision for some 40 years, without any indication of market disquiet, a court should be very cautious before departing from such a decision so as to disturb the predictability of the law and detract from its certainty'.

In relation to the appeal from the finding of anticipatory breach by renunciation, the Court of Appeal declined to interfere with the decision of the Commercial Court. Sir Terence Etherton MR observed that it involved a multi-factorial assessment by the trial judge, which should not be disturbed unless the judge had made some error of principle or reached a decision that was outside the bounds of any reasonable judicial determination. There had been no such error or decision. Although there existed different formulations of the test for repudiatory breach, there was no divergence in principle. The foundational principle, in light of the assimilation in *Hongkong Fir Shipping*[10] of the test for repudiatory breach of an innominate term and the test for frustration, was that there will be a repudiatory breach if, absent fault, there would be frustration, ie where, according to Lord Radcliffe's formulation in *Davis Contractors Ltd v Fareham Urban District Council*,[11] a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. Whilst Gross LJ cautioned that the test could not be applied mechanistically to renunciation,

[9] [1981] 1 WLR 711.

[10] *Hongkong Fir Shipping Co Ltd v Kawakaki Kisen Kaisha Ltd (The Hongkong Fir)* [1962] 2 QB 26.

[11] [1956] AC 696.

he expressed no doubt as to its general applicability. As Sir Terence Etherton MR stated: 'the conduct of GCS evinced an intention to turn each of the contracts into something radically different from its terms, namely from a contract for payment in advance … to one for payment in arrear'.

Commentary

The Court of Appeal confirms what had long been treated by many as the law. Indeed, to those who had assumed the proper classification of the obligation to be relatively well settled, the expression of divergent views in the debate that preceded the decision came as something of a surprise.

A powerful opinion (albeit expressed only as his 'current view') was presented by Lord Phillips, formerly a justice of the Supreme Court, in his Cedric Barclay Memorial Lecture of 2015. His preference was for the judgment of Flaux J, on the basis that 'the judgment of Popplewell J does not lead to a sensible commercial result'. In this regard, Lord Phillips observed that prompt and regular payment of hire was of great importance to the shipowner, since he is likely to be relying on it to fund his own obligations under the charter, or to pay instalments due under finance arrangements that had funded the building or purchase of the ship. Indeed, hire had, as Lord Phillips noted, been described as 'the lifeblood of the commercial adventure'. If there existed only a contractual right of withdrawal without any attendant exposure to loss of bargain damages, there would only be a strong incentive to pay hire where the market had *risen* since the conclusion of the charterparty, since otherwise the charterer would lose the benefit of a valuable contract. Where, however, the market had *fallen*, there was, he noted, no equivalent incentive. In that situation, the charterer, who was having to pay more than the market rate for the vessel, would be overjoyed to have the vessel withdrawn. The threat of withdrawal was, therefore, of no concern to such a charterer, unless it carried with it a liability to pay damages for the loss of future hire. Hence Lord Phillip's opinion that, if the obligation to pay hire promptly was to have any weight in a falling market, it must be a condition of the charter.

However, Lord Phillips' view of the commercial imperatives itself proved controversial. When giving the O'May Lecture in November 2015,[12] Sir Bernard Eder, formerly a judge of the Commercial Court, queried the usefulness of considerations of commercial common sense at all. With reference to 'the clash' between *The Astra* and *Spar Shipping*, he asked:

> In that specific context, what is "commercial common sense"? The truth is: I have no idea. From the owner's point of view, it may well be commercial common sense that the charterer should pay the hire due on time – and not a minute or even a second late; and that any failure to pay by the due date should entitle the owner to bring the charter to an end and claim substantial damages. From the charterer's point of view, it may well be commercial common sense that if, for example, the hire is late by a very short period due to no fault of his own (eg some fault in the banking system), such failure should not amount to a repudiation so as to entitle the owner 'to bring the charter to an end and claim substantial damages'.

Having expressed doubt whether a judge is equipped to weigh these competing arguments properly, he recommended a black-letter law approach to the classification of conditions, as exemplified in *Bunge v Tradax*.[13] He commented: 'Owners and charterers are, of course, perfectly entitled and able to make the obligation to pay hire a condition. It is easy-peasy. They can, I think, do so by saying that "time shall be of the essence" … But absent language of such kind, there is, in my view, no warrant for the Court, in effect, to insert those words in the charterparty under the banner of commercial common sense'.

In the event, all three Lords Justice of Appeal expressly referred to the approach recommended by Lord Scarman in *Bunge v Tradax*,[14] ie, 'Unless the contract makes it clear, either by express provision or by necessary implication from its nature, purpose, and circumstances … that a particular stipulation is a condition or only a warranty, it is an innominate term'. Both Gross and Hamblen LJJ particularly commended this approach. Whilst commercial expectations were still taken into consideration by Gross LJ as part of the concomitant exercise in interpretation, he expressly declined to follow the

[12] Now published as 'The construction of shipping and marine insurance contracts: why is it so difficult?' [2016] LMCLQ 220.
[13] Note 9.
[14] ibid.

views of Lord Phillips on the basis, as noted above, that the 'real question' lies not between certainty and no certainty, 'but as to the degree of certainty best likely to achieve the right balance'. It is respectfully suggested that the decision of the Court of Appeal is indeed the fair result.

In this context, it can be said that a right of withdrawal adequately defines the circumstances in which the charterparty can be terminated, which is surely the area where certainty is most required. It is true that if the obligation is an innominate term, any claim to damages for loss of bargain will depend on the gravity of the breach, but that is true for all innominate terms. Moreover, in answer to the point that a charterer only has an incentive to pay hire on a rising market and that a bare right to withdraw might not adequately compensate the shipowner on a falling market, there is surely merit in the riposte that in that situation the shipowner is unlikely to withdraw unless the charterer's conduct has been so egregious as to amount to a repudiation or renunciation entitling it to terminate and claim damages in any event.

As regards the argument based on the anti-technicality clause, such a clause, where it exists, generally only qualifies the express right of withdrawal. It would therefore be very odd that the presence or absence of this essentially adjectival clause should affect the correct categorisation of the substantive obligation to pay hire. Moreover, as cogently pointed out by Popplewell J, there is a conceptual distinction between a provision that time is of the essence in relation to a particular term and a notice that allows one party subsequently to make time of the essence in relation to what was initially an innominate term. An anti-technicality provision is of the latter type and so cannot have the effect of retrospectively converting an innominate term into a condition.

Turning to the other main issue in the case, ie anticipatory breach by renunciation, it is worth observing that the application of this doctrine to repeated late payments represents a development in the existing case law in this area, even if the principles are hardly new. In *The Brimnes*, repeated late payment of hire did not amount to a renunciation, Brandon J observing that: 'it would be necessary to find that they evinced clearly by it an intention not to be bound by the terms of the contract. I am not satisfied that, on an objective view, their conduct in relation to late payment, although persisted in over a long time, went as far as this'.[15] Two points in particular merit comment.

The first is that, notwithstanding the acknowledgement that punctual payment is of critical importance to shipowners, the actual breaches involved in late payment between April and September 2011 were insufficient of themselves to amount to actual repudiatory breach, hence the need to rely on the doctrine of anticipatory breach. (It appears that the shipowner may have argued before the Court of Appeal that Popplewell J should have found an actual repudiatory breach, but the argument did not find traction.) That the actual breaches were insufficient is consistent with the high test for repudiatory breach, akin to frustration.

The second point is that, whilst the doctrine of anticipatory breach is useful in coming to the aid of an innocent party who cannot yet rely on actual repudiatory breach, the question of whether the relevant conduct amounts to renunciation is likely to be highly fact sensitive, and different, reasonable answers are possible. It is a conspicuous fact that, although the argument succeeded in *Spar Shipping*, it did not succeed in such cases as *Valilas v Januzaj*,[16] in which there had been a failure to pay three consecutive monthly instalments under a contract for the provision of dental practice facilities; or in *Financings v Baldock*, in which the hirer failed to pay two consecutive monthly instalments due under its contract of hire-purchase.

Conclusion

After the imbroglio of an acute disagreement in the Commercial Court, the decision of the Court of Appeal provides much needed clarity. If shipowners dislike the decision, there remains a 'self-help' solution open to them. The latest edition of the New York Produce Exchange form, NYPE 2015 (a *pro forma* time charterparty wording), includes a provision that intends to reflect, by express wording, the result in *The Astra*. However, given the soft market conditions currently being experienced, one wonders how regularly this provision will be used.

[15] At 409–10.

[16] [2014] EWCA Civ 436, [2015] 1 All ER (Comm) 1047.