September 27, 2021

Cutting Corners: Freighters, Fire Engines and Formula One

The puzzle of pure services, skimped performance and market value

By Rob Blackett

Introduction

In *Tibermede* v *Graham & Co* (1921) 7 Ll.L.Rep. 25 a charterer hired a freighter. It seems that, when the time came to load it, the charterer discovered the vessel was slightly smaller than had been warranted, but the charterer was still able to carry all its intended cargo without difficulty. The charterer nonetheless claimed damages for this breach of warranty.

In English law, the purpose of contract damages is for the claimant "*so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed*" (*per* Baron Parke in *Robinson* v *Harman* (1848) 154 ER 363). Lords Scott and Sumption confirmed this to be the 'fundamental principle' governing the quantum of damages for breach of contract (in *Golden Strait Corporation* v. *Nippon Yusen Kubishka Kaisha ("The Golden Victory")* [2007] UKHL 12 at paragraph 29 and again in *Bunge SA* v *Nidera BV* [2015] UKSC 43 at paragraph 14).

Tibermede's owner had 'skimped' on performance but the charterer was no worse-off than if the contract had been performed in full. The undersized ship carried all the cargo. A larger ship would have carried the same cargo. The charterer was already in the same situation as if the contract had been performed. No money was needed to place him there. Yet the charterer was awarded damages for breach of contract. In this article, we consider whether that award can be justified.

An error of law?

Breaches of contract (as distinct from torts) are 'actionable *per se'*, meaning a claimant who proves a breach but suffers no loss is still entitled to a small sum by way of 'nominal' damages. The answer to the question is thus that the charterer in *Tibermede* should properly have been awarded nominal damages. The same logic applies more generally, if the charterer had been supplied with a vessel which was deficient in some other way besides cargo capacity, but still performed the commercial function for which the charterer required it.

Contrary to that fundamental principle, however, the court in *Tibermede* nonetheless awarded the charterer a material sum, being the difference between the market value of what was contracted for (use of a bigger vessel) and what was supplied (use of a smaller one), assessed by reference to the charter rates for such vessels at the time of contracting. The case suggests that when an owner supplies an undersized vessel, the charterer can always, as of right, claim at least this amount, irrespective of the charterer's real loss.

The judgment (mistakenly) treated contracts to hire and sell ships as relevantly the same, assuming that the same considerations which justify awarding difference in market value when a sale of goods contract is breached justify the same result for breach of a contract of hire.

Compounding the error

This error was compounded because *Tibermede* was followed uncritically in *Sterns Ltd* v *Salterns Ltd* [1922] Lloyds' Rep 385 and then cited without more in *Tor Line AV* v *Alltrans Group of Canada Ltd (The "TFL Prosperity")* [1982] Lloyd's Rep 1 p622) (both cases involving charterparties). The three cases are now referred to in the practitioner works on charterparties as apparently having established a special rule for how damages are to be calculated when the cargo capacity of a ship is misdescribed.

Broadly the same scenario which arose in those cases has been considered in other cases, too. The scenario is: a claimant, with a view to profit, retains a defendant to perform a 'pure' service (one which is not intended to deliver some saleable residue like a new or improved piece of property), the defendant skimps on performance, but the claimant suffers no, or little, financial loss. At least two Court of Appeal cases (*White Arrow Express Ltd.* v *Lamey's Distribution Ltd*. [1995] CLC 1251 and *HM Attorney General* v *Blake* [1997] EWCA Civ 3008) and one House of Lords case (*HM Attorney General* v *Blake* [2000] UKHL 45) contain *obiter dicta* which appear to support awarding such claimants the difference in market value.

These *obiter dicta* suggest such awards are justified by pointing to (hypothetical) consumer cases where a claimant would recover the difference in market value, like where a claimant pays £50 for a five course meal and receives three courses with a market value of £30, and recovers £20 in damages. But, on close analysis, the underlying principles which justify that result when services were purchased with a view to securing some non-financial benefit – pleasure, utility or safety – will rarely lead to the same result in a commercial case, where the services were purchased with a view to profit alone.

The much-discussed first instance case *Giedo Van Der Garde BV & Anor* v *Force India Formula One Team Ltd* [2010] EWHC 2373 is sometimes cited as a further example of a court having awarded difference in market value for 'skimped' performance of commercial pure-services contract. In truth, though, that case is hard to characterise as a purely commercial contract. *Tibermede*, *Sterns*, *TFL Prosperity* and *White Arrow*, by contrast, were indisputably commercial contracts, and illustrate far more clearly than *Giedo Van Der Garde* the error which is committed when a court awards damages on such a basis. These decisions are discussed in turn below.

1920 - *Tibermede*

During the First World War, the British government responded to the loss of shipping by ordering thousands of new cargo ships, to be owned by the state for the duration of the war. Each was given a name prefaced by 'War', making for incongruous names such as *War Joy*, *War Idyll* and *War Lemon*. In late 1919 one such ship, *War Monsoon* was sold to Mede Lines, who promptly renamed her *Tibermede*. She had a short career. On 13 November 1919 a charterer called Graham & Co chartered *Tibermede* for a voyage from Bombay, apparently her first charter. We do not know the intended cargo or destination. This first charter gave rise to a dispute which was referred to arbitration. The award was appealed. By the time the court handed down its judgment, in 1921 *Tibermede* was no more, having sunk in May 1920 off the coast of Portugal.

The judge was Montague Shearman. He had been an accomplished athlete, swimmer and rugby player, founded the Amateur Athletics Association and wrote several books on football and athletics. According to commercialcourt.com, "*his professional life did not achieve the same heights*", with his biographers describing his as a "*useful*" judge who had "*a nodding acquaintance with the commercial court*". His judgment in *Tibermede* was two paragraphs long and appears to have been given *extempore*.

© 2021 Haynes and Boone, LLP

The charterparty said *Tibermede* had a certain deadweight capacity and cubic capacity. According to the case report: "*The ship was a new ship, and when she was first loaded it was discovered that the statements were wrong. Her deadweight capacity was greater than stated, and her cubic capacity was less than stated*". The charterers failed to pay the hire. The owners brought a claim for the hire. The charterers counterclaimed for the breach of warranty. The case report says:

> "*… It was obvious that the claimants' claim for hire must be allowed in full. When it came to a question of whether anything should be allowed by reason of this breach of warranty the owner said there ought to be disclosure of documents passing between Messrs. Graham & Co. in London and Messrs. Graham & Co. in Bombay to show whether or not there was any damage suffered in fact by reason of this breach of warranty. The owners very shrewdly suspected that Messrs. Graham & Co. had no cargo to load at Bombay. The Umpire had awarded Messrs. Graham & Co. £2000 damages* [equivalent to £100,000 in 2021 adjusted for inflation] *against the owners on the basis of the difference in cubic capacity, and the owners said there was no evidence before him on which he could make that award. As it was a matter of counterclaim, the damages had to be proved, and there was no proof of any damage whatever.*"

The sum of £2,000 was the difference between the contract price and the charter rate for the smaller vessel as at 13 November 1919, that being the date the contract was entered into, not the date when the larger vessel should have been provided.

We are told the shortfall in cubic capacity was discovered when the ship was "*loaded*" yet the owners are said to have "*suspected that Messrs. Graham & Co. had no cargo to load*". Presumably what the owners were alleging was that all the charterer's intended cargo was successfully loaded and there was none left over. But the owners might have been saying the charterer had no cargo at all, so that the ship lay idle for the duration of the charter. The documents which the owners requested, to show whether there was a cargo to load, do not seem to have been before the arbitrator, but they were apparently before the court. The judge said, cryptically, that these documents: "*were only further admissions by the charterers of a statement which they had candidly put before the Court showing that in one event the damages would be merely nominal*". So it is entirely unclear what cargo the claimant (the charterers) had, and whether it was all successfully loaded.

The court went on the find, however, that it simply did not matter whether the claimant had any cargo. Shearman J concluded (<u>emphasis</u> added):

> "*Now comes the question whether the Umpire was right in his award. I am clearly of opinion that he was. In the Charter-party there was a warranty as to deadweight capacity and the cubic capacity. The latter was wholly wrong. The charterers' contention is that if they had wanted to hire a smaller ship they could have got it for £2000 less. It did not matter in the least when they entered into the contract what was the purpose for which they wanted the ship, or what was the cargo they wanted to put in it. They might have wanted to sub-let it. If they had wanted a ship of that capacity they could have got it cheaper. <u>In the events that happened it did not matter that they might not have got a cargo to fill up the ship. That was something that happened after the bargain</u> which was not contemplated by the parties. The contract was entered into on the basis that the charterers wanted a ship of the size guaranteed. There is no question that <u>in the case of a sale</u> the measure of damages is perfectly clear. It is the difference in market value. If you buy a ship of a certain cubic capacity, and one of less cubic capacity is tendered, you can deduct the difference in value from the price. <u>I am unable to see that there is any difference in the case of a hiring</u>. The true measure of damages is the difference in the value of the ship, and on that the Umpire has awarded £2000*

© 2021 Haynes and Boone, LLP

> *damages. I think he is right, and I uphold the award with costs.*"

According to Shearman J, then, the charterer had an absolute right to damages equal to the difference in value between the smaller vessel and the larger one, irrespective of whether the charterer would have used the 'missing' capacity if the larger vessel had been supplied.

In order to arrive at this result, Shearman J seems to have presumed: (i) that the charter – a contract of hire – was meaningfully analogous to a contract for the sale of goods; and (ii) that, when a seller of goods 'skimps' on performance and delivers a lesser quantity or lower quality of goods, then the buyer has an absolute entitlement to damages equal to the difference in market value as at a particular date, with subsequent events to be disregarded.

This reasoning is flawed, for reasons discussed below. But before considering why that is so, it makes sense first to consider some other, similar, decisions.

1920 - *Sterns*

Sterns was decided in 1920, the same year as *Tibermede*. The case was broadly the same. An owner supplied a charterer with a vessel which was smaller than had been warranted in the charter. An arbitrator awarded the charterer the difference between the contract price and the market rate for the smaller vessel. On appeal the owner argued that damages should instead be calculated by reference to what cargo the claimant was actually prevented from carrying. The court, however, dismissed the appeal and upheld the award. The judgment is a single line: "*It is on all fours with* [*Tibermede*] *and the award must stand*".

As with *Tibermede* the facts of the case – what the vessel actually carried, and what it would have carried if it had been as warranted – are not really clear. The court, and the arbitrator, do not seem to have made any findings as to those matters, proceeding on the assumption that the charterer was entitled, as of right, to the difference between the contract price and the market rate for the smaller vessel, irrespective of what the vessel would actually have carried.

1982 - *TFL Prosperity*

In *TFL Prosperity,* the charterer chartered a roll-on roll-off vessel called the *TFL Prosperity*. The charter stated the vessel's dimensions, including the free height on the main deck. The charterer had intended to ship MAFI-type trailers double stacked with 40ft containers there, but the height proved to be less than was stated, preventing the charterer from shipping double stacked trailers. The charterer claimed the loss of freight – i.e. the extra revenue it would have earned if it had been able to ship double stacked containers. The arbitrator awarded damages on that basis.

The owner challenged that award, arguing that this was the wrong measure. Citing *Tibermede* and *Sterns* the owner argued "[i]*t was very well-established that, in the case of a breach of warranty as to the cargo capacity of a ship, the measure of damages was the difference between the rate of hire payable on the market at the date of the charter for a ship complying with the warranty and for one of the actual capacity of the ship chartered*". Bingham J rejected this, saying (at 624):

> "*… the rule is only a prima facie rule and it can be no more than that given the underlying object of any rule of damages. If on the facts before it a tribunal concludes that application of a prima facie rule will not compensate an injured party who has shown himself to have suffered loss of a*

© 2021 Haynes and Boone, LLP

> *sufficiently proximate kind, then a departure from the rule is warranted.*"

The substantive result is entirely correct. The charterer was awarded its real loss – the difference between the freight it earned and the freight it would have earned if the vessel had been as warranted.

The problem with *TFL Prosperity* is that Bingham J only recognises the possibility of departing from the (supposed) "*prima facie rule*" if applying it would undercompensate the injured party. What is to happen if applying the rule will overcompensate the injured party? The judges in *Tibermede* and *Sterns* evidently thought that one should not depart from the rule in that scenario. Their view was that the charterer was entitled to the difference between the contract price and the charter rate for the smaller vessel as of right, even if the shortfall in capacity had not caused them any loss. Hence why they did not enquire as to whether the charterer would have shipped anything different if the ship was as warranted. *TFL Prosperity* leaves that aspect of the *Tibermede* and *Sterns* judgments undisturbed.

Treatment of these cases in the practitioner texts

Citing *Tibermede* and *Sterns, Time Charters* (7th Ed. (2014) says, at 3.38 (<u>emphasis</u> added):

> "*In some cases, the misdescription of a ship <u>may not cause a specific loss</u>, or the charterers <u>may not be able to show that they have suffered any specific loss</u>. Nevertheless, the ship's failure to match its description <u>may still amount to a real impairment of the ship's value</u> to the charterers. In such cases, the charterers are entitled to claim damages measured as the difference between the hire agreed and the hire that would have been payable for the ship if accurately described. This measure of loss has been applied, for example, in a case of misdescription of the ship's cubic capacity.*"

The editors take the ratio of *Tibermede* to be that if a misdescription does not "*cause a specific loss*" but there is nonetheless "*a real impairment of the ship's value to the charterer*" then the charterers "*are entitled*" to claim the difference in market value.

It is unclear where this distinction between "*specific loss*" and "*real impairment of … value*" is thought to originate from. It does not form any part of the judgments in *Tibermede*, *Sterns* or *TFL Prosperity*. In practice it is hard to draw any distinction between "*loss*" and "*real impairment of … value*". The "*value*" of a chartered vessel to a charterer is just the revenue it generates during the charter term. So in most cases a vessel's value is "*impaired*" if it generates less revenue and if the vessel generates less revenue, the charterer suffers "*loss*". If a vessel can, in fact, generate the same revenue with the defect as without, then its value to the charterer is unimpaired by the defect.

Admittedly, there may be some cases where it is meaningful to speak of value being impaired despite the revenue generated being the same. A tour operator charters a cruise liner and some defect in the vessel makes the voyage less pleasant for the passengers and crew but the vessel does not generate any less revenue – the guests have paid up-front and the defect is not one which entitles them to any compensation. The tour operator nonetheless suffers some bad reviews and loss of goodwill, potentially reducing revenue earned on subsequent tours using other vessels. In that scenario it seems meaningful to say the vessel was less valuable, despite being unable to point to a specific loss.

Another example might be where the defect in the vessel is that some element of safety equipment is not as warranted - perhaps the vessel has fewer lifeboats or lifejackets than the contract had specified. The vessel does

© 2021 Haynes and Boone, LLP

not sink during the charter, so these defects do not cause any loss (physical, financial, reputational). But one would probably accept that there had nonetheless been a real impairment of the ship's value to the charterer (as well as potentially placing the charterer in breach of safety requirements).

The defects in *Tibermede*, *Sterns* and *TFL Prosperity* were not defects of these kinds, though. In each case, there was simply a shortfall in the vessel's capacity compared to what had been warranted. The only way a shortfall in cargo capacity could impair a ship's value would be if it prevented the charterer carrying some cargo which the charterer would otherwise have carried.

Citing *Tibermede*, *Sterns* and *TFL Prosperity*, *Scrutton on Charterparties and Bills of Lading* (24th Ed) says, at 20-030 (emphasis added):

> "*Where, under a charter there is a breach of a guarantee of the ship's deadweight or carrying capacity, the prima facie measure of damages is the difference between the rate of hire or freight payable on the market at the date of the charter for a ship complying with the guarantee and for one of the actual capacity of the ship chartered. This is only a prima facie rule; if its application will not compensate an injured party, who has shown himself to have suffered loss of a sufficiently proximate kind, a departure from the rule is warranted*."

As in *TFL Prosperity*, the question of whether one can also depart from the supposed *prima facie* rule where its application will overcompensate the injured party is left open. The difference in market price is acknowledged to be only a *prima facie* measure. If the claimant can prove it would have made a profit from the extra capacity, and not merely broken even, then it will be awarded damages to compensate it for that loss.

1995 - *White Arrow*

In 1995 Bingham J, now Bingham MR, gave the leading judgment in *White Arrow*, an appeal in another case involving skimped performance of a commercial contract purely for services. There was no reference to *Tibermede*, *Sterns* or *TFL Prosperity* in that judgment. The claimant in *White Arrow* was a mail order business which for several years had used the services of the defendant, a road transport contractor, to deliver the claimant's goods. The claimant had then entered into a new contract with the defendant, under which the defendant had agreed to provide an 'enhanced service' for which the claimant was to pay a higher price than before. The enhancements consisted of delivery drivers wearing special uniforms, calling ahead to ascertain whether customers were in and removing packaging from customers' premises. In the event, the defendant delivered the 'basic' service as before (i.e. delivered the parcels) but failed, to some extent, always to provide the 'enhanced' service.

The case hinged on a point of pleading. The claimant had calculated what part of the price related to the enhanced services which had not been performed and claimed that amount. A preliminary issue arose as to whether the claimants were entitled to recover on that basis. The judge at first instance characterised the claim as being for "*repayment of part of the price which they have paid*" and so "*a claim in quasi-contract based on partial failure of consideration and not … a claim for damages for breach of contract*". Rather than claiming damages for breach of contract, the claimant was seeking to claim restitution of an unjust enrichment.

The problem (not stated expressly in the judgment) is that a claim for unjust enrichment requires a total failure of consideration and does not arise where there is only a partial failure. *Per* Lord Porter in *Fibrosa Spolka Akeyjna* v *Fairbairn Lawson Combe Barbour Limited* [1943] AC 32:

© 2021 Haynes and Boone, LLP

"*Money had and received to the plaintiff's use can undoubtedly be recovered in cases where the consideration has wholly failed, but unless the contract is divisible into separate parts it is the whole money not part of it, which can be recovered. If a divisible part of the contract has wholly failed and part of the consideration can be attributed to that part, that portion of the money so paid can be recovered, but unless this be so there is no room for restitution … A partial failure of consideration gives rise to no claim for recovery of part of what has been paid.*"

In *White Arrow* there had been only a partial failure of consideration. The contract was not 'divisible'. The enhanced service was not a distinct, separable part of the contract. It was not possible to perform the enhanced services (calling ahead, removing packaging) separately from the 'basic' service (delivering the goods). Thus a claim in unjust enrichment could not succeed. The judge at first instance held that the claimants were not entitled to recover on the pleaded basis and the Court of Appeal upheld that. Bingham MR did, however, make the following *obiter* comment:

"*It is … obvious that in the ordinary way a party who contracts and pays for a superior service or superior goods and receives a substantially inferior service or inferior goods has suffered loss. If A hires and pays in advance for a 4-door saloon at £200 per day and receives delivery of a 2-door saloon available for £100 per day, he has suffered loss. If B orders and pays in advance for a 5-course meal costing £50 and is served a 3-course meal costing £30, he has suffered loss. If C agrees and pays in advance to be taught the violin by a world-famous celebrity at £500 per hour, and is in the event taught by a musical nonentity whose charging rate is £25 per hour, he has suffered loss. It is irrelevant whether A, B or C might have been entitled to reject the goods or services tendered if they in fact accept them. It would defy common sense to suggest that A, B and C have suffered no loss, and are not financially disadvantaged by the breach. The measure of damage in each of these cases is the difference between the price paid (or, if it is lower, the market value of what was contracted for) and the market value of what was obtained.*"

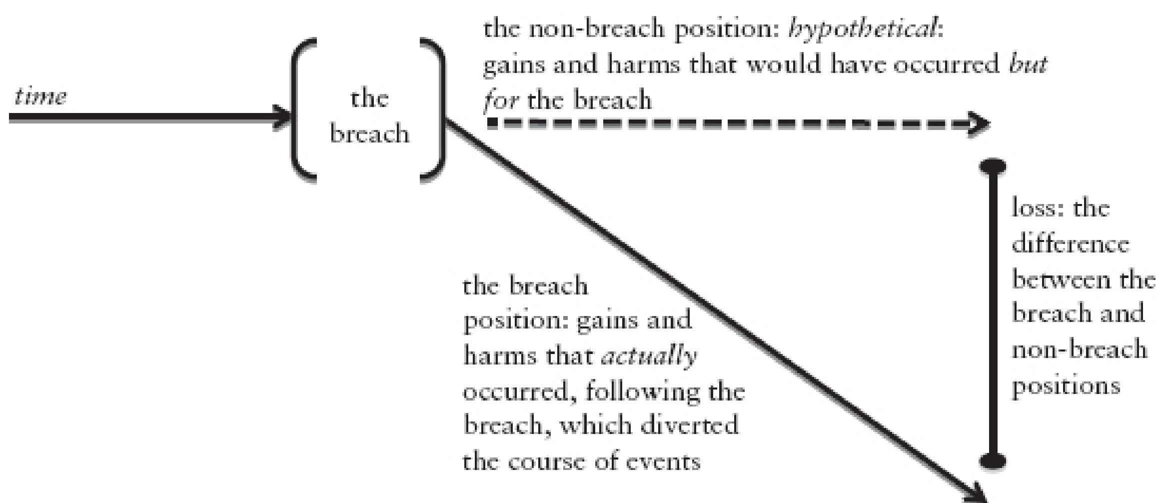
If it was true that the claimant would properly have been entitled to "*the difference between … the market value of what was contracted for … and the market value of what was obtained*" then the result seems hard on the claimant. The claimant had identified what part of the price related to the services received, and what part related to the missing enhanced services. The claimant's sole mistake seems to have been to fail to say in terms that those prices were also the 'market values' of the associated services. One might have thought that was implicit. At least one person (the claimant) had demonstrably been willing to pay these prices for these services and so, absent other evidence, that was the 'market value of the services. Bingham MR did say "*It may … be … that they can re-formulate their claim so as to found a claim for substantial damages*". Whereas in *Tibermede* Shearman J derived a right to claim difference in market value by way of an (inapt) analogy with contracts for the sale of goods, Bingham MR did so by way of an analogy with what might be termed 'non-commercial' transactions, where the services were purchased with a view to securing some non-financial benefit – pleasure, utility or safety.

Breach and non-breach positions

The purpose of contract damages, as stated in *Robinson* v *Harman* and affirmed by the House of Lords / Supreme Court in *The Golden Victory* and *Bunge* is "*so far as money can do it, to be placed in the same situation, with respect to damages, as if the contract had been performed*".

Kramer (*The Law of Contract Damages* 2nd Ed. at 1-47) usefully characterises the process of assessing damages for breach contract as consisting of a comparison between a 'breach position' and a counterfactual 'non-breach position', as illustrated in his diagram below.

© 2021 Haynes and Boone, LLP



For a judicial expression of this same idea, see *Stephenson Blake (Holdings) Ltd* v *Streets Heaver Ltd* [2001] Lloyd's Rep PN 44:

> "*159. … an inquiry into damages should … normally take the form of a comparison, in financial terms, between the events which have actually happened and those which would have happened had the relevant breach not occurred …*"

The second stage in the enquiry

In *BPE Solicitors & Anor* v *Hughes-Holland (in substitution for Gabriel) (Rev 1)* [2017] UKSC 21 at paragraph 20 Lord Sumption (with whom Lords Neuberger, Mance, Clarke and Hodge agreed) said:

> "*It is generally a necessary condition for the recovery of a loss that it would not have been suffered but for the breach of duty. But it is not always a sufficient condition. The reason … is that the law is concerned with assigning responsibility for the consequences of the breach, and a defendant is not necessarily responsible in law for everything that follows from his act, even if it is wrongful. A variety of legal concepts serves to limit the matters for which a wrongdoer is legally responsible. …*"

In *Tiuta International Ltd (in liquidation)* v *De Villiers Surveyors Ltd* [2017] UKSC 77 Lord Sumption (giving the unanimous judgment) said:

> "*The basic measure of damages is that which is required to restore the claimant as nearly as possible to the position that he would have been in if he had not sustained the wrong. This principle is qualified by a number of others which serve to limit the recoverable losses to those which bear a sufficiently close causal relationship to the wrong, could not have been avoided by reasonable steps in mitigation, were reasonably foreseeable by the wrongdoer and are within the scope of the latter's duty. In the present case, we are concerned only with the basic measure …*".

An enquiry as to damages, then, has two stages. First there is factual, 'but for' (*sine qua non*) causation (what Lord Sumption here calls the 'basic measure' and the 'necessary condition'). As a matter of fact, and on the balance of probabilities, how would the claimant's position have differed if the contract had been performed? If

© 2021 Haynes and Boone, LLP

the answer is that it would be no different, or worse, then the breach has not caused any loss and the claimant is not (generally) entitled to anything but nominal damages. If the breach did cause a loss in the factual 'but for' sense it is then necessary to proceed to the next stage. Does the law require that any of the losses (or gains) which make up the claimant's breach position be disregarded? Lord Sumption references several legal concepts which can cause gains or losses to be disregarded. The relevant concept for the purpose of this article is mitigation.

Factual causation and the presumption of breaking even

In deciding what the non-breach position would have been, as part of the initial, factual, enquiry English law applies what has been called (by Kramer *The Law of Contract Damages* 2nd Ed. At 18-59) a 'presumption of breaking even'. The law presumes that if the defendant had rendered the missing performance, then the value of that performance would have been sufficient to recoup any costs the claimant incurred to secure that performance. The law presumes, in other words, a 'neutral' bargain. If the claimant considers that this was not merely a 'neutral' bargain but a 'good' one – that they would have received more value – then the burden is on the claimant to prove that. If the defendant considers that this was not even a 'neutral' bargain, but was in fact a 'bad' one, where the claimant would have received less value, then the burden is on the defendant to prove that.

The presumption finds its clearest judicial expression in *Yam Seng Pte Ltd* v *International Trade Corp Ltd* [2013] 1 Lloyd's Rep 526 at 190 where Leggatt J referred to a "*(rebuttable) presumption that the claimant would have recouped expenditure incurred in reliance on the defendant's performance*" and "*where money has been spent in that expectation* [of making a profit] *but the defendant's breach of contract has prevented that expectation from being put to the test, it is fair to assume that the claimant would at least have recouped its expenditure had the contract been performed unless and to the extent that the defendant can prove otherwise*".

Why have a presumption of breaking even?

Why have a presumption of breaking even? In *Yam Seng* it is said to be because it is "*fair*" - the defendant's conduct has prevented the expectation being put to the test. But there is potentially a better explanation. The court's aim is to discover the 'truth' of what would have happened if the contract had been performed, in so far as one can apply that word to a counterfactual enquiry. What matters is not fairness but *accuracy* (or, at least, cogency and plausibility). In seeking to form an accurate counterfactual picture, the contract price is a known fact to which we assign a lot of weight, not because it is *fair* to do so, but because the contract price is genuinely highly probative. In every case, conveniently for the judge, someone who was familiar with, or even expert in, the subject matter of the transaction has already made a careful assessment as to what the value of that promised performance would be. That person, of course, was the claimant. And – since they entered into the contract – they demonstrably concluded that the value would exceed, or at least be equal to, the price. That assessment was formed at a time when the claimant had not yet entered into the contract, so had a strong incentive to make an accurate assessment. The presumption of breaking even thus represents a useful shortcut or heuristic – piggybacking on the work which a relatively-expert claimant has already done in assessing the value of the promised performance.

Presumption of breaking even applied to a *Tibermede* type case

In *Tibermede*, the charterer had not paid the charter hire – it was defending a claim by the owners, seeking payment. The arbitrator had determined that the full amount of the hire was properly payable according to the terms of the charterparty. The hire, then, was a cost which the charterer had incurred, or at least had incurred the liability to pay. The correct approach to the charterer's counterclaim would therefore have been to work out what

© 2021 Haynes and Boone, LLP

part of that price represented the 'missing' capacity. One way to do that might be to simply use the difference between the contract price for the larger vessel and the market price for the smaller vessel as at the date of the contract.

That approach seems to make less sense, though if the contract price for the larger vessel was much higher, or much lower, than the market price for the larger vessel. Suppose the charterer had hugely overpaid for the larger vessel, or had obtained a bargain. In such a case, part of the difference between the price of the bigger vessel and market value of the smaller one does not represent a payment for additional capacity – it is simply the overpayment or underpayment. In such a case, the better approach is arguably to compare the market price of a bigger vessel and a smaller vessel at the contract date, and apply the same proportions *pro rata* to the contract price.

Having worked out what the charterer paid for the 'missing' capacity, the charterer would then seek to claim that amount as damages for breach of contract, relying on the presumption of breaking even, and being careful to couch the claim in those terms, and not as seeking restitution for a partial failure of consideration. An example of a similar claim having succeeded, albeit not in a pure service case, is *Playup Interactive Entertainment (UK) Pty Ltd* v *Givemefootball Ltd* [2011] EWHC 1980 (Comm). There the claimant paid for contact details of around 1 million people, but the defendant supplied only a proportion. The court awarded a corresponding proportion of the contract price as damages, apparently applying the presumption of breaking even (see paragraph 272 in that judgment: "*PlayUp's approach proceeds upon the assumption that the Sponsorship Agreement was worth what PlayUp paid for it. There is no suggestion by GMF that this is an inappropriate assumption.*").

The burden would be on the owner to prove that, in fact, the charterer would not have 'broken even' on what it paid for the 'missing' capacity, because the charterer had no cargo which it could have carried in that space, and so the price paid for that space would always have been wasted. Given proper disclosure, and the opportunity to cross-examine the charterer's witnesses, one might have thought it would be relatively easy to prove that, if it was true. The court in *Tibermede* never made any finding as to what cargo would have been carried if the vessel had been as warranted, because they considered it to make no difference.

The presumption as applied to non-commercial contracts

Yam Seng refers to the presumption as applying when contracts are entered into in the expectation of making a profit, and when the benefit of the contract is monetary (recouping expenditure). But the same logic applies to contracts which are entered into for other purposes. In *The Royal Devon and Exeter NHS Foundation Trust* v *ATOS IT Services UK Ltd* [2017] EWHC 2197, an NHS trust (a public healthcare provider not seeking to make a profit) retained a contractor to supply an electronic system for managing patients' health records. The Trust later terminated that contract and claimed damages based on its wasted expenditure. The court (O'Farrell J) observed:

> "*The burden of proof lies on the defendant to show that the expenditure would not have been recouped and would have been wasted in any event: … In the case of a contract where no financial gains were expected, the recoupment in question would not be payments but alternative gains, such as use or enjoyment. To establish a bad bargain in such a case, the defendant would have to show that the value of the asset or other performance promised was less than the expenditure incurred by the claimant.*"

When the purpose of the contract was not to make a profit or save expense, but to procure utility or subjective enjoyment, it is going to be difficult to rebut the presumption of breaking even, and show the utility / enjoyment would have been worth less than the price. The presumption thus explains why the hypothetical consumers

© 2021 Haynes and Boone, LLP

referred to by Bingham MR in *White Arrow*, who purchase meals, or piano lessons or hire cars, will typically recover the difference between what was promised and what was received. It is simply that, in such cases, the defendant will find it hard to rebut the presumption and prove that the pleasure one would have derived from the missing courses or lessons would not have been worth the price. This reason does not apply in commercial cases. It is suggested that Bingham MR was wrong to say, in *White Arrow*, that the award based on the market value in these hypothetical consumer cases supports making similar awards in commercial cases.

In the Court of Appeal judgment in *HM Attorney General* v *Blake* [1997] EWCA Civ 3008, Lord Woolf discussed a decision of the Louisiana Court of Appeal called *City of New Orleans* v *Firemen's Charitable Association* 9 So 486 (1891), which Lord Woolf apparently considered would have been decided differently as a matter of English common law (emphasis added):

> "*The defendant contracted with the plaintiff to provide a firefighting service and was paid the full contract price. After the expiry of the contract the plaintiff discovered that the defendant had not provided the stipulated number of firemen or horses or the promised length of hosepipe. The defendant had saved itself substantial expense by that breach, but had not failed to put out any fires in consequence. The court ruled that the plaintiff had not proved it had suffered any loss and was unable to recover more than nominal damages. Justice surely demands an award of substantial damages in such a case, and the amount of expenditure which the defendant has saved by the breach provides an appropriate measure of damages. This could be achieved by presuming that the plaintiff has suffered a loss of an amount corresponding to the amount by which he has been overcharged for the service actually provided; and the presumption could be justified by invoking the notion of "the consumer surplus."*"

Again, the result argued for by Lord Woolf can be justified by reference to the presumption of breaking even. The City was not just buying these services to secure that any such fires as actually occurred were put out, and to save its citizens the associated financial losses. Rather, the City wanted to put in place a particular safety mechanism – the ability to put out up to X number of fires whether they occurred or not, and to purchase for its citizens the peace of mind and voter satisfaction and other benefits (such as lower insurance premiums) associated with having in place that safety mechanism to prevent both financial losses and personal injury. There are lots of public services which are like this – they provide against a contingency which might not occur during the contract period. Examples include contracts to guard defence facilities and nuclear power stations against terrorist attack, contracts to clear rivers of foliage which might cause flooding in extreme weather, contracts to remove trees near rail and power lines, and so on. When a defendant skimps on these services, we award the claimant the price paid for the missing services, because the defendant cannot rebut the presumption that the non-financial benefit (security, peace of mind) was at least worth the contract price. The same considerations would apply where a charter vessel was supplied with too few lifeboats or lifejackets, or a hire car which had been described as having airbags, did not. The hirer would be entitled to the difference in market value between what was contracted for and what was received because in each case the defendant would fail to prove that the benefit – security, peace of mind – was not worth the price paid for it.

The 'duty' to mitigate

The presumption of breaking even forms part of the initial factual enquiry. If no loss is identified at that stage, then it is unnecessary to proceed to the next stage, and consider whether any of the losses and gains which make up the breach position require to be disregarded. In *BPE Solicitors* Lord Sumption gave as an "*example of a legal filter which serves to eliminate certain losses from the scope of a defendant's responsibility*" "*the rule that the defendant cannot be held liable for losses that the claimant could reasonably have been expected to avoid*".

© 2021 Haynes and Boone, LLP

English law does not permit claimants to recover damages in respect of losses they could reasonably have avoided. See, for example, Lord Toulson (with whom Lords Neuberger, Mance and Clarke agreed) in *Bunge SA* v *Nidera BV* [2015] UKSC 43 paragraph 81:

> "*… the so-called duty to mitigate … is an aspect of the principle of causation that the contract breaker will not be held to have caused loss which the claim could reasonably have avoided …*"

Mitigation and sale of goods

A claimant contracts to buy goods. The defendant 'skimps' on performance and delivers something less than was contracted for (whether that is a lesser quantity or a lower quality). The nature of the goods is such that substitute goods are available in the market. Commodities, like oil or grain, are common examples of goods which can usually be substituted. But the same is also true of many other, more complicated, mass-manufactured goods, like cars and refrigerators. The reasonable thing for the claimant to do, in such a case, is to go to the market, sell any non-compliant goods they received at market price and buy the thing they contracted for at market price. The claimant will then have what they contracted for, and the difference between the breach position and the non-breach position is purely financial – the additional net cost incurred to achieve that.

When that is the reasonable thing to do, the law deems the claimant to have done it, and so that is the 'breach position'. The claim is thus for the difference between the market value of what was received (nothing, or some goods of lesser quality) and the market value of what was promised. These common law principles are reflected in Sections 51 and 53 of the Sale of Goods Act.

> "***51 Damages for non-delivery.***
>
> *(1) Where the seller wrongfully neglects or refuses to deliver the goods to the buyer, the buyer may maintain an action against the seller for damages for non-delivery.*
>
> *(2) The measure of damages is the estimated loss directly and naturally resulting, in the ordinary course of events, from the seller's breach of contract.*
>
> *(3) Where there is an available market for the goods in question the measure of damages is prima facie to be ascertained by the difference between the contract price and the market or current price of the goods at the time or times when they ought to have been delivered or (if no time was fixed) at the time of the refusal to deliver.*"
>
> "***53 Remedy for breach of warranty.***
>
> *(2) The measure of damages for breach of warranty is the estimated loss directly and naturally resulting, in the ordinary course of events, from the breach of warranty.*
>
> *(3) In the case of breach of warranty of quality such loss is prima facie the difference between the value of the goods at the time of delivery to the buyer and the value they would have had if they had fulfilled the warranty*."

In *Bunge,* the Supreme Court confirmed that these *prima facie* rules are just that – presumptive, *prima facie* rules. They do not confer an absolute right, always to be awarded the difference in market price, assessed at the time of delivery, come what may:

© 2021 Haynes and Boone, LLP

"*Sections 50 and 51 … reflect common law principles … Section 51(2) states the compensatory principle in the context of a seller's non-delivery. Subsection (3) states the prima facie measure of damages where there is an available market, but it is not so much a rule as a technique which is prima facie to be treated as satisfying the general principle expressed in subsection (2).*"

"*… where there is an available market for the goods, the market price is determined as at the contractual date of delivery, unless the buyer should have mitigated by going into the market and entering into a substitute contract at some earlier stage: … Normally, however, the injured party will be required to mitigate his loss by going into the market for a substitute contract as soon as is reasonable after the original contract was terminated. Damages will then be assessed by reference to the price which he obtained. If he chooses not to do so, damages will generally be assessed by reference to the market price at the time when he should have done: … The result is that in practice where there is a renunciation and an available market, the relevant market price for the purposes of assessing damages will generally be determined not by the prima facie measure but by the principles of mitigation.*"

Admittedly, in spite of *Bunge*, the erroneous idea that there is, in effect, an absolute right to claim the difference in market value at the time of breach seems to have a long half-life. A particularly egregious example is *OMV Petrom SA* v *Glencore International AG* [2016] EWCA Civ 778. A buyer contracted to buy a quantity of 'branded' crude oil. Oil was delivered. The buyer sold it to a subsidiary, which refined the oil and sold the resulting products. A decade later the buyer discovered it had been the victim of a fraud – the oil sold as branded oil had in fact been 'unbranded' oil. The market value of the unbranded oil at the time of delivery would have been $40 million less than that of branded oil, because of uncertainty about the unbranded oil's quality/composition and whether it might damage a refinery. In the event, the unbranded oil had not caused any damage. The only difference compared to if the oil had been branded oil was that the yield was slightly lower, and so the distillate product had been worth $5.5 million less. The correct analysis, then was:

Breach position	Non-breach position
Buyer receives U oil believing it to be B oil	Buyer receives B oil
Buyer sells oil to subsidiary for $X as B oil	Buyer sells oil to subsidiary for $X as B oil
Subsidiary refines oil and sells distillate for $Y	Subsidiary refines oil and sells distillate for $Y+5.5 million

The only difference between the breach and non-breach position was that, in the breach position, the buyer had a $5.5 million liability to its subsidiary so, applying *Robinson* v *Harman*, the buyer should have been awarded damages in that amount (or an indemnity for that liability). Instead, the buyer was awarded $40 million for the difference in market price between branded and unbranded oil at the date of delivery. This did not put the buyer in the position it would have been in if the seller had delivered branded oil as promised. Rather, it placed the buyer in the position which the buyer would have been in if it had entered into a ***different*** contract, and agreed to purchase branded oil instead of unbranded oil for $40 million less. For a comprehensive debunking of the decision see Andrew Summers (2017) *Deceit, difference in value and date of assessment.* Law Quarterly Review, 133. pp. 41-46.

The analogy with sale of goods is inapt

Returning now to the *Tibermede* against the background of these legal principles, it can be seen that the analogy which Shearman J drew between the charter and a contract for sale of a ship is inapt for several reasons. The

© 2021 Haynes and Boone, LLP

only reason why difference in market value is awarded for sale of goods with an available market is because of the logic of mitigation – because, when there is an available market, the reasonable thing to do is to sell the non-compliant goods and buy replacements. If a buyer had bought the *Tibermede*, and found her to be smaller than warranted, the reasonable thing would have been to sell her and buy a ship of the relevant size, and claim the difference. But we only need to resort to the logic of mitigation at the second stage of the enquiry – if we have passed the first hurdle, and determined at the factual, but-for stage that a loss has occurred. The charterer's claim in *Tibermede* never passes that first hurdle. The smaller ship carried all the cargo. A larger ship would have carried the same cargo. The charterer was already in the same situation as if the contract had been performed. No money was needed to place him there.

When a defendant 'skimps' on pure services, it will rarely be practicable, let alone reasonable, to buy substitute services. When the charterer came to load the *Tibermede*, and found it was too small, that was only a breach of warranty. The charterer would not have been entitled to terminate, reject the smaller vessel and hire a bigger vessel, of the size promised. In any case, if the charterer's cargo was in fact going to fit on the smaller vessel, it would hardly have been reasonable to reject it and hire a bigger one. Even if it was lawful and reasonable to reject the small vessel and hire a bigger one, the charterer's loss would then have been the difference between: (i) the contract price for the big vessel; and (ii) the market price to hire the big vessel, sometime after the shortfall in capacity was discovered. However, the charterer in *Tibermede* was awarded the difference between: (i) the contract price for the big vessel and (ii) the market price for the small vessel, at the date of the contract.

The analogy with sale of goods is even less relevant in a *White Arrow* type case. The parcels had been delivered. The moment for performing the enhanced services – calling ahead, disposing of packaging – had passed. It was not just unreasonable to purchase substitute services – it was impossible. The court's other error in *Tibermede* was to assume that, under a sale of goods contract, skimped performance by the seller gives rise to an absolute, irrebuttable right to claim the difference in market value between what was received and what was provided, assessed at a particular point in time and without regard to what happened thereafter. That is wrong, and *Bunge* confirms that. The effect of the award in *Tibermede* was not to place the charter in the position it would have been in if the contract had been performed, but to place the charterer in the same position as if the parties had entered into a ***different*** contract, and the charterer agreed to hire a smaller vessel for a lower price.

Besides *Tibermede* there is one other case where a court seems to have relied on an analogy with sale of goods to argue in favour of market value damages for skimped performance of a pure services contract. In the House of Lords judgment in *Blake* ([2000] UKHL 45), Lord Nicholls suggested (in a short *obiter* remark):

> "*If a shopkeeper supplies inferior and cheaper goods than those ordered and paid for, he has to refund the difference in price. That would be the outcome of a claim for damages for breach of contract. That would be so, irrespective of whether the goods in fact served the intended purpose. There must be scope for a similar approach, without any straining of principle, in cases where the defendant provided inferior and cheaper services than those contracted for.*"

The reference to a "*shopkeeper*" implies that what Lord Nicholls had in mind when he drew this analogy may have been the provision of services to consumers, rather than to businesses. As explored above, when the contract is a consumer contract (or, more generally, the services are intended to render some non-financial benefit) difference in market value will often fall to be awarded by operation of the presumption of breaking even, but the same will not always be true in a commercial setting.

2010 – *Giedo Van Der Garde*

© 2021 Haynes and Boone, LLP

In the first instance case *Giedo Van Der Garde BV & Anor* v *Force India Formula One Team Ltd* [2010] EWHC 2373, the claimant paid for practice laps in a Formula One car with a view to improving his chances of becoming a Formula One driver. The defendant failed to provide some of the laps. *Pro rata*, the contract price paid for the missing laps was $1.865 million. The financial return which the missing laps would have provided for the claimant was highly speculative. Had the claimant received the missing laps his small chance of becoming a professional F1 driver, and of receiving the stellar earnings associated with that career, would have increased slightly. The court valued that lost chance at $100,000. In purely commercial terms, then, the claimant had made a bad bargain – paying $1.865 million for laps with an expected average return of $100,000.

The court nonetheless awarded the claimant $1.865 million, said to have been the 'market value' of the missing laps, relying upon *White Arrow* and *Blake*. *Giedo Van Der Garde* is thus sometimes cited as an example of a commercial contract for pure services where a court has actually awarded difference in market value for 'skimped' performance. *Giedo Van Der Garde* is, however, hard to characterise as a purely 'commercial' contract. The missing laps had a subjective, non-pecuniary value for the claimant in the sense that, having driven them, he would have had the satisfaction of knowing he had thereby given it his best shot, and have been spared forever having to wonder whether he might have succeeded in his chosen career if only he had received the missing laps. *Tibermede* and *Sterns* by contrast, are clearly cases where courts awarded difference in market value for breaches of commercial contracts for pure services. Their simple facts help to illustrate, more starkly than *Giedo Van Der Garde*, the error which is committed when damages are awarded on such a basis.

Conclusion

Tibermede was wrongly decided, the reasoning does not stand up to scrutiny and should not be followed. Such cases should be decided according to the normal principles which govern contract damages, and there is no good reason to import a special rule for when the cargo capacity of a vessel is misdescribed in a charter. Neither the analogy with sale of goods (in *Tibermede*), nor the analogy with non-financial contracts (in *White Arrow*), justify awarding a claimant, as of right, the difference between the market price of what was promised and what was received in a case where a defendant has skimped on performance and pure services, and the claimant purchased the services with a view to making profit or saving expense.

© 2021 Haynes and Boone, LLP