BENTLEYS

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INTER-CLUB AGREEMENT 1996, CLAUSE 8(d): MEANING OF "ACT OR NEGLECT"

Bentleys recently acted for the owners of the Yangtze Xing Hua in successfully defending an appeal on a point of law from an award in London arbitration. The underlying dispute concerned damage to a cargo of soya bean meal. The vessel had loaded the cargo for discharge at a port in Iran. On arrival at the discharge port, the vessel was ordered to wait there by the time charterers, as they had not received payment for the cargo.

The vessel waited for over four months. The cargo became damaged by self heating caused by the cargo's inherent nature (its oil and moisture content) combined with the lengthy period spent at anchor. Cargo claims were made by the Iranian receivers and were settled by the owners. The Inter Club Agreement 1996 ("ICA") was incorporated in the time charterparty so Owners sought recourse from the charterers, the respondent in the arbitration and the appellant in the recent appeal to the High Court.

The Tribunal found that the cause of the cargo damage was clearly attributable to the nature of the cargo loaded by the charterers and the prolonged period at anchorage. They then went on to consider clause 8(d) of the ICA which states:

8) Cargo claims shall be apportioned as follows:

…

d) All other cargo claims whatsoever (including claims for delay to cargo):

50% Charterers

50% Owners

unless there is clear and irrefutable evidence that the claim arose out of the act or neglect of the one or the other (including their servants or sub-contractors) in which case that party shall then bear 100% of the claim.

This provision is intended to 'sweep up' those cargo claims which do not fall into any of the preceding categories, i.e. unseaworthiness and/or error or fault in the navigation of the vessel (8(a)), loading, stowage and cargo handling (8(b)) and shortage and overcarriage (8(c)). Claims falling within the scope of 8(c) and 8(d) are split 50/50 unless it is possible to identify an "act or neglect" of one or other party. The Tribunal found that the charterers were liable for 100% of the cargo claim, although they were not at fault in loading the cargo or providing the orders that they did, because of their decision to use the vessel as floating storage for this particular cargo:

"Either Owners or Charterers must bear the risk of something going wrong caused, on our analysis, by Charterers' decision to not only protect their position but we sense actually profit from it. We can but conclude that this is a case where the ICA must regard Charterers' decisions as an "act" falling within clause 8(d) and bear 100% of the consequences."

The charterers appealed. The question on appeal was whether the allocation of 100% liability could apply where the cause of the damage was attributable to the non-culpable act of one party, or whether the relevant "act" required the party in question to be at fault, i.e. in breach of a contractual, tortious or some other form of obligation.

In the Commercial Court, Teare, J. recognised that there was no directly applicable precedent which could determine the point, and that it was necessary to construe clause 8(d) in light of the ICA as a whole. He was referred to cases dealing with the words "act, fault or neglect" in Article IV, r.3 of the Hague Rules, in which it had been suggested that "act" was not synonymous with the meaning of "fault" or "neglect" (see for example Hirst, L.J. in *The "GIANNIS NK" [1996] 1 Lloyd's Rep. 579).*

The charterers argued that the phrase "act or neglect" implied some element of fault and that the word 'act' must be coloured by the meaning of 'neglect'.

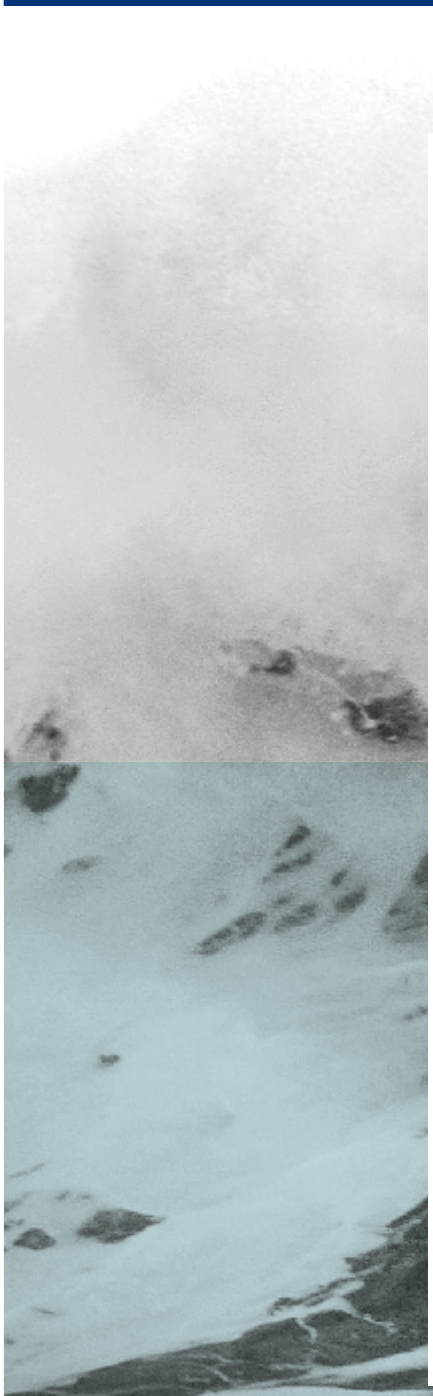
The court decided however that the word "act" in clause 8(d) can mean any act, whether culpable or not. The key to this provision is therefore to be able to identify, on the basis of clear and irrefutable evidence, the cause of the cargo damage and the party to whom that cause is attributable, irrespective of whether that party is at fault in that respect. Conversely, the 50/50 apportionment under clause 8(d) will continue to apply in cases where the cause of the cargo damage cannot be clearly determined or where it is attributable to neither the owners nor the charterers. The latter point is illustrated by the examples discussed during the appeal such as a claim by receivers against the owners for loss caused by delay as a result of a vessel's deviation in order to respond to a distress call: the cause of the loss in that case is the danger to which the master responds by deviating, as opposed to the master's decision to deviate, and a 50/50 apportionment would likely apply.

Teare, J.'s decision is in our opinion correct. While the ICA as a whole provides a mechanism for a 'rough and ready' apportionment of cargo claims, this decision confirms that clause 8(d) is able to accommodate cases both where there is insufficient evidence of the cause of the cargo damage or where it is caused by a third party, as well as those where there is clear evidence that the cause of the damage is attributable to the act of the owners or the charterers, even if there is no suggestion of fault.

Permission has been given for an appeal to the Court of Appeal.

WHAT IS A PACKAGE? THE HAGUE RULES AND BULK CARGOES

Until the recent case of *The "AQASIA" [2016] EWHC 2514 (Comm)*, there was no English authority determining whether Article IV rule 5 of the Hague Rules applied to bulk cargo. In this case, Sir Jeremy Cooke extensively reviewed the Rules themselves, the background work leading up to their drafting and the general law in this area.



The case concerns a cargo of fishoil in bulk, part of which was damaged during transit. Article IV rule 5 provides that the carrier's liability is limited to £100 *"per package or unit".* The relevant charterparty described the cargo as *"2,000 tons cargo of fishoil in bulk".* The bill of lading, though, referred to the cargo's weight in kilogrammes. Owners admitted liability but contended that they were entitled to limit liability to the sum of £100 per mt of cargo damaged.

It was common ground that the words *"per package"* could not apply to a bulk cargo, so the debate turned on the meaning of the word *"unit"* in Article IV rule 5. Although the owners put forward a number of detailed arguments, the Court held that the word *"unit"* did not apply to bulk cargoes. The word *"unit"* refers to a physical item (or composite of items) rather than an abstract unit of measurement. In His Lordship's words a *"unit"* is *"something akin to a package, namely a shipment unit, being a suitable item for shipment, not a unit of measurement".*

The Court's conclusion is in line with the majority of commentators and textbooks, as well as other common law jurisdictions on this point. It is hardly controversial, but does give welcome clarity in this area. In this respect, the type of items which might constitute a *"unit"* would be a car or a piece of machinery, which may not be *"packaged"* as such. The Hague-Visby Rules have different limitation provisions which allow for limitation on the basis of weight and therefore in cases governed by those Rules the outcome may differ.

As the point was argued, the Court nonetheless went on to consider how any limit based on a unit of measurement would have applied in the present case. The only realistic construction would be to apply to customary freight unit measure (i.e. the unit of measurement applied to calculate the freight). Because of the lump sum freight and the bill of lading using kilograms, the limitation figure would never have come to a sum lower than the claim.

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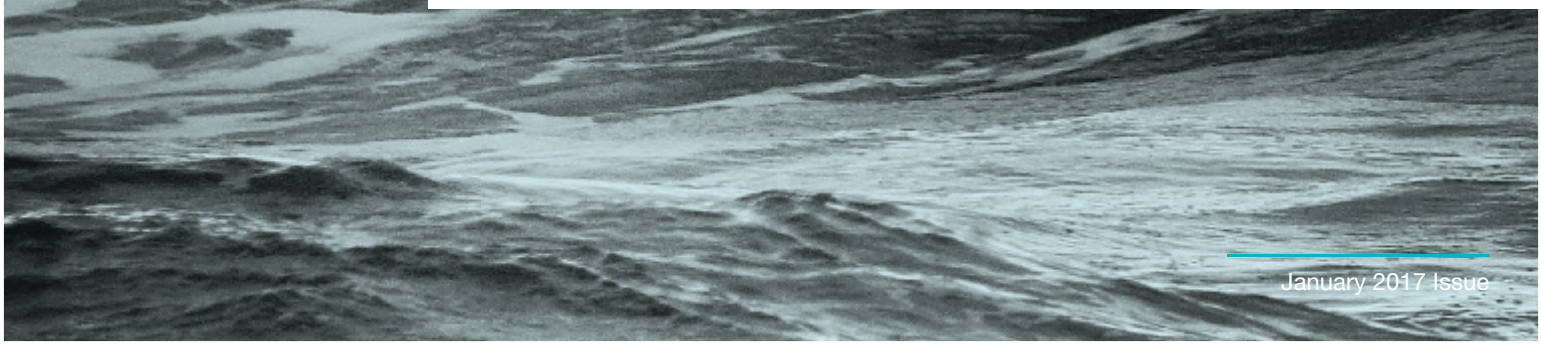

PROPER AND CAREFUL CARRIAGE UNDER THE HAGUE RULES: *VOLCAFE LTD AND OTHERS v COMPANIA SUD AMERICANA DE VAPORES SA [2016] EWCA CIV 1103*

The operation of Article III rule 2 of the Hague Rules is often unclear, particularly where a shipowner claims that an exception in Article IV rule 2 applies. It is common for there to be a dispute even as to basic matters such as who bears the burden of proof regarding the presence or absence of negligence where goods are shipped in good condition but discharged damaged. Recognising it as *"something of a test case"* the Court of Appeal has recently given some welcome guidance in this regard.

CSAV were carriers of nine consignments of bagged coffee beans loaded into unventilated containers from Columbia to Europe. The bills of lading were all on LCL/FCL terms (less than container load/full container load), so that CSAV's stevedores were responsible for preparing and stuffing the containers at the container terminal. Upon discharge some of the bags were found damaged by condensation.

All of the bills of lading incorporated the Hague Rules and recorded shipment in apparent good order and condition. Cargo interests alleged that insufficient or inadequate kraft paper was used to line the containers. It was common ground that condensation is inevitable when coffee beans are carried from a warm climate to a cold climate and that (regardless of the paper used) there was no certain way to prevent condensation damage to bagged coffee carried in lined, unventilated containers. It was also agreed that carriage in unventilated containers lined with kraft paper was common industry practice.

The Court of Appeal took the matter in stages: at stage one, it is for the cargo claimant to prove damage or non-delivery, although this is easily done where the bill of lading records shipment in good order and condition. At stage two, the burden is on the carrier to explain what happened to the goods whilst in its care, and to establish that the loss apparently falls within one or more of the exceptions in Article IV rule 2. The carrier, however, is not required to prove that the damage occurred without its negligence or notwithstanding that it properly and carefully carried the goods. Rather, there is a third stage where the burden is on the cargo claimant again to negative the operation of an Article IV rule 2 exception by establishing negligence or want of care on the part of the carrier.

In Mr Justice Flaux's view:

"…the fact that, in the case of the "catchall" exception in [Article IV] rule 2(q), it provides expressly that the burden of proof is on the carrier to disprove, inter alia, fault or neglect, is a strong pointer to the correct analysis being that, in the case of the other exceptions, including rule 2(m), the application of the exception is not dependent upon the carrier disproving negligence".

Since the damage was due to condensation and the source of the condensation was the coffee beans themselves, CSAV had made out a sustainable defence within Article IV rule 2(m) (inherent vice). The claimants then had to show that the cargo had not been carried *"properly"* (i.e. in accordance with a sound system). The system employed did not have to guarantee that no damage will occur, and compliance with general industry practice is one of the indicia of a sound system. On the evidence, the claimants could not establish that the cargo had not been carried properly, and the inherent vice defence succeeded.

As pointed out in argument, the vessel owner has possession of all the documents relating to what happened during carriage, and therefore it may be difficult for a cargo claimant to plead a positive case of negligence or want of care pending disclosure. However, many cases do not turn on the burden of proof and the carrier will need to put in evidence relating to any Article IV rule 2 exception relied upon. As such, difficulties faced may be more apparent than real, and the decision may prove a discouragement to opportunistic or spurious cargo claims.

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POST-DELIVERY DEFECTS UNDER SHIPBUILDING CONTRACTS – THE *"STAR POLARIS" [2016] EWHC 2941 (COMM)*

In recent years many ships have been constructed under an SAJ form shipbuilding contract (or an amended version of the same) and found, following delivery, to have defects. The "STAR POLARIS" was a vessel which suffered a serious engine failure shortly after delivery from the yard. Her buyers sought to recover repair costs and other losses suffered as a result of the engine failure, including towage costs, agency fees, survey fees and off-hire. In addition, a claim for diminution in value of the vessel was made.

In arbitration the Tribunal found that the yard had breached its warranty of quality due to weld spatters in the vessel's pipework. However, only part of the repair costs claimed were awarded because the chief engineer was negligent in not reacting to various alarms sooner. They ruled that buyers' other claims (including diminution in value) were excluded by Article IX(4)(a) of the shipbuilding contract, which provided that:

"the BUILDER shall have no liability or responsibility whatsoever or howsoever arising for or in connection with any consequential or special losses, damages or expenses unless otherwise stated herein".

Express exclusions of *"consequential"* or *"special"* losses have been construed in many cases, and they are usually held not to exclude loss which directly and naturally results in the ordinary course of events from the breach. In the present case it would be expected that the costs claimed would not be excluded if the phrase *"consequential or special losses"* were given its traditional meaning.

The Court held to the contrary. In the particular context it was found that the parties intended a different meaning. Apart from repair costs, the buyers' claims were all excluded by Article IX.4.

Article IX of the contract was an express and complete code governing the yard's liability for defects discovered following delivery. The only positive obligations assumed by the yard under that Article were to repair or replace defects and physical damage caused by such defects, or to pay the costs of repair or replacement if carried out at another yard.

This case turned on particular wording, but the similarities to Article IX of the standard form SAJ contract suggest that this case will be deployed by shipyards in many post-delivery defect disputes. The Article IX regime is known to be favourable to shipyards, and this decision appears to continue the trend of limiting post-delivery liability.

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ON DEMAND GUARANTEES AND BAREBOAT CHARTERS: *BITUMEN INVEST AS v RICHMOND MERCANTILE LIMITED FZC [2016] EWHC 2957 (COMM)*

Guarantees by parent companies or associates of contracting parties are a common feature of maritime trade. The value of such a guarantee in practical terms can often be less than originally contemplated. One common issue raised by a guarantor who does not wish to pay is whether the party entitled to the benefit of the guarantee must establish the liability of the party whose performance is guaranteed under the underlying contract, or whether the guarantee is an "*on demand*" guarantee and the sums are payable regardless of such liability.

The claimant owners claimed under a Deed of Guarantee signed by Richmond which guaranteed the liabilities of Windrush Intercontinental SA ("charterers") under a bareboat charter with owners. The bareboat charter was on *"hell or high water"* terms, meaning that hire was payable in all circumstances, without any set-off, counterclaim or off-hire, until expiry or termination of the charter or receipt of insurance proceeds following a total loss of the vessel.

Owners contended that the guarantee was an *"on demand"* guarantee; that they had made the required demands for sums due from charterers under the bareboat charter; and that Richmond had failed to pay under the guarantee.

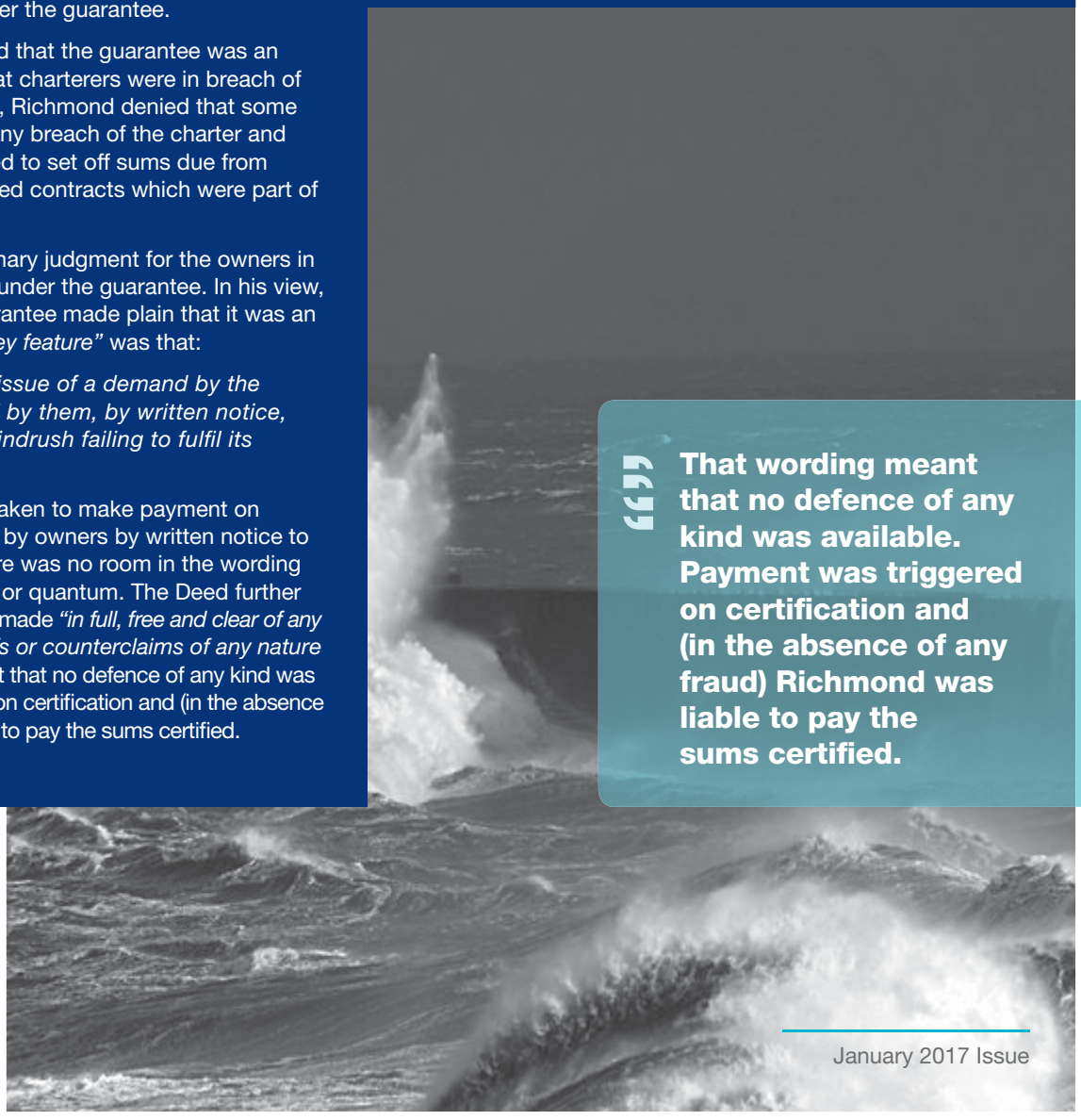
Unsurprisingly, Richmond denied that the guarantee was an *"on demand"* guarantee, and that charterers were in breach of the bareboat charter. In addition, Richmond denied that some of the costs claimed related to any breach of the charter and contended that they were entitled to set off sums due from owners to charterers under related contracts which were part of the financing of the vessel.

Sir Jeremy Cooke entered summary judgment for the owners in respect of the sums demanded under the guarantee. In his view, the wording of the Deed of Guarantee made plain that it was an *"on demand"* guarantee. The *"key feature"* was that:

"the trigger for payment is the issue of a demand by the Owners for an amount certified by them, by written notice, as due as a consequence of Windrush failing to fulfil its obligations under the Charter".

Richmond had expressly undertaken to make payment on demand of any amount certified by owners by written notice to be due from charterers, and there was no room in the wording for Richmond to dispute liability or quantum. The Deed further provided that payment should be made *"in full, free and clear of any deductions, withholdings, set-offs or counterclaims of any nature whatsoever"*. That wording meant that no defence of any kind was available. Payment was triggered on certification and (in the absence of any fraud) Richmond was liable to pay the sums certified.

There is authority to the effect that, outside the banking context, unless the document is described as a "*performance bond*" or an "*on demand bond*", there is a strong presumption against it being such. This guarantee, however, formed part of a financing transaction in the form of a sale and bareboat charter arrangement. As such, presumptions applicable to non-banking transactions were given much less weight. The bareboat charter and the guarantee were intended to ensure the cash flow for what was, in effect, a loan, which is why both expressly provided for payment to be without set-off, counterclaim or deduction.



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