JUDGMENT : The Honourable Mr Justice Langley : Commercial Court. 16th December 2005

INTRODUCTION

1. This is an Arbitration Appeal, under Sections 69(2) and (3) of the Arbitration Act 1996, brought by the Claimants with the permission of Morison J granted on 26 May 2005. Such an appeal has, of course, to be on a question of law arising out of the Award or Awards.

THE CLAIMS

2. The Claimants were the Buyers and the Respondents the Builders under four shipbuilding contracts executed on 23 February 2003, each for one vessel, a 53,800 DWT bulk carrier, at a price of US$ 17,970,000 per vessel. The Buyers are companies incorporated in the Marshall Islands. They were all managed by Enterprises Shipping and Trading SA ("EST") a company with its principal place of business in Athens. Their brokers were Barry Rogliano Salles ("BRS"). The Builders were founded as a private company in the People's Republic of China (PRC) in 2002. Their brokers were Asia Shipping International ("ASI").

3. The Buyers made claims for damages for breach of the contracts. They alleged the Builders had repudiated the contracts.

THE AWARDS

4. The claims were referred to arbitration. The arbitrators were Anthony Diamond QC, Anthony Hallgarten QC and Mr Philip Yang. The Builders raised jurisdiction issues. They denied that any binding contracts had been concluded. Those issues were resolved in favour of the Buyers in four Awards (one in respect of each contract) dated 11 January 2005. But, to quote from paragraph 178 of the Reasons for Award ("the Reasons"):

   "(c) The contracts are not void for uncertainty but the binding effect of the contracts was dependent upon the parties being able and willing to reach agreement on the supplier of the main engines and on their being able and willing to fulfil the other conditions set out in para (b) of Art(icle) 21 within the prescribed time.

   (d) The contracts have been automatically rescinded under the provisions of para(graph) (b) of Art(icle) 21 due to the conditions set out in that paragraph not having been met and accordingly the parties have been discharged from their obligations duties and/or liabilities under the contract(s).

   (e) The issue of repudiation does not arise and neither party is liable to the other for any loss sustained as a result of the non-performance of the contract(s)."

5. The Buyers, for those reasons, failed in their claims.

ARTICLE 21

6. The relevant issues on this appeal all arise from Article 21(b) of the contracts. The wordings of the Articles in the Pioneer and Explorer Contracts were identical. The wordings of the Covington and Washington Contracts were (so far as material) identical save that in the introductory words of paragraph (b) and in paragraph (b)(v) of Article 21 the time periods were stated to be three and six calendar months respectively and not 20 banking days.

7. The wording of Article 21 in the Pioneer and Explorer Contracts provided:

   "21. EFFECTIVENESS OF THIS CONTRACT

   This Contract shall become effective from the date of its execution by the parties provided that:

   (a) if within Twenty (20) banking days from the date of this Contract the board of directors of the Builder do not approve plans for the construction of a new slipway at the Shipyard or the Builder and the Buyer are unable to reach an agreement granting the Buyer or its nominees options to build additional vessels at the Shipyard on terms acceptable to the Buyer, …….the Buyer may rescind this Contract in its sole discretion;

   and

   (b) if any of the following conditions are not met in the following order (or such other order as the parties may agree) within Twenty(20) banking days from the date of this Contract, then this Contract shall be automatically rescinded (unless the party to whom performance is then next owed agrees otherwise):

   (i) agreement between the parties as to the supplier of the main engine described under Article 1(c)(ii), which the parties shall use their best endeavours to reach within Ten (10) banking days from the date of this Contract;

   (ii) receipt by the Buyer of the Letter of Guarantee issued and registered in accordance with Article 10(h);

(iii) receipt by the Buyer of evidence acceptable to the Buyer and the Guarantor of the validity and binding effect of this Contract, the Specifications and the Letter of Guarantee and that all governmental licenses (including without limitation for the exportation of the Vessel) permits, approvals (including without limitation from the State Administration for Foreign Exchange) and consents in relation to the construction, delivery and/or sale of the Vessel pursuant to this Contract and the Specifications and the provision of the Letter of Credit have been obtained;

(iv) receipt by the Builder of the Performance Guarantee issued in accordance with Article 10(i);

(v) receipt by the Builder of the first instalment paid by the Buyer in accordance with Article 10(b)(i), provided that notwithstanding the Twenty (20) day period aforesaid the Buyer shall always have Five (5) banking days after the date of receipt of the original of the Letter of Guarantee within which to make the said payment.

Upon such rescission, the parties hereto shall be immediately and completely discharged from their obligations, duties and/or liabilities under this Contract without incurring any liability whatsoever to each other.

8. Article 21(a) is not material. The Buyers agreed not to rely upon it. Article 1(c)(ii) provided:
*"(ii) The main propelling unit will consist of MAN B&W 6S50MC-C having a maximum continuous rating of 9480 kW (metric unit) at 127 R.P.M. Speed at C.S.R. (90% MCR) of main engine output with fifteen percent (15%) sea margin on the design draft (moulded) of 12.00 meters with clean bottom and wind force not exceeding Beaufort scale 2 under calm sea shall be not less than 14.5 knots (the "**Guaranteed Speed**")."*

9. Article 10(h) provided: "(h) **LETTER OF GUARANTEE**
*As security for the due performance of its obligations under this Article 10, the Builder shall deliver, or procure that there is delivered, to the Buyer the original of an irrevocable and freely assignable letter of guarantee, in a form reasonably acceptable to the Buyer and the Guarantor, issued by the Bank (the "**Letter of Guarantee**") together with confirmation in writing from the Bank of due registration of the letter of Guarantee with the State Administration for Foreign Exchange. All expenses in issuing, registering and maintaining the Letter of Guarantee and all charges or expenses relating to a refund made under this Contract shall be borne by the Builder.*
If for whatsoever reason the Letter of Guarantee ceases to be in full force and effect, the Buyer shall be entitled to rescind the Contract in accordance with the provisions of Article 12 hereof."

10. The obligations of the Builder under Article 10 were to refund sums paid by the Buyer prior to delivery of the vessel in the event that the Buyer was entitled to rescind the Contract. I shall refer, as the parties did, to this Guarantee as the Refund Guarantee.

11. Article 10(i) provided: "(i) **PERFORMANCE GUARANTEE**
*As security for the second, third and fourth instalments due in accordance with Article 10(b), the Buyer shall deliver, or procure that there is delivered, to the Builder an irrevocable letter of guarantee (the "Performance **Guarantee**") in a form reasonably acceptable to the Builder and the Bank issued by an international first class bank (the "**Guarantor**") acceptable to the Builder and the Bank within five (5) banking days of the Buyer's receipt of the Letter of Guarantee."*

12. Article 19(b)(i) required the buyers to pay a first instalment of 5% of the contract price five banking days after the date of receipt by the buyer of the original Letter of Guarantee referred to in Article 10(h).

THE APPLICATION

13. The Arbitration Application, which led to the grant of permission to appeal, raised three ***"questions of law":***

"(i) whether there was an agreement as to the supplier of the main engine between the parties arising out of the parties' exchanges of 18 and 19 March 2003 for the purposes of Article 21(b)(i) of the contracts;

(ii) whether, if there was no agreement as to the supplier of the main engine, notwithstanding that the [Builder] had decided for commercial reasons not to perform the contracts in any way whatsoever from 19 March or after 20 March 2003, conduct which of itself was found by the arbitrators to be capable of being repudiatory of the contracts, the [Builder] was entitled to rely upon that absence of agreement as to the supplier of the main engine and to invoke Article 21 as rescinding the contracts;

(iii) whether, if had there been agreement on the supplier of the main engine under Article 21(b)(i), it was open to the [Buyers] on the true construction of Article 21 to extend time to Xiamen for the provision of the refund guarantees under Article 21(b)(ii) of the contracts and to treat Xiamen's refusal to take any steps to provide the refund guarantees, pursuant to its decision not to perform the contracts in any way from 19 March, as repudiatory."

14. It is to these three questions that the submissions of the parties have been directed on this Appeal.

QUESTION (i)

Article 21(b)(i)

15. Article 21(b)(i) provided, in effect, that the Covington and Explorer Contracts should be *"**automatically rescinded**"* if by 21 March 2003 (20 banking days from their date) there was no agreement between the parties *"**as to the supplier of the main engine**"* described in Article 1(c)(ii). That was not a provision in respect of which *"**performance**"* was *"**owed**"* to either party and so, neither at common law nor under the express provisions of Article 21(b) itself, could it be waived by either party to the contracts.

The 18 and 19 March Letters

16. It is and was the Buyers' case that the requisite agreement was achieved by an exchange of letters between the brokers dated 18 and 19 March 2003. The Arbitrators concluded that there was no agreement for want of an offer open to acceptance and lack of an acceptance (paragraphs 159 to 171 of the Reasons), albeit they acknowledged in respect of that conclusion that, whilst it was submitted by the builders that the wording of the exchanges of 18 and 19 March 2003 did not *"**look like a final agreement**"*, but was only *"**tentative and provisional**"*, that submission *"**was not developed in any detail**"* whereas it was their own view that it did merit *"**detailed consideration**"* (paragraph 165). There is, I think, even with Arbitrators of the acknowledged experience of the present tribunal, a risk in such an approach. It meant that whilst it cannot be and is not submitted that the question was not before them, it was given *"**detailed consideration**"* by the arbitrators without detailed submissions from the parties to assist them and without the question being focused upon in the evidence insofar as it might have been relevant to do so.

17. The letter of 18 March, addressed by ASI to BRS, as set out by the Arbitrators, read: *"…. after very frank discussion with the yard at length, we think it is necessary to mention the following points*

A. Refund Guarantee [The letter stated that Exim Bank insisted on certain words which (EST) had queried, that it selected Alternative A (jurisdiction of the English Courts) and that the Shipyard would try to persuade the bank to accept a qualification to the "drop dead" date if the buyers agreed to it].

B. Main Engine The Shipyard will agree to import the Main Engine subject to

1. The Buyer shall assist the yard to squeeze the price to the same level as domestic Licence Supplier

or

2. The Buyer bears the coats [costs] of price difference after the shipyard present the Buyer clear evidence.

Payment [performance] Guarantee Please find the attached payment guarantee proposed by Shipyard and accepted by some shipowners who ordered the vessel in the yard previously. We much appreciate if you pass the proforma to the Buyer and Buyer's bank for their comments and reference."

18. As the Arbitrators noted: *"Item B may have reflected the price formula adopted for "preferred makers" set out in the makers list, annexed to the contracts, which read:*

'Preferred makers' mean makers which may be selected by the Buyers, and upon receiving the Builders' written request the Buyers shall within 5 banking days thereafter begin to use their best endeavours to positively influence the said makers during price negotiations or, at their option, pay any difference between the Builders and the Buyers preference."

19. The letters of 19 March, (one for each contract) sent by BRS to ASI, as set out by the Arbitrators, read: *"Re: shipbuilding contract (the "Shipbuilding Contract") dated 23 February 2003 made between yourselves and ourselves*

We refer to our pleasant conversation of earlier today with Mr Edward Jiang [of the Builders] with respect to the effectiveness of the Shipbuilding Contract. The position under Article 21 can be summarised as follows:

1. In accordance with its terms, the Shipbuilding Contract is today fully effective and has been since the date of its execution.

2. The continuing effectiveness can now be confirmed as the following conditions have been lifted/extended:

a. Article 21(a) – Options. As was made clear to Edward earlier today, the Buyer understands the difficulty in finalising the new slipway arrangements at this time and therefore only wishes to finalise the options for the 2 berths in the existing slipway which will become available only if the options held by third parties are not exercised. The proposed wording for this option will be sent separately.

b. Article 21(b)(I) – Main Engine. The Buyer will bear the additional costs, if any, arising from the importation of the main engine from Korea.

c. Article 21(b)(ii) – Refund Guarantee. The Buyer accepts the Builder's proposal that EXIM bank of China provide the refund guarantee and that the refund guarantee be issued in the agreed form, as attached. As discussed with Edward, the Buyer now expects confirmation within tomorrow whether EXIM Bank prefers Alternative A or Alternative B set out in that draft document.

The Buyer appreciates that the Builder may require additional time to arrange for EXIM Bank to issue the refund guarantee. Being the party to whom performance is now due, the Buyer agrees to extend the 20 day period provided for under Article 21(b) for a further 10 banking days. Please advise whether the Builder believes this additional period is sufficient.

d. Article 21(b)(iii) – Due Diligence. This process is progressing accordingly.

e. Article 21(b)(iv) – Performance Guarantee. The Buyer has instructed its bank to issue the performance guarantee in the form of the attached agreed wording and will provide this document to the Builder in accordance with Article (10(I) notwithstanding the periods provided for in Article 21(b), as amended by this letter.

f. Article 21(b)(v) – Payment of the First Instalment. The Buyer will make this payment in accordance with the Shipbuilding Contract, as amended by this letter.

With the effectiveness of the Shipbuilding Contract confirmed, we look forward to the development of this relationship and to the Builder's prompt performance of its obligations. We also look forward to learning when we can expect to welcome Mr Zhao to Athens to celebrate our mutual achievement.

Given market interest in this project, we are preparing a draft press release regarding our cooperation for your review and immediate release.

We also take this opportunity to confirm that of course the Buyer agrees to amend the Shipbuilding Contract to provide for a contract number, as previously requested. Replacement pages will be forwarded to the Builder by email and courier (executed by the Buyer).

This letter shall be governed by and construed in accordance with English law, and Article 14 (arbitration) of the Shipbuilding Contract shall apply to this letter as if set out in this letter in full (mutatis mutandis).

Subject to the amendments introduced by this letter, the Shipbuilding Contract remains in full force and effect."

20. Each letter concluded with a sentence to be signed on behalf of the Builders confirming their agreement with its contents.

"Accepted Repudiation"

21. As the Arbitrators recorded (paragraphs 28 and 29 of the Reasons) no reply was ever sent to the 19 March letters and "despite numerous messages sent on behalf of EST it proved impossible to progress the matter or to obtain any response". The reason was that, on 19 March, the Builder signed contracts to build essentially three of the same vessels for another buyer. On 2 May 2003, Pioneer and Explorer accepted the conduct of the Builders as a wrongful repudiation of their contracts. Covington and Washington did the same on 21 May and 16 September 2003 respectively.

The Arbitrators' Reasons

22. The Arbitrators' reasons for concluding that no agreement was reached within Article 21(b)(i) by the letters of 18 and 19 March appear from paragraphs 165 to 171 of the Reasons. It is, however, important to note that in paragraphs 160 to 164 the Arbitrators rejected the two submissions by the Builders which were at the forefront of their case on this question.

23. In paragraphs 160 to 163 they rejected the submission that the letters did not comply with (b)(i) because they did not provide for a particular named supplier of the main engine. They did so on the basis that the ***"surrounding circumstances"*** showed that (b)(i) was intended to address only the unresolved issues that the Buyers wanted engines manufactured in Korea, with which they were familiar, and not in the PRC, whilst the Builders were concerned about the extra cost of engines from Korea rather than from the PRC. There were in fact only two possible suppliers of the specified engines in Korea and the Arbitrators'

conclusion was that agreement that the supplier should be one or other of them or *"**any Korean supplier**"* would be sufficient to satisfy (b)(i). That conclusion is not the subject of any cross appeal and so must be taken to be right. For what it is worth, in any event I agree with it. The consequence is that all that had to be agreed to satisfy Article 21(b)(i) was that the engine supplier should be Korean and references to importing the engine were references to importing it from Korea to the Builders.

24. In paragraph 164, the Arbitrators also rejected the submission of the Builders that the letters could not be construed as an agreement that the main engine supplier should be a Korean supplier because it was impossible to import Korean engines without the consent of the Chinese licensees of MAN B&W which would not be granted. The submission was rejected on the evidence, in particular the evidence that MAN B&W were able and willing to supply Korean engines to the Builders.

25. The "***detailed consideration***" by the Arbitrators which led them to their conclusion on this question should be set out in full:

"166. We begin by pointing out that ASI's letter of 18th March 2003 was not the kind of letter, which judging from previous exchanges, Xiamen would have been likely to send if it had intended to make a firm offer as to the supplier of the main engine. ASI's letter is stated to have been the result of an oral discussion with the yard, whereas all previous proposals had been contained in letters or emails sent directly by Xiamen itself. This is not all. When Xiamen had previously made an offer relating to this very topic, it had embodied the offer in a formal document requiring the signature of the buyers; see the draft agreement of 7th March 2003 proposing that the supplier should be a "Chinese manufacturer under the license of MAN B & W". The letter from ASI lacks any formality.

167. Next, the language used by ASI is not entirely consistent with the making of an offer on behalf of Xiamen. As was pointed out, there is no doubt some uncertainty as to what sums are included in the phrase "The Buyer bears the (costs) of price difference after the shipyard present the Buyer clear evidence." Does price difference include any sums that might have to be paid to compensate the Chinese licensees for loss of business? The point however goes somewhat further. If it was open to the buyers to "accept" the second alternative set out in ASI's letter, then logically one would expect that the first alternative solution proposed in the letter would also constitute an offer open for acceptance. But the first alternative ("The Buyer shall assist the yard to squeeze the price to the same level as domestic License Supplier") is so uncertain in language and effect that it can hardly constitute more than a proposal open for further discussion and more detailed elaboration.

*168. It is noteworthy in this connection that item B of the letter seems to have reflected the price formula adopted for "preferred makers" set out in the makers list. But in its original context the formula referred to a category of item where Xiamen had freedom to select the maker subject only to the buyers having the right to request that a particular maker be selected in which event the buyers had to use their best endeavours "to positively influence the makers during price negotiations with Xiamen" or, at their option, to pay any difference in cost between Xiamen's selection and the buyers' preference. We can see that this formula may have been satisfactory for the purpose of distinguishing "**strongly preferred makers**" from "**preferred makers.**" We can see also that it might have seemed a useful basis for discussion to adapt this formula to the situation where the buyers were requesting that the main engine be imported from Korea. But it is one thing to put forward a formula as a basis for discussion; it is quite another to make a firm offer on the basis of such a formula. The language used in the letter with its many uncertainties and ambiguities is far more consistent with the former than with the latter. We read the words "**The Shipyard will agree….**" as putting forward a basis for resolving the matter and not as an offer which was open for acceptance.*

169. There is then the circumstance that Xiamen was known to be thinking of "escaping" from the contracts at the time the letter was sent. If indeed ASI's letter contained an offer made on behalf of Xiamen and it had not been revoked before acceptance, this circumstance would not prevent the buyers from accepting the offer. But the known fact that Xiamen was thinking of withdrawing from the contact was, we think, a relevant circumstance in assessing whether the letter contained a formal offer to resolve one of the most important matters in issue between the parties.

170. Finally, the buyers' letter of 19th March 2003 may be significant in assessing whether they (and therefore a reasonable person) would have regarded ASI's letter as containing an offer open for acceptance. These letters dealt, not just with the supplier of the main engine, but with several outstanding matters and contemplated

that Xiamen should accept the package as a whole by signing a copy of each letter. When dealing with the main engine, the letters did not refer to any offer but used different, and slightly more exact language than had been used in ASI's letter; "The Buyer will bear the additional costs, if any, arising from the importation of the main engine from Korea." (The wording goes beyond "price difference" to embrace additional costs involving yet another area of uncertainty.) Just as Xiamen had proposed a formal variation of the contracts in its draft agreement of 7th March 2003, so also the buyers seem to have had in mind that one document signed by both parties required to be executed; see Art 22 para (b). All this is hardly consistent with treating ASI's letter of 18th March 2003 as containing a firm offer open for acceptance.

171. For all these reasons we conclude that the exchanges of 18th and 19th March 2003 did not contain any final agreement but were tentative and provisional. Accordingly we find that by 21st March 2003 there had been no agreement between the parties as to the supplier of the main engine. "

The Submissions: the Buyers

26. Mr Rainey QC for the Buyers submitted that:

i) The 18 March letter addressed the outstanding concerns of both parties:

*a) The Buyers' concern that the engines should be made in Korea by suppliers with whom they were familiar was met by the offer that the Builder "**will agree to import the Main Engine**"; and*

b) The Builders' concern that importation might increase the cost to them of the engines was met by putting forward the alternative proposals that the Buyers should either help the Builders to use their commercial power to achieve the same price from Korea as was available in the PRC or the Buyers should pay any difference in price provided the difference was clearly evidenced.

*ii) Read objectively, as the law required, the letter connoted to a reasonable person in the position of the Buyers that the Builders were making an offer in accordance with Article 21(b)(i) of the Contract by which they intended to be bound should it be accepted. Mr Rainey referred to **Chitty on Contracts** (29th Edn) para 2-002.*

*iii) In the 19 March letter, the Buyers had chosen and agreed to the second alternative offered to them by agreeing to "**bear the additional costs, if any, arising from the importation of the main engine from Korea**".*

*iv) In reaching their conclusion, the Arbitrators had relied on matters which were "**misconceived or (in three instances) wrong as a matter of legal approach**".*

27. Mr Rainey's criticisms of the reasoning of the Arbitrators in the paragraphs I have set out can be summarised as follows.

28. **Paragraph 166** did not read easily with the findings in paragraph 48 of the Reasons, addressing an issue of authority raised by the Builders and rejected by the Arbitrators, where it was recorded that the Builders had had "a running correspondence" with the Buyers "both directly and through the broking chain with regard to the matters which needed to be agreed under Article 21 including the country of origin of the main engine". It read even less easily with the findings in paragraph 153 of the Reasons in which, addressing and rejecting the case of the Builders that the 18 March letter itself was written by ASI without their authority, the Arbitrators had noted that the letter had attached to it a draft performance guarantee which could only have come from the Builders themselves and concluded that they had to accept *"that the message sent by ASI on 18 March 2003 broadly set out what ASI had been told"* by the Builders. Nor was it relevant to compare the formality of a previous "offer" made by the Builders to an "offer" which contained alternatives, as this one did, which could not therefore be embodied in a formal document before one of the alternatives was accepted if it was. The Refund Guarantee sent with the letter was, of course, the next step required to be completed under Article 21(b) after agreement was reached on the supplier of the main engine. It was not submitted nor found that there was an established or conventional method of making an offer open to acceptance and the Arbitrators should therefore have focused on the words used in their context and the objective legal test for an offer.

29. **Paragraphs 167 and 168.** The reference by the Arbitrators to the language of the letter (which was written by non-native English speakers), albeit tentative in its terms, ignored the context in which it was written, namely addressing the only reasons why agreement on the main engine supplier had not been reached before the contracts were signed. The question of compensation to the Chinese licensees had largely been dismissed in rejecting the submission that importation from Korea was impossible and was not raised in

the 18 March letter. The comment that the first alternative put forward in the 18 March letter was "so uncertain in language and effect" that it could "hardly constitute more than a proposal open for further discussion and more detailed elaboration" ignored the fact that it was a concept familiar to and recognised as binding and workable by the parties from the provisions of the Makers' list (see paragraph 18 above) as the Arbitrators themselves recognised in paragraph 168 of the Reasons. Why it should work and be effective there but not when transposed to the main engine is not explained but merely asserted in that paragraph. In any event, as a matter of law, if a chosen alternative is sufficiently certain and otherwise satisfies the legal requirements of an offer it is open to acceptance as such. The apparent emphasis on the words "will agree" in the final sentence of paragraph 168 was misplaced: the words merely reflected in context the offer of a concession to the expressed wish of the Buyers to source the engines from Korea and the terms available for that to be agreed.

30. **Paragraph 169.** The fact that the Builders were *"known to be thinking of escaping from the contracts at the time"* the 18 March letter was sent was, Mr Rainey submitted, *"in law a wholly irrelevant consideration"*. Mr Rainey referred to **Chitty** at para 2.003 where, so far as is material to this case, it is said: *"Whether A is actually bound by an acceptance of his apparent offer depends on the state of mind of the alleged offeree(B); to this extent, the test of agreement is not purely objective. With regard to B's state of mind, there are three possibilities. First, B actually believes that A has the requisite intention: here the objective test is satisfied so that B can hold A to his apparent offer even though A did not subjectively have the requisite intention …. Secondly, B knows that in spite of the objective appearance, A does not have the requisite intention: here A is not bound; the objective test does not apply in favour of B as he knows the truth about A's actual intention …*

31. The Arbitrators made no findings either as to the belief or knowledge of the Buyers nor as to the intention of the Builders. No doubt there was no evidential basis on which they could do so. The paragraph represents, so Mr Rainey submitted, an impermissible halfway house, ***"a mess".*** It derives from an email sent on 17 March, and referred to in paragraph 148 of the Reasons, in which a partner in BRS had informed a member of the family which owned the ships which EST existed to manage that he had *"a strong feeling that"* the Builders were *"slowly escaping and in any case"* had *"clearly decided not to leave all their eggs in one basket"*. The *"one basket"* was a reference to what was addressed in Article 21(a). Mr Rainey submitted that the correct approach was for the Arbitrators to address the terms of the letter as an objective reader would have read them and that they had failed to do so.

32. **Paragraph 170.** The first and last sentences appear to address the 18 March letter whereas the remainder of the paragraph addresses the 19 March letter and, it seems, whether or not it amounted to an acceptance. The first sentence muddles the subjective and objective. The whole paragraph wrongly uses the "acceptance" to construe *"the offer"*. The fact that the 19 March letter addressed the further provisions of Article 21(b) is hardly a matter for surprise whether or not it was accepting an offer in respect of the main engine. Indeed the letter presumes that there is agreement on sub-paragraph (b)(i) and so moves on to the next condition to be fulfilled (the Refund Guarantee) as had the 18 March letter itself. The fact that the 19 March letter *"did not refer to any offer but used different and slightly more exact language than"* the 18 March letter was, Mr Rainey submitted, to put literalism before commercial reality. He also referred the Court to Chitty at para 2-030 to the effect that there is no rule requiring exact or precise correspondence between offer and acceptance.

33. **Paragraph 171.** Mr Rainey stressed that it was *"for all"* of the reasons they had given that the Arbitrators had concluded that the 18 and 19 March letters *"did not contain any final agreement but were tentative and provisional"*.

The Submissions: The Builders

34. The primary submission of Mr Young QC, for the Builders, was that this question was a question of fact not law and therefore not a permissible ground of appeal at all. Mr Young's secondary submission was that even if the question raised issues of construction of the 18 and 19 March letters and those were issues of law or mixed fact and law, then a contrary conclusion to the conclusion of the Arbitrators could only be reached if they had misdirected themselves in law and so reached a decision *"outside the legitimate areas of potential conclusion"* or which *"it was legally impossible"* for them to have arrived at. Mr Young submitted, on this basis, that *"there were two arguable and legally possible conclusions as to the effect of the letters and the learned*

Arbitrators had to choose between them. The Court cannot and should not interfere when the parties' chosen tribunal do what is required of them." The 18 March letter was, so Mr Young submitted, *"only a proposal of a route to a solution"* or *"moving towards a solution"* of the problem of who was to be the supplier of the main engines.

The Law

35. I was referred to a number of authorities on whether or not questions of construction such as arise here are questions of law and as to the correct approach of a Court exercising an appellate jurisdiction in relation to such questions.

36. In **Pilgrim Shipping Co Ltd v The State Trading Corporation of India** [1975] 1 Lloyd's Rep 356 there was a sharp division between Lord Denning, MR (on one side) and Roskill LJ and Sir John Pennycuick (on the other side) as to whether a question of construction (in that case of clauses in a charterparty) was a question of law or one to be left to the decision of the arbitrators who, in accordance with the arbitration clause, were to be ***"commercial men"***. Lord Denning (at pages 360-361) was for leaving it to the arbitrators and keeping the lawyers away. Roskill LJ and Sir John Pennycuick considered the question to be one of law for the court. Roskill LJ said *"it is axiomatic that all matters of construction of documents are questions of law. Upon questions of law the final determination rests with the Court and not with arbitrators or an umpire, however distinguished and experienced".*

37. In **André et cie v Cook Industries Inc** [1986] 2 Lloyd's Rep 200, Bingham J, on appeal from the Board of Appeal of GAFTA, had to construe a series of exchanges between the buyers and sellers of soya bean meal extract to determine whether or not they amounted to an accord or agreed variation of a contract of sale so as to substitute 40% of the full contract quantity for the full contract quantity to be shipped in the month of July. In the course of his judgment, at page 204, Bingham J said: *"I should be very slow to differ from a trade tribunal on the meaning reasonably to be given to telex exchanges of the sort in issue here. Ultimately, of course, the construction of any written instrument is a question of law on which the Court is entitled and bound to rule, but the significance of a meaning attributed by the reasonable non-lawyer varies widely from instrument to instrument and according to the circumstances of the case. Here one is dealing with communications by trader to trader in the context of an unexpected and fast-moving situation. A trade tribunal brings to the task of interpretation certain insights denied (to a greater or lesser extent) to the Court: an informed appreciation of the commercial situation as it unfolded, seen through the eyes of a trader; an understanding of the hopes and fears and pressures which moved traders at the time; an awareness of the extent to which, at the time, the future course of events appeared obscure and unpredictable; a knowledge of the language which one trader habitually uses to another. So, in a case such as this the Court's task is not one of pure construction and I should be reluctant to differ from the board unless it appeared that the board's construction was fairly plainly untenable."*

38. This statement, in my judgment, reflects the present law and, to an extent, provides a useful reconciliation of the conflicting views of the Court of Appeal in **Pilgrim**. It should be noted that there is no submission on behalf of the Builders that the letters here in issue contain anything on which the views of "***a trade tribunal***", even if it were sensible so to describe these Arbitrators, would bring any particular insight.

39. In **The Chrysalis** [1983] 1 Lloyd's Rep 503 Mustill J addressed the question how an award could be shown to be wrong in law in a case which involved a finding of commercial frustration of a charterparty. He said, at page 507: *"In a case such as the present, the answer is to be found by dividing the arbitrator's process of reasoning into three stages:*

(1) The arbitrator ascertains the facts. This process includes the making of findings on any facts which are in dispute.

(2) The arbitrator ascertains the law. This process comprises not only the identification of all material rules of statute and common law, but also the identification and interpretation of the relevant parts of the contract, and the identification of those facts which must be taken into account when the decision is reached.

(3) In the light of the facts and the law so ascertained, the arbitrator reaches his decision.

In some cases, the third stage will be purely mechanical. Once the law is correctly ascertained, the decision follows inevitably from the application of it to the facts found. In other instances, however, the third stage involves an element of judgment on the part of the arbitrator. There is no uniquely "right" answer to be derived from marrying the facts and the law, merely a choice of answers, none of which can be described as wrong.

The second stage of the process is the proper subject matter of an appeal under the 1979 Act. In some cases an error of law can be demonstrated by studying the way in which the arbitrator has stated the law in his reasons. It is, however, also possible to infer an error of law in those cases where a correct application of the law to the facts found would lead inevitably to one answer, whereas the arbitrator has arrived at another: and this can be so even if the arbitrator has stated the law in his reasons in a manner which appears to be correct – for the Court is then driven to assume that he did not properly understand the principles which he had stated.

Whether the third stage can ever be the proper subject of an appeal, in those cases where the making of the decision does not follow automatically from the ascertainment of the facts and the law, is not a matter upon which it is necessary to express a view in this present case. The Nema and The Evia show that where the issue is one of commercial frustration, the Court will not intervene, save only to the extent that it will have to form its own view, in order to see whether the arbitrator's decision is out of conformity with the only correct answer or (as the case may be) lies outside the range of correct answers. This is part of the process of investigating whether the arbitrator has gone wrong at the second stage. But once the Court has concluded that a tribunal which correctly understood the law could have arrived at the same answer as the one reached by the arbitrator, the fact that the individual judge himself would have come to a different conclusion is no ground for disturbing the award."

40. Mr Young relied on this passage in support of his secondary submission. But I do not think it assists him. Mr Rainey relies on errors he submits were committed by the Arbitrators at "the second stage" not the third stage. Nor does the passage in any way suggest that a question of construction is other than a question of law, rather the contrary.

41. Mr Young also referred me to the decision of Saville J in **Alfred C Toepfer Intnl.v Itex Itagrani Export SA** [1993] 1 Lloyd's Rep 360. The issue was whether an exchange of messages between the buyers and sellers of *"**one full cargo**"* of maize amounted to a renunciation by buyers. The arbitrators directed themselves correctly on the law that a clear and unambiguous statement of unwillingness or inability to perform the contract was required and concluded that it had not been shown. The sellers contended that the exchanges demonstrated a refusal to load a full cargo and so the arbitrators *"**must have paid only lip service to the correct legal test**".* At pages 361-2, Saville J said: *"I am wholly unpersuaded that this happened. On examining the exchanges in question not only do I consider that it was open to the arbitrators to reach the conclusion that the exchanges did not amount to a renunciation by the buyers, but also I consider that I would have reached exactly the same conclusion. Indeed even if I had formed a different view I was not persuaded that I should substitute that for the view of the arbitrators, since in my judgment their conclusion on the facts did not demonstrate that they had failed properly to apply the law."*

42. This passage does not assist Mr Young either if Mr Rainey is right in his submissions. I think in substance it is making the same point as made by Mustill J in **The Chrysalis**.

Conclusion: Question (i)

43. In my judgment, Mr Rainey's submissions are much to be preferred to those of Mr Young:
    i) The question whether or not the letters do constitute a binding agreement is one of law or mixed fact and law.
    ii) Subject only to actual knowledge on the part of the Buyers that no offer was in fact intended to be made, both alleged offer and acceptance have to be viewed objectively, the one to determine whether the offeror intended to be bound if the offer were accepted, the other to determine whether the offer or, in this case, one of the alternatives proposed, has been accepted.
    iii) Both are to be considered in their commercial context and viewed commercially rather than literally where the two might give different answers.

44. The 18 March letter:
    i) If it was not intended to make or to be read as making alternative offers open to acceptance in relation to the source and cost of the main engine it is difficult to understand what other purpose was to be served by what was said;
    ii) In contrast, the references to the guarantees, including the Refund Guarantee, the next steps required by Article 21(b), were matters expressed as requiring further negotiation;
    iii) I think Mr Rainey's criticisms of the matters on which the Arbitrators relied are well directed.

45. The 19 March letter is phrased in terms of acceptance and not further negotiation as regards the main engine. An objective reader would, I think, readily conclude that there was agreement on the main engine and so the need to move on to address the further items required to satisfy Article 21(b). The terms of the agreement were clear. They mean what they say and cover the outstanding commercial concerns of the Builders. In substance they do not differ from the terms of the 18 March letter.

46. In my judgment, therefore, the Arbitrators were wrong to conclude that there was no agreement on the main engine. Their conclusions and their reasoning are wrong in law.

QUESTION (ii)

47. My decision on question (i) means this question does not arise. I will comment upon it briefly albeit to my mind it raises questions of some nicety.

48. Article 21(b)(i) is *"**an agreement to agree**"* which does not fit easily into a clause which otherwise provides that the agreement itself shall become effective on the date of its execution. The submissions made to the Arbitrators on the nature of the agreement are recorded in paragraphs 111 to 115 of the Reasons and their discussion of them is to be found at paragraphs 120 to 138. I think the hybrid nature of sub-clause (b)(i) would justify the conclusion that whilst the four contracts were effective on 23 February 2003 *"**their initial contractual force was to be provisional and even tenuous**"* (paragraph 137) but I do not think the same can be said for the other conditions in sub-clauses (ii) to (v).

49. In my judgment, the reasoning of the Arbitrators is again at fault. The contracts plainly take the form of contracts with conditions subsequent not precedent. Article 21 expressly states that the contracts are effective from the date of their execution and uses the language of *"rescission"* and *"discharge from these obligations"* if the conditions are not met. Mr Young, rightly, did not seek to contend otherwise.

50. The Arbitrators' construction of the words in parentheses *"unless the party to whom performance is then owed agrees otherwise"* is, in my judgment, wholly erroneous. The Arbitrators construed the word *"agrees"* as requiring a bilateral agreement and so agreement on each of the five conditions in the Article (paragraph 130). The words are, however, addressed to the fact that conditions (b)(ii) and (iii) are conditions of which the performance is *"**owed**"* to the Buyer and conditions (iv) and (v) conditions of which performance is *"**owed**"* to the Builder. The words are also to be contrasted with the clear reference to the need for a mutual or "***bilateral***" agreement appearing in the previous parentheses of the very same provision. The purpose is obvious. The provision is intended to preserve or reflect the common law right of a party to whom performance of an obligation is owed to waive the time for or the entire performance of that obligation. The reference to an obligation "owed" is otherwise otiose. To describe, as the Arbitrators do in paragraph 132 of the Reasons, the automatic rescission provision as being for the protection of the Builders if the obligations on the Builders themselves in sub-paragraphs (b)(ii) and (iii) were not performed by them is to achieve the exact opposite of the objective of the provisions as I construe them. It is also to ignore the separate obligation on the Builders to provide the Refund Guarantee provided for in Article 10(h) of the contracts. Again, Mr Young did not seek to defend the reasoning or conclusion of the Arbitrators.

51. On the basis, therefore, that, contrary to the view of the Arbitrators, Article 21 is properly to be read as providing for a binding agreement subject to *"automatic rescission"*, and as providing for or endorsing a right to waive performance of obligations for the benefit of the party agreeing to the waiver, there remains the difficulty of sub-paragraph (b)(i) which does require mutual agreement on the supplier of the main engine and is plainly not for the benefit of either party.

52. It is, of course, trite law that an agreement to agree is of no effect. Nor is it submitted by the Buyers that an agreement to use best endeavours to reach or to co-operate to reach an agreement or to do nothing to prevent or to act reasonably to achieve agreement or the like is of any greater effect.

53. Refined in the course of submissions, Mr Rainey's ultimate submission was that:
    i) Some effect should be given to the fact that the contracts were effective from their date of execution; and
    ii) As a minimum, the court should imply an obligation on both parties not to renounce the contracts before the time fixed (20 days, 3 or 6 months) in which agreement on the main engine was to be reached if it could be.

54. Such an obligation would, it was submitted, recognise that commercially a time provision of that kind would act as a real incentive to reach agreement rather than leaving the employment of the yard and the building of the ships in a state of uncertainty for the period concerned. If it were otherwise, the contracts would be of no more binding effect than the letter of intent which the parties had signed earlier (paragraphs 8 to 12 of the Reasons) and it would mean that within hours of executing the contracts either party could have announced to the other that they had thought better of it, despite the reference to "***automatic rescission after 20 days***".

55. These are powerful submissions. But, I think, they are erroneous. The parties may well each have been content to rely on the commercial pressures on the other to reach an agreement on the supplier of the main engine so as to secure the contracts. The remedy for breach of the term the Buyers seek to imply would be of very doubtful and uncertain value. In the case of the 3 and 6 month periods it must, I think, also be open to serious question whether or not such a term could pass the test of necessity.

56. I was referred to a number of authorities. I do not think the "***principle***" in **Mackay v Dick** (1881) 6 App Cas 251 assists the Buyers. This would not be a case of one party preventing performance by the other of a matter they have agreed should be done because in sub-para (b)(i), in contrast to the other sub-paragraphs, the Builders have not agreed more than to agree. Nor would the Builders be taking advantage of their own wrong or breach of a duty owed to the Buyers: **Cheall v A.P.E.X.** [1983] 2 AC 180. It would not be a wrong or a breach of duty not to agree on the supplier of the main engine.

57. Had it been necessary to decide this question, therefore, I would have answered it in the affirmative albeit for reasons different from those of the Arbitrators.

QUESTION (iii)

58. I have already addressed the question whether or not the Buyers were entitled to waive compliance with Article 21(b)(ii). In my judgment the Article plainly entitled them to do so. The reference to an entitlement to "extend time" to provide the Refund Guarantee seems to me to obscure the real issue. Granted that the Buyers could waive compliance with the requirement to provide the Refund Guarantee by 21 March, there would remain the independent obligation upon the Builders to provide the Guarantee under Article 10(h) to which no time limit was applied. The law would require provision within a reasonable time and the 19 March letter referred to a further 10 days whilst enquiring if that would be sufficient. In my judgment that is to be read as a waiver of the 20 day period and seeking to establish a reasonable time to discharge the obligation of the Builder.

59. Mr Young accepted that if I reached the conclusions which I have so far, then it must follow that the Builder was in repudiatory breach of the Covington and Washington contracts. Those breaches were accepted as bringing the contracts to an end before the expiry of the 3 and 6 month periods for the fulfilment of sub-paragraphs (ii) to (v) of Article 21. In paragraph 175 of the Reasons the Arbitrators concluded: *"Had we found that by 21st March 2003 there had been agreement between the parties as to the supplier of the main engines and had we also accepted the submission that it was open to the buyers to extend the time for performance unilaterally and subsequently to treat the non-provision of the refund guarantee as a repudiatory breach of contract, we would have concluded that by 20th March 2003, coincidental with the conclusion of the Pacific Basin contracts, Xiamen had decided not to perform the contracts. It is clear to us that, for a variety of reasons, Xiamen took a commercial decision not to perform the contracts after 20th March 2003 and thereafter communicated this decision to the buyers by consistently failing to respond to their letters. Accordingly, on the assumptions set out earlier we would have found that the conduct of Xiamen in failing to take any further step towards issuing the refund guarantees coupled with the failure to communicate in any way with the buyers in the period following 19th March 2003 constituted a wrongful repudiation of the contracts."*

60. The reference to "***the Pacific Basin contracts***" is a reference to the contracts made by the Builders with other buyers for essentially the same vessels.

61. As Mr Young stated, there is no appeal against paragraph 175 and whilst the conclusions in paragraphs 176 and 177 cannot, I think, be reconciled with paragraph 175 (and other parts of the analysis of the Arbitrators) it follows, as Mr Young acknowledged, that if there was, as I have found there was, an agreement on the supplier of the main engine, there was an accepted repudiation by the Builder of both the

Covington and Washington contracts before the time expired for the performance of the remaining conditions.

62. Mr Young submitted, however, that the same was not the case with the first two contracts. His submission was that even if performance within 20 days of the Builder's obligations had been waived, the Builder had not waived performance by the Buyer of the Buyer's obligation to provide the Performance Guarantee and the Builder had not received that Guarantee within that period. Clause 21(b) required all the conditions [except sub-paragraph (b)(v)] to be met within the 20 days. That had not occurred and so the contracts were "automatically rescinded" on 21 March before the Buyers had accepted any repudiation by the Builders.

63. I do not accept this submission. Article 21(b) requires (absent mutual agreement to the contrary) the conditions to be met in a set and commercially sensible sequence. It is true, as Mr Young submitted, that sub-paragraph (b)(iv), unlike (b)(v), does not expressly provide for an extension of time dependent on fulfilment of the previous conditions. Article 10(i), however, does provide for a period of 5 days from delivery to the Buyer of the Refund Guarantee for provision by the Buyer to the Builder of the Performance Guarantee.

64. In my judgment, the reconciliation of these provisions, to make commercial sense of them, which this court will seek to achieve, is not hard to find. Article 21 provides for the performance of the stated conditions in a particular sequence within the 20 days under sanction of automatic rescission if it is not achieved. In the case of those conditions which are for the benefit of one party, if the other party cannot or will not perform when it is for them to do so, the other party may waive the time for compliance rather than have the contract automatically rescinded. But, absent mutual agreement, the sequence of performance of the conditions remains unaffected and the non-performing party cannot call on the other party to perform their subsequent obligation or rely upon automatic rescission until he has performed his own anterior obligation. If it were otherwise it would, in effect, be open to the non-performing party (A) to achieve automatic rescission, or to alter the sequence of conditions, unilaterally, by relying on the other party's (B's) non-performance of a condition within the 20 days, when the contract entitled B not to perform until after A had met the condition it was for A to meet. In my judgment the contracts continue, the sequence remains and the obligations stand. Only the provision for automatic rescission is affected. Otherwise, as Mr Rainey submitted, the express right to waive performance would be meaningless.

65. The Arbitrators were, in my judgment, right in their conclusion in paragraph 175 and the Builders were not entitled to rely upon the fact that no Performance Guarantee had been received by them by 21 March as automatically rescinding the Pioneer and Explorer contracts.

THE PROPER ORDER

66. Section 69(7) of the 1996 Act provides that on an appeal under the section, the court can confirm, vary or remit the award or set it aside in whole or in part. It also provides that "the court shall not exercise its power to set aside an award, in whole or in part, unless it is satisfied that it would be inappropriate to remit the matters in question to the tribunal for reconsideration".

67. Mr Young submitted that I should remit the matters to the Arbitrators. But he acknowledged that there were no other admissible factors, contextual or otherwise, than those to be found in the Reasons which could affect the outcome on questions (i) and (iii). As I have also concluded that question (i) does give rise to matters of law and the Arbitrators were wrong in law in their approach to the analysis of offer and acceptance, and in some of the factors and their use which they did take into account, and in their construction of the letters of 18 and 19 March, and that, properly approached, there was agreement as to the supplier of the main engines within Article 21(b)(i), I think there is nothing to be said for remitting the issue to the Arbitrators. The right order is to vary the Awards so as to provide that the contracts were not automatically rescinded under the provisions of Article 21(b) and were repudiated by the Builders who are liable in damages to the Buyers accordingly. The precise terms of the appropriate Order and any ancillary matters should be addressed when this judgment is handed down.

Mr S. Rainey QC and Mr S. Picken (instructed by Messrs Clifford Chance) for the Claimants
Mr T. Young QC (instructed by Messrs Lovells) for the Respondents