



**LEGAL COSTS COVER (LCC) -
FORMATION OF THE CONTRACT:
WHAT HAPPENS WHEN THE FIXTURE IS
ON 'SUBJECT TO...?'**



SHIPOWNERS

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What is a contract?

Under English law, a contract is a legally enforceable agreement which gives rise to new rights and duties to those who agree to its terms.

There are five elements that are required to form a contract:

1. **Offer:** A promise by one party to enter into a contract on certain terms. The offer must be *specific, complete, capable of acceptance* and made with *the intention of being bound by acceptance*.
2. **Acceptance:** A contract only becomes legally binding if/once the offer is accepted. It must be made in response to an offer and must correspond exactly with the terms of the offer. An attempt at varying the terms will be construed as a counteroffer, which effectively rejects the original offer. While acceptance is generally communicated to the offeror, it is possible for a party's conduct to be interpreted as acceptance, if it is clear that the party did the act with the intention of accepting the offer.
3. **Consideration:** For the promise to be enforceable, something must be given or promised in return. This is called consideration. An agreement to provide a benefit or gift with no act or omission being provided by the recipient would not form a contract. Under English law, the adequacy of the consideration would not interfere with the agreement between the parties, though it must have some value, however small. In case law, a mere peppercorn is considered to be adequate consideration.
4. **Intention to create legal relations:**

Both parties need to intend to create a legally binding arrangement for there to be a contract. This is presumed in commercial situations, though it may be argued that at a particular point in time there was no such intention because there were remaining issues to be agreed.

5. **Certainty of terms:** A court will not be able to enforce a contract if no definite meaning can be given. Contractual terms should therefore be expressed clearly.

'Subject to...'

In a charterparty context, it is often the case that the parties negotiate terms quickly and efficiently. Hence, it is common that the charterparty terms are agreed in stages.

The parties will usually agree the main or essential terms first and draw what is widely called as a 'fixture recap'. However, they often add a proviso 'subject to', in order to indicate that further details or other factors will have to be considered first and agreed later on, before their contract is finalised and becomes legally binding.

In other words, where a fixture is being negotiated, the presence of 'subject to' wordings indicate that the parties have not entered into a legally binding charter.

A binding fixture will be only created once the parties expressly agree to lift all 'subjects'. Usually, the parties agree to a specific time frame by when the 'subjects' are to be declared or lifted, after fixing the main terms.

In some instances, the parties may imply that all 'subjects' have been lifted by performing the contract.

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For example, by delivering and accepting the vessel.

While there are '*subject to*' phrases remaining, both parties are free to withdraw from negotiations. That said, it is possible for the parties to be bound to terms that have already been agreed, while they seek to reach an agreement on outstanding terms unless the failure to reach an agreement on the outstanding terms renders the contract unworkable or void for uncertainty.

It is therefore best practice to mark all correspondence relating to negotiations of a fixture with one of the phrases below. This will make it clear that no contract is made until the parties have accepted the terms.

Subject to details:

When the essential terms have been agreed, the phrase 'subject to details' can be added to ensure that only when all the details are agreed by the parties, a binding contract has been formed. This is referred to as there being no 'live' subjects remaining and 'all subjects lifted', along with the expression 'clean fixed' to signify that the fixture has been concluded. As long as the subject remains, it is inferred that the parties do not intend to be bound until the negotiations are complete.

Subject to contract:

This suggests that a formal agreement is necessary before the contract becomes binding.

Subject to [a pre-condition]:

No contract exists until the relevant condition has been fulfilled. A pre-condition will most

likely apply where the subject requires the exercise of a personal or commercial judgement by one of the parties. For example, 'subject to board approval' would postpone the decision to enter into legal relations to a later stage. In some cases, a further agreement after the condition is satisfied may be required before the contract becomes binding. For example, the completion of sea trials as a condition would still require the parties to evaluate the outcome of the trials before entering into the contract. Where the agreement is 'subject to supplier's approval', if the identity of the suppliers is uncertain, it is likely that the approval will be a pre-condition due to the degree of uncertainty.

Subject to a performance condition:

A contract exists and the parties are obliged to perform the condition. This is usually where the 'subject' is dependent on a third party or if the lifting of the 'subject' is to occur automatically on the occurrence of some external event.

Conclusion

Fixing on 'subs' is undoubtedly a very efficient way of conducting negotiations, especially when time is of the essence. It allows parties to negotiate freely and feel comfortable that they are not bound, until such time that they are absolutely certain that they are able to go ahead with the fixture.

However, there has been some criticism of this widely used trading practice, as the power of subs can be misused. After all, it does allow the parties (charterers or owners) to look around for a better deal or seek

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for lower freight rates, whilst the fixture is still on subs.

When fixing on subs, we advise Members to seek advice and be conscious that other jurisdictions may have different views on whether the fixture is actually binding or not.

If you have any further questions about LCC, please contact the LCC Managers.

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