



DRUCES^{LLP}

Corporate & Commercial Briefing Note

Relevant to

All those involved in commercial negotiations.

Summary

It is a long established principle of law that where a contract is induced by duress, it is voidable by the injured party. The High Court has recently considered how economic duress, which may arise as a result of the illegitimate use by one party of its superior bargaining power, applies even where that conduct is not in itself unlawful. Progress Bulk Carriers Ltd v Tube City IMS LLC [2012] EWHC 273 (Comm) gives judicial endorsement to a previously held view that illegitimate pressure, which is not sufficient to amount to an unlawful act, may still constitute economic duress and render a contract voidable.

Economic Duress

Generally a contract will only be valid if it has been entered into freely and voluntarily. Where a party is, therefore, induced into entering a contract by duress, it is voidable by the injured party. There are two elements to proving economic duress.

First, the injured party must show that the economic pressure applied was illegitimate. The pressure may be a crime, a tort, or a breach of contract (including past and threatened breaches). There have also been suggestions that unethical behaviour may suffice although until *Progress Bulk Carriers Ltd v Tube City IMS LLC* it is not thought that a Commercial Court has ruled on this specific point.

When considering whether the pressure applied was illegitimate, a distinction is made with everyday bargaining during the course of negotiations. In drawing this distinction, the courts will consider a variety of factors including the seriousness of the impropriety, whether the person exerting the pressure was acting in good or bad faith and whether the injured party had a realistic alternative.

Secondly, there must be causation. In other words, but for that illegitimate economic pressure, the injured party would not have entered into the relevant contract or made a payment.

Facts of the Case

Tube City IMS LLC (the “Charterers”) hired a cargo ship from Progress Bulk Carriers Ltd (the “Owners”) for the transportation of shredded scrap from the Mississippi River to China. The charter did not give any right to substitute the vessel.

After the charter had been entered into, the Owners hired the cargo ship to a third party, rendering performance of the contract impossible. Although this amounted to a repudiatory breach of contract, the Charterers neither exercised their right to terminate the contract nor sought to hire a vessel elsewhere. Instead, they relied on assurances from the Owners that they would find an alternative vessel. The Owners also said that they would compensate the Charterers for all damages resulting from their failure to provide the contracted vessel.

The Charterers looked to hold the Owners responsible for the losses they incurred, including a reduction in the scrap price they agreed in return for the receivers of the cargo extending the shipment date. Contrary to the terms of their assurances, the Owners sought to renegotiate this amount. After failing to secure a better amount, the Charterers settled on the Owners’ offer of a \$2 discount, reserving their rights in respect of all claims for damages arising out of the breach of the charter.

On the same day the Charterers agreed a new rate and delivery date with the receivers, the Owners made, what was found in the ensuing arbitration to be a “take it or leave it” offer. The offer required the Charterers to accept a \$2 per metric ton reduction and waive all claims for loss and damage arising out of the nomination of a substitute vessel which was outside of the charter time. Despite the inconsistencies with the Owners’ original assurances, the Charterer had no alternative. In reply to the Owners’ offer, the Charterers said: *“given the exigencies of the circumstances and our urgent need to mitigate our losses and accommodate our customer in China, we are forced to accept the Owners terms under protest”*.

The Charterers later argued that their agreement to waive their claim was obtained by economic duress and should be set aside.

Decision of the High Court

Following an Arbitration ruling in favour of the Charterers, the case was appealed to the High Court by the Owners. They argued that their behaviour in refusing to supply a substitute ship was lawful and that lawful acts could not amount to illegitimate pressure or economic duress.

The High Court’s judgment centres on the issue of whether the Owners conduct amounted to “the illegitimate pressure” required to establish economic duress. The Judge referred to an earlier Court of Appeal authority (*CTN Cash & Carry Ltd v Gallaher* [1994] 4 AER 714) which commented on the issue of lawful pressure. In this case, the Court of Appeal recognised that to allow *“lawful act duress’ in a commercial context in pursuit of a bona fide claim, would be a radical one with far-reaching implications.”* However it was considered to be a *“mistake for the law to set its sights too highly when the critical inquiry is not whether the conduct is lawful but whether it is morally or socially unacceptable”*.

In light of these comments from the Court of Appeal, and analysis of other authorities, the Judge in the High Court found that *“illegitimate pressure’ can be constituted by conduct which is not in itself unlawful, although it will be an unusual case where that is so. Particularly in the commercial context.”* This was one such unusual case.

The Court agreed with the Arbitrator’s ruling that the Owners were not threatening to break the contract at the time, nor committing any tort in refusing to enter into a variation of the charter with the substitution of another cargo ship. The Court, however, found that the Owners’ repudiatory breach was the root cause of the problem. The Arbitrator had found that *“the Owners had manoeuvred the Charterers into the position they were in, following the breach, in order to drive a*

hard bargain.” The Court recognised that “*the Charterers had no realistic practical alternative but to submit to the pressure and they did protest at the time.*”

Whilst the Owners’ refusal to supply a substitute ship was, therefore, lawful, the Court held that it had to be seen in the light of their repudiatory breach and subsequent conduct. This conduct included their deliberate refusal to comply with the assurances they had previously given about providing a substitute vessel and paying full compensation in respect of that breach. This amounted to illegitimate pressure for the purposes of economic duress.

Comment

Whilst the High Court took the view that the bar to establishing economic duress in cases involving lawful conduct is a high one, this case should give all those involved in commercial negotiations food for thought.

In this case, the repudiatory breach of contract by the Owners appears to be key to the Court’s finding of economic duress in their subsequent conduct. It is, therefore, unlikely that ordinary commercial bargaining will be sufficient to constitute economic duress on its own. If there is lawful but unconscionable conduct, however, coupled with past actions such as, for example, a repudiatory breach, then the validity of the contract could be at risk.

Where a party feels that it has been placed in such a position, it is critical to reserve all rights wherever possible and only accept the enforced terms under protest with a view to having the agreement set aside as soon as possible.

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This note does not constitute legal advice but is intended as general guidance only. It is based on the law in force on 18 June 2012. If you would like further information please contact Toby Stroh on +44 (0)20 7216 5564 or on t.stroh@druces.com or email us at corporate@druces.com.