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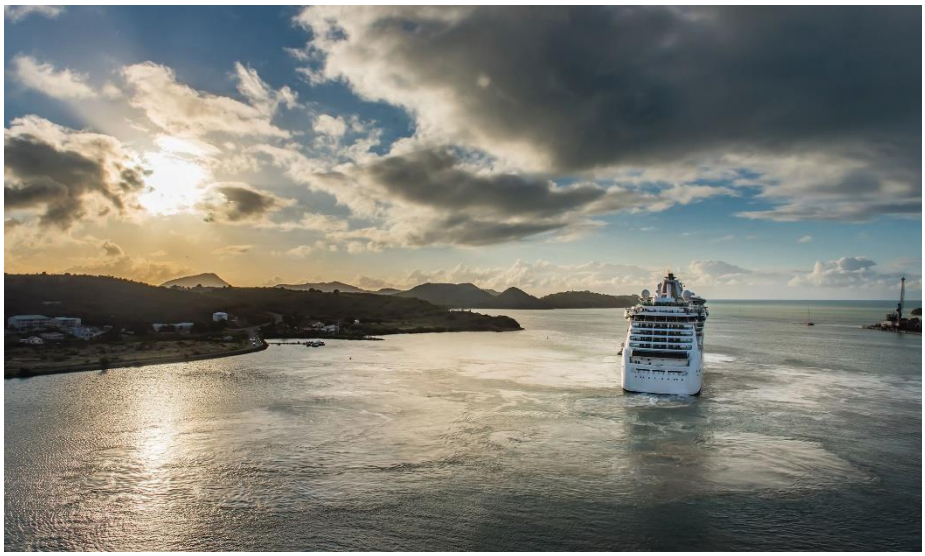
BRIEFING

DAMAGES AND MITIGATION: SUPREME COURT TAKES A SHORT CRUISE ON BENEFITS

JULY 2017

- SUPREME COURT RULES THAT EARLY SALE OF VESSEL FOLLOWING REPUDIATORY BREACH OF CHARTERPARTY SHOULD NOT BE BROUGHT INTO ACCOUNT TO DIMINISH OWNER'S DAMAGES.
- SALE OF VESSEL WAS NEITHER CAUSED BY BREACH NOR A SUCCESSFUL ACT OF MITIGATION.



In an eagerly awaited decision the Supreme Court has overturned the Court of Appeal's judgment in *Globalia Business Travel S.A.U. (formerly TravelPlan S.A.U.) of Spain v Fulton Shipping Inc of Panama*[1] and has ruled that a shipowner's benefit from selling its vessel, following a time charterer's repudiatory breach, was not to be taken into account when assessing the shipowner's damages. This decision has relevance to the law of damages generally, beyond its time charter context.

"THIS DECISION HAS RELEVANCE TO THE LAW OF DAMAGES GENERALLY, BEYOND ITS TIME CHARTER CONTEXT."

Facts

The claimants (the "Owners") and the defendants (the "Charterers") entered into a time charter for the cruise ship *NEW FLAMENCO* (the "Vessel"). The Charterers committed a repudiatory breach of the charterparty and the Owners accepted the breach and terminated in August 2007, suing for damages for lost income over the remaining two years of the charter.

On termination, the Owners were unable to charter out the Vessel as there was no available market. They therefore agreed to sell the Vessel for US$23.765m. This was fortuitous as vessel values fell significantly following the financial crisis in 2008, and had the Owners sold the Vessel at the end of the charterparty period, i.e. in 2009, the market price for the Vessel would have been only US$7m. The Owners had therefore made a windfall of almost US$17m.

[1] [2017] UKSC 43

Arbitration

The Owners commenced arbitration to recover the hire that would have been earned during the remaining two years of the charter.

The arbitrator found that the sale of the Vessel by the Owners in October 2007 was caused by the Charterers' breach of the charterparty, and that the sale was made in reasonable mitigation of the Owners' loss. Consequently, the Owners' windfall/benefit of US$16.765m, due to selling the Vessel in 2007 rather than in 2009, had to be taken into account when determining the Owners' damages. This meant that the Owners losses were extinguished.

Commercial Court

The Owners were granted permission to appeal to the High Court on a question of law under section 69 of the Arbitration Act 1996. The issue on appeal was whether the Charterers were entitled to have taken into account, as diminishing the Owners' loss of hire, a benefit being the Owners' avoidance of a drop in the capital value of the vessel between 2007 and 2009. Mr Justice Popplewell overturned the arbitrator's decision, holding that:

"THE ISSUE ON APPEAL WAS WHETHER THE CHARTERERS WERE ENTITLED TO HAVE TAKEN INTO ACCOUNT, AS DIMINISHING THE OWNERS' LOSS OF HIRE, A BENEFIT BEING THE OWNERS' AVOIDANCE OF A DROP IN THE CAPITAL VALUE OF THE VESSEL BETWEEN 2007 AND 2009."

1. in order for a benefit to be taken into account, the breach must have caused the benefit. It is not enough for the breach merely to provide the occasion, context or trigger for the benefit, nor is it sufficient just to show that the benefit would not have occurred but for the breach;
2. the analysis was the same if the actions giving rise to the benefit were considered as mitigation of loss. It was not sufficient for the mitigating step to be reasonable or logical, nor was it sufficient for there to be a causative connection linking breach, mitigation and benefit;
3. the fact that the benefit was of a different kind to the loss (i.e. the benefit was capital and the loss was income) or that the benefit arose from something that the innocent party could have done in a non-breach situation was indicative that the benefit was not legally caused by the breach; and
4. it would be contrary to fairness and justice to allow the Charterers to benefit from the Owners' business acumen in obtaining a good deal for the Vessel.

Mr Justice Popplewell concluded that, in all the circumstances of this case, the benefit was not legally caused by the breach. The Vessel was purchased in 2005 and could have been sold at any time thereafter at the prevailing market rate. The difference in the Vessel's value between 2007 and 2009 was not caused by the Charterers' breach but by the financial crisis. The decision to sell was a matter of the Owners' commercial judgment and involved commercial risk taken for their own account.

Court of Appeal

The Charterers were granted permission to appeal to the Court of Appeal, which overturned Mr Justice Popplewell's decision and upheld the original arbitration award.

The Court of Appeal's starting point was the House of Lords' decision *in British Westinghouse Electric and Manufacturing Co Ltd v Underground Electric Rlys Co of London Ltd*[2], namely that if a claimant adopts a course of action which arises from the consequences of a breach by way of mitigation and is in the ordinary course of

[2] [1912] AC 673

business, then any benefit obtained through that course of action is to be taken into account when determining damages, unless it is wholly independent of the relationship between the claimant and defendant. In the Court's view, this principle was sufficient to guide a decision maker in any particular case.

Applying the *British Westinghouse* test, the Court of Appeal held that where there is no available market at the time of termination, an Owner may decide to sell its vessel as mitigation rather than spot trade her. Provided that the sale was: (i) made in mitigation; (ii) made in the ordinary course of business; and (iii) had arisen from the consequences of the Charterers' breach, it would be acceptable to take any earnings from such a sale into account when determining the Owners' damages.

The Supreme Court

The Owners made a final appeal to the Supreme Court, which overturned the Court of Appeal's decision. Lord Clarke (with whom the rest of the Court agreed) held that the sale of the Vessel may have been triggered, but was not legally caused by the Charterers' repudiation of the charterparty. Further, on the facts, the fall in value of the Vessel between 2007 and 2009 was not relevant as the Owners' interest in the capital value of the Vessel had nothing to do with the interest that had been injured by the Charterers' breach of the charterparty.

The Supreme Court did not go so far as to state that when determining loss/damages the benefit taken into account must be the same as the loss caused by the wrongdoer. The key point is whether there is a sufficiently close link between the two and not whether they are similar in nature.

"THE BENEFIT THAT IS TO BE TAKEN INTO ACCOUNT MUST HAVE BEEN CAUSED EITHER BY THE WRONGDOER'S BREACH OR BY A SUCCESSFUL ACT OF MITIGATION."

The benefit that is to be taken into account must have been caused either by the wrongdoer's breach or by a successful act of mitigation. Lord Clarke held that the Owners' made a commercial decision to sell the Vessel, something which was not linked to the charterparty and which had nothing to do with the Charterers or their repudiation of the charterparty.

Lord Clarke agreed with Mr Justice Popplewell in that there was no relevant causal link between the Charterers' breach of the charterparty and the Owners' decision to sell the Vessel. At most, the premature termination of the charterparty was the occasion for selling the Vessel and not the legal cause of it.

As the sale of the Vessel was not caused by Charterers' breach, it could also not be considered an act of (successful) mitigation. The Charterers' breach of the charterparty had cost the Owners an income stream, and the sale of the Vessel, which resulted in recovery of capital investment, could therefore not mitigate against this loss of income.

Comment

This case shows the difficulties often experienced finding consistent reasoning on cases on damages, causation and mitigation where unusual facts are involved. It is with this in mind that Lord Clarke began his conclusion with an observation that most damages issues arise from the default rules which the law devises to give effect to the principle of compensation but the courts recognise there will be cases with special facts where default rules will not work.

"THIS CASE SHOWS THE DIFFICULTIES OFTEN EXPERIENCED FINDING CONSISTENT REASONING ON CASES ON DAMAGES, CAUSATION AND MITIGATION WHERE UNUSUAL FACTS ARE INVOLVED."

While the Supreme Court has recognised this as a special case and (particularly in view of the detailed judgments in the courts below) appears to have adopted a "less said the better" approach, a number of questions arise. Whereas the Court of Appeal gave a more expansive view of actions that could be considered as acts of mitigation according to the principle in *British Westinghouse*, the Supreme Court has sided with the Commercial Court in providing a more restrictive view when considering the necessary causal link. Has the test changed? Arguments as to what exactly is the requisite causal link required between breach and benefit will go on and, in particular, whether a benefit of a different kind (in this case loss of an income stream and recovery of capital) can ever mitigate a loss.

The Supreme Court did not expressly address the public policy/fairness and justice ground raised by Mr Justice Popplewell in the Commercial Court that it was unfair for a party found liable for repudiatory breach to escape its liability because the non-defaulting party exercised its business acumen and made a decision to sell. However, many business people would agree with Mr Justice Popplewell that this just does not seem right.

FOR MORE INFORMATION

Should you like to discuss any of the matters raised in this Briefing, please speak with one of the authors below or your regular contact at Watson Farley & Williams.

ANDREW HUTCHEON
Partner
London

+44 20 7814 8049
ahutcheon@wfw.com

THOMAS WHITFIELD
Associate
London

+44 20 7814 8175
twhitfield@wfw.com

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