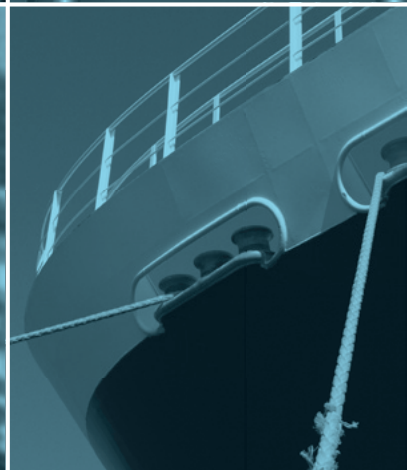
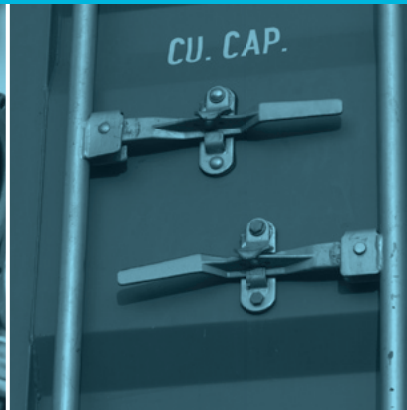




# Gard Guidance on Maritime Claims and Insurance

Richard Williams





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## Preface

I am pleased to present the latest publication in the 'Gard Guidance' series – the *Guidance on Maritime Claims and Insurance*. As always, a publication of this depth and breadth is a genuinely collaborative effort. We are delighted that it has been once again led by Richard Williams, Professor at the School of Law, Swansea University, with valuable assistance from a wide group of Gard experts. They have again contributed tremendous knowledge and enthusiasm to the project, and I am grateful to them for their efforts.

Knowledge and learning are key to Gard's core purpose: to help our Members and clients in the marine industries to manage risk and its consequences. To that end we invest significant resources in building the intellectual capital within our group, not only to improve our own operations but also as a resource for our Members and clients. Publications such as this one are tangible evidence of that commitment to being a learning organisation – committed to research, education and publication, and to share the best and most relevant information both internally and externally.

This Guidance is designed with the claims' manager in mind, offering practical assistance in the event of a maritime incident – whether large or small. It looks at the types of claims they might face, common issues that arise, which policies would respond, and some management issues that they should bear in mind. It is designed to be as relevant for those shipowners whose insurances are not with Gard, as for our Members and clients, and it looks across all the products in P&I and hull & machinery – as well offering a range of reference sources.

I hope that readers will find the *Guidance on Maritime Claims and Insurance* a useful companion to their work, and that it will become an invaluable source of reference and guidance offering readers an increased understanding of the risks and liabilities involved in modern ship operations.

**Claes Isacson**

Chief Executive Officer

Gard AS

April 2013

## Acknowledgements

This Guidance is the cumulative result of much exasperation that I and others have experienced over many years. Maritime incidents tend to result in complex claims and I have often heard the complaint that whilst there are many sources of guidance on specific issues, there is no 'one stop shop' that can give the unfortunate claims handler the guidance and direction that he needs to firstly, identify the likely issues that require attention, and to, secondly, formulate a sensible claims strategy. Therefore, when I learned some years ago that Gard were also hearing the same complaint from their Members, it was with some enthusiasm that I also learned that they had, typically, decided to do something about it. I was even more honoured to hear that they would like me to help them do so, and the road that we have travelled together whilst doing so has been educational, rewarding and enjoyable in equal measures.

I commented in the Acknowledgements to the *Gard Guidance to the Statutes and Rules* that *"I have been exceedingly fortunate to have had the assistance, support and encouragement of those whose expertise and experience I respect and value"*. I can repeat that comment in even greater measure on this occasion since this project has demonstrated even more clearly to me how fortunate Gard's Members and assureds are to have the help and support of a team that is so experienced, knowledgeable and dedicated to their welfare. I cannot really add much more to the comments that I have already made in this regard in the Acknowledgements to the *Gard Guidance to the Statutes and Rules*. However, I very much wish to repeat the following: *"This publication is the result not only of the raw material that has been provided by many Gard individuals based on actual cases and situations, but also of the many comments, observations and suggestions which have been made by them subsequently with the aim and desire of making this Guidance as helpful as possible to its readership. My task has been made so much easier by the fact that I have been able to rely on good, sensible and quick assistance and advice whenever it has been needed – and I assure you that it has often been needed!"*

It is not possible to thank each and every individual at Gard who has contributed to, and helped with, the production of this Guidance but you know who you are and I want you to know that I have genuinely appreciated and been exceedingly grateful for your contribution and support. However, particular thanks must be given to certain individuals. Kjetil Eivindstad has again demonstrated that he has the vision to identify worthwhile projects and the calm ability and determination to pursue them to fruition with patience and equanimity and with the minimum of fuss. He also has the knack of identifying issues which the other members of the team have overlooked or misunderstood.



Profound thanks must also be given to Nick Platt and Christen Guddal who have again made contributions that are way beyond the call of duty. Nick's font of knowledge and experience is a constant source of astonishment. There seems to be no situation that he does not seem to have encountered and he has the mature ability to suggest solutions that are both eminently sensible and helpful. The Claims Management chapter in Tier 4 is Nick's brainchild and is apt proof of his ability and long experience. Christen never fails to step up to the mark. If something needs to be done, it will be done, and it will be done both accurately and properly. Christen never leaves anything undone. These two gentlemen have again been the cornerstones upon which this Guidance has been founded. To repeat myself yet again: *"I can safely say without fear of contradiction that this Guidance would not have been possible without the support of these gentlemen"*.

I also wish to thank Randi Gaughan at Gard UK who has again brought order and control to offerings that have often been less than perfect in form and presentation. Randi is our 'style Guru' who leads us tactfully by the nose to a better and more stylish land!

Finally, I wish to convey my gratitude to Morten Lund Mathisen and Herman Steen of Wikborg Rein who, although not Gard employees, were, nevertheless, very ready to take time out of their busy professional lives to contribute their evident knowledge and experience to this project.

To end, I can do no better than to repeat the comment that I made in the *Guidance to the Statutes and Rules* and thank Gard *"for the opportunity to be involved with this worthwhile project. I repeat that I have learned much in the process and have had both the good fortune and the pleasure of learning from those whose knowledge and understanding is impressive and who have a real concern for the wellbeing of Gard and its Members"*.

**Richard Williams**

April 2013

## Introduction

Maritime incidents tend to be complex, complicated and time-consuming. They usually occur without much prior warning and require quick decisions to be taken, decisions which can have a major impact on the future handling of the incident and on the merits of the consequent claims and liabilities. In the early stages of the incident the personnel that are likely to be most directly affected are the ship's officers and crew and those shore based personnel designated by the particular organisation to have responsibility for emergency response in one capacity or another. The degree of experience possessed by such personnel will vary but they will all nevertheless, need to take immediate control of the situation.

Similarly, those who subsequently become involved in the handling of claims resulting from such an incident will need to have a firm sense of perspective overall in relation to the control of the claim, They will, no doubt, have assistance from experienced professionals such as surveyors, lawyers, insurance advisers and others. However, they will be the individuals responsible for gathering together the individual pieces of advice from such professionals and for moulding them into a sensible and rational strategy which can best serve the interests of the organisation that they represent.

All such personnel will need to consider issues affecting the ship, the crew, the cargo, the charterers, the authorities, the environment and a host of other interested parties that may have been affected. Their decisions will require an assessment of practical, operational, regulatory, legal and insurance issues. They will also be aware that a decision taken in relation to one issue is likely to have a major impact on all other related issues. They will need to develop a sensible strategy for dealing with all aspects of the incident. Yet, they may not feel confident that they have all the necessary experience or expertise to fully appreciate all the likely ramifications. They will need to decide what needs to be done and when, whom they should involve or consult, and at what stage to do so.

There are very many useful websites, books and other sources that can give detailed and comprehensive assistance in relation to most of the legal, commercial, operational, regulatory and insurance aspects of maritime activity.<sup>1</sup> However, they almost invariably focus on particular issues and do not give an overall, holistic commentary on the various types of problems and claims that can arise as a result of a maritime incident and, in particular, on how various issues interlink. Therefore, the aim of this publication is to identify the legal, practical and insurance problems that arise most frequently as a result of the most common type of maritime incidents, to provide guidance to those who have the responsibility to deal with such problems, and to identify where insurance can provide comfort. It is aimed not so much at the shipping professional but at claims handlers employed by shipping organisations who may feel that they often 'cannot see the wood for the trees' and who may be looking for comfort in that regard.

Whilst Gard would normally be involved in one way or another with most of the issues considered in this book, the book is not intended purely for Gard members or assureds but is intended to have wider application and to be of assistance to the shipping community generally.

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<sup>1</sup> See the sources itemised in Tier 5 (Help Centre).

# Contents

## **Tiers and Chapters**

The aim of this publication is to identify the legal, practical and insurance problems that frequently arise as a result of most types of maritime incidents, to provide guidance in relation to case handling and related issues and to identify and comment on the most relevant insurance products that can provide support and assistance and, most importantly, financial compensation for liability and loss. Consequently, each chapter has sections that comment separately on the relevant issues and case studies that illustrate those issues.

To assist the reader the handbook is structured in tiers each one of which comments on a particular issue in alphabetical progression. Tier 1 provides guidance on those claims that arise most often in relation to shipping operations whilst Tier 2 comments on more general issues that are usually relevant either individually or collectively in relation to such claims. Tier 3 comments on the insurance aspects of such claims whilst the reader will find in Tier 4 a detailed progressive commentary which, although based on a fictional case, comments on the issues that can be expected to arise in relation to such a scenario. Finally, Tier 5 (the Help Centre) provides the reader with further sources of assistance in the form of more detailed reading materials and contact details for specialist organisations. However, Gard does not recommend or endorse the use of any particular book or organisation.

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## Categories of Claims

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## Chapter 1

# Building and Sale and Purchase Claims

### 1.1 Introduction

Shipbuilding and ship sale and purchase (S&P) contracts are notorious breeding grounds for litigation. In one sense, such contracts are merely one form of sale of goods and are, therefore, subject to the sale of goods legislation that most countries have in one form or another for consumer protection. However, since ships are individual, shipbuilding and S&P contracts are normally subject to specifically negotiated detailed terms which are based on a limited number of standard contract forms.<sup>1</sup>

It must be emphasised at the outset that the rights and obligations of the parties to such contracts will depend heavily on the law and jurisdiction that may be agreed in the particular contract.<sup>2</sup> Therefore, the comments that follow must necessarily be read subject to the specific requirements of such law and jurisdiction.

### 1.2 Pre-Contractual Issues

The parties will normally engage in pre-contractual discussions prior to concluding a shipbuilding or S&P contract. The duties of the parties in such situations can vary depending on the law that may be relevant to such discussions<sup>3</sup> and it is not possible to comment in detail on all possibilities. However, there is no general duty of disclosure or good faith under the common law.<sup>4</sup> Nevertheless, any statements or promises that are made during such discussions which serve to encourage the other party to enter into the contract must be factually correct. If they are not factually

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1 See Chapter 1.4.1 below.

2 See Chapter 1.4.11 below and for more detailed commentary see Chapter 19 (Law and Jurisdiction).

3 See Chapter 1.3.4 below.

4 On the other hand, civil law countries recognise the duty to act in good faith in commercial dealings and this principle appears to be accepted more readily in the United States than in England and Wales. It is also true to say that some English judges have urged commercial parties to adopt this principle – see for example, the comments of Lord Justice Bingham in *Interfoto Picture Library Ltd v Stiletto Visual Programs Ltd* [1989] 1 QB 433.

correct, the party making such statements or promises is guilty of misrepresentation and the other party may be entitled either to claim damages for any loss or damage that it has suffered because it has relied on the accuracy of the statements etc., or, in some cases, to terminate the contract.

Silence during negotiations does not normally amount to misrepresentation whereas the making of a false statement can amount to misrepresentation. Therefore, if a ship that has a defective hull is offered for sale on an 'as is' basis despite the fact that the defect is known to the seller, the seller is not obliged to point this out to the buyer. However, if the seller were to say that the hull is in sound condition, that would be a misrepresentation.

### **1.3 Is there a Binding Agreement?**

The law of most countries will impose contractual responsibilities only when it can be said that the parties have reached an agreement. Until that moment has been reached, either party is free to discontinue the negotiations and to commence negotiations with any other party. However, once it can be said that the parties have reached agreement, there is a binding, legally enforceable contract between them, which means that if one of those parties fails thereafter to carry out its obligations under that contract, that party may be liable in damages to the other party.

Consequently, it is important to ascertain exactly at what stage of the negotiations it can be said that the parties have reached agreement. Such an agreement need not normally be recorded in a formal document that has been signed by both parties; all that is required is that there is evidence that a consensus has been reached by, for example, an exchange of faxes, emails etc.

In commercial practice it is common for such contracts to be negotiated through brokers in two stages. The parties will try firstly to reach agreement on the 'main terms' of the contract (e.g. the type of ship, its deadweight, loading capacity, propulsion systems, price, guarantors etc.) whilst leaving the more detailed terms (e.g. the contract form, law and arbitration etc.) to be worked out only if and when agreement is reached on the main terms. If the parties agree on the main terms, it is often said that they have agreed a fixture which is 'subject details'.

#### **1.3.1 'Subject Details'**

Opinions differ around the world as to whether, in these circumstances, a binding contract exists. It is a basic principle of English law that there is no concluded contract unless and until agreement has been reached on all relevant terms, which means that if there is still anything left to agree, there is no concluded agreement and either party can withdraw from the negotiations without penalty. Therefore, if

the recap provides that the fixture is 'subject details' there is no binding contract at that stage since the parties still have something left to agree. It was emphasized in one case that;

*" 'Subject details' is a well known expression in broking practice which is intended to entitle either party to resile from the contract if in good faith either party is not satisfied with the details as discussed between them."*<sup>5</sup>

The English court takes this view since it does not consider that it should interfere with the contracting freedom of commercial parties to decide for themselves whether a term is or is not acceptable. However, if the court is satisfied that the negotiations have reached the stage where the parties are in fact in agreement, and that any remaining issue that needs to be resolved is merely a matter of logical deduction or analysis, it may hold that there is a binding agreement. For example, if the negotiations have reached a stage where it is said, "main terms agreed subject to agreement of the contract form" there is unlikely to be a binding contract. However, the position might well be different if it were to be said "main terms agreed subject to logical amendments (or alterations) of the contract form." In the first case, the parties have still to agree on the appropriate contract form, whereas in the second case, they have agreed the form and, since it is merely a matter of logical analysis whether any amendments or alterations are necessary, the parties are deemed to have reached agreement on all relevant terms. Consequently, if the parties disagree on what is or is not logical, that issue can be decided by the court or arbitrators.

The English court also takes the view that even if the parties have agreed the main terms and most of the details, neither party is obliged in good faith to continue the negotiations to conclude agreement on the outstanding details. Therefore, until all details have been agreed, it is a case of 'all or nothing'.

However, US courts and arbitrators appear more ready to hold that the parties are legally bound to each other if the main terms have been agreed even though details have not yet been worked out. For example, it was said in one case that:

*"The details are not meaningful to the trade in the same way that the main terms of the fixture are, in as much as the fixture affects the trade directly and determines whether it will be a successful piece of business. When no amendment of details is agreed upon, however, the terms of the printed form govern."*<sup>6</sup>

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5 *The Nissos Samos* [1985] 1 Lloyd's Rep. 378 at page 385.

6 *Great Circle v Matheson*, 681 F.2d 121 (2d Cir. 1982).

### 1.3.2 Other 'Subjects'

Alternatively, the parties may have agreed on all the main terms and the details, but have agreed that the conclusion of the contract is subject to a condition that one of the parties requires to be satisfied, e.g. 'subject to survey' or 'subject to board approval'. The English court takes a similar and consistent view that there is no concluded contract unless and until the condition has been satisfied.

### 1.3.3 Counter Offers

Under the common law, there is an agreement when an offer has been unconditionally accepted. However, if the receiver of an offer does not accept it but makes a counter-offer, the counter-offer is treated as though it has destroyed the original offer. Therefore, once the counter-offer is made and rejected, the party that has made it cannot subsequently accept the offer which he had originally received before making that counter-offer. For example, if A were to offer to build a ship for USD 1 million but the offer is rejected by B, and B's counter-offer to buy the ship for USD 800,000 is rejected by A, B cannot then accept the original offer of USD 1 million even if this has not been expressly rejected in the meantime by A. B's counter-offer to buy the vessel at USD 800,000 has destroyed A's original offer to build the ship at a price of USD 1 million, and, therefore, A is free either to submit a new offer for another price or to build the ship for another customer.

### 1.3.4 The Governing Law

Because of the different approaches adopted by, for example, the US and English courts in relation to whether or not there is a fixture, it is important to determine which law should decide whether negotiations have resulted in a binding agreement. In normal circumstances, contractual disputes are determined in accordance with the law that is agreed to govern the contract. However, until the contract is agreed, it cannot be said that there is an agreed law. Therefore, there is a logical difficulty in applying an agreed law if the subject matter of the dispute is the very existence or otherwise of the contract. If both parties are resident in the same jurisdiction and the negotiations have been conducted in that jurisdiction, there is normally no difficulty since the issue will be determined by the courts of that country in accordance with its local law.

However, shipbuilding and S&P contracts are normally negotiated between two different parties or two different brokers who are resident in two different countries. Therefore, the problem is more complex since, for example, if the contract were to be negotiated between brokers who were resident in the UK and the USA, a court in the UK applying the law of England and Wales might conclude that there is no binding contract, whilst a court in the USA might conclude that there is a binding



contract. In such situations, parties often engage in forum shopping<sup>7</sup> and try to obtain the jurisdiction and law that is most favourable to them. However, that court will still have to decide which law should be applied to decide whether or not there is a binding contract.<sup>8</sup> The courts of different countries may well approach this issue differently. However, the approach that is adopted, for example, by the English court if it were the relevant forum for these purposes, is to decide the matter in accordance with the law that would govern the contract assuming (simply for these purposes) that the contract is in fact a binding fixture.

## 1.4 Shipbuilding Contracts<sup>9</sup>

The shipping community has always been susceptible to periodic ups and downs and such fluxes cause shipowners and shipbuilders to drastically re-evaluate the viability of contracts which were entered into in better times. A shipbuilding contract which appeared sensible and viable when concluded some years ago may begin to look completely unrealistic and unacceptable to one side or the other with the passage of time, particularly since substantial time may elapse between the signing of the contract and the launching of the ship that is to be built. Many factors contribute to this situation – the inability of shipbuilders to access raw materials at reasonable cost, political events and the depressed world economy have all had their impact. Both parties are affected by such factors and because there is always the possibility that breaches will occur, both parties will endeavour to ensure that their contracts give them rights to claim damages or to terminate the contract in the event of such occurrences, and that such rights are protected by third party securities. However, such factors are relevant not only in relation to current disputes. Experience gained in dealing with such disputes will be of great benefit in avoiding difficulties when drafting future contracts.

### 1.4.1 Contract Terms

Most shipbuilding contracts have traditionally been based on one of the following standard sale forms:

- The Shipbuilders' Association of Japan (SAJ) form;
- The Association of West European Shipbuilders and Shiprepairers (AWES) form;
- The Maritime Administration of the United States Department of Commerce (MARAD) form;
- The BIMCO standard NEWBUILDCON form;
- The Norwegian Shipowners' Association and Norwegian Shipbuilders' Association (SKIP 2000) form.

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<sup>7</sup> For more detailed commentary see Chapter 19.2 (Law and Jurisdiction).

<sup>8</sup> For more detailed commentary see Chapter 19.10 (Law and Jurisdiction).

<sup>9</sup> For more detailed commentary see *The Law of Shipbuilding Contracts* by Simon Curtis, Informa, 4th edition 2012.

In most cases, yards in the Far East have used the SAJ form but, in recent years, Chinese yards have started to use the China Maritime Arbitration Commission (CMAC) form. Similarly, European yards have tended to use the AWES form. However, these forms have been considered by some to favour the building yard and consequently, the BIMCO NEWBUILDCON is intended to operate as a more balanced framework of terms.

The terms of most shipbuilding contracts can be categorised as follows:

**a** General terms including:

- the design and description of the newbuilding;
- sub-contracting rights;
- the price, price adjustments and method of payment;
- inspection of work in progress;
- the power to make modifications to the contract and specifications;
- performance trials;
- the time and place of delivery;
- the documents that are required on delivery;
- transfer of title and risk;
- a warranty of quality;
- rectification of defects;
- *force majeure*.

**b** Detailed technical specifications and plans including:

- a detailed description of the hull, machinery and equipment of the new ship;
- details of the work to be carried out in relation to the hull, machinery and equipment;
- the manufacturing process that is to be adopted – e.g. type of welding/ steel plate;
- modification rights;
- requirements that are mandatory under conventions such as SOLAS, MARPOL, Load Line Convention etc.<sup>10</sup> The precise requirements will depend on the conventions adopted by the state where the ship is to be registered;
- Classification Society requirements;
- the tests and checks that must be carried out before and during sea trials;
- the builder's scale plans and drawings relating to the construction of the ship.

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<sup>10</sup> For more detailed commentary see Chapter 22.3 (Maritime Regulation and Compliance).

- c Securities and remedies such as:
- guarantees;
  - insurances;
  - assignments and third party rights;
  - the payment of liquidated damages for breaches of contract;
  - cancellation rights;
  - an entire contract clause (i.e. a clause specifying that the agreed terms are merely those contained in the written signed contract and that reference cannot be had to any other source material for further terms);
  - the choice of law and jurisdiction.

## 1.4.2 The Duties of the Parties

### 1.4.2.1 The Builder's Duties

The builder usually has a duty to:

- provide a refund guarantee (and if necessary register it with the relevant financial authority);<sup>11</sup>
- build a ship that is fit for purpose and of merchantable quality in accordance with the design specification and international good practice;<sup>12</sup>
- provide a design that is fit for purpose;<sup>13</sup>
- deliver the ship by the agreed delivery date;
- provide all agreed certificates that the ship may require in order to trade internationally.<sup>14</sup>

### 1.4.2.2 The Buyer's Duties

The buyer usually has a duty to:

- approve plans, drawings and specifications;<sup>15</sup> and
- provide agreed supplies to the builder for incorporation into the ship.<sup>16</sup>

However, the most important duties of the buyer are to:

- pay instalments of the purchase price as and when the same fall due;<sup>17</sup> and to
- take delivery of the completed ship.<sup>18</sup>

<sup>11</sup> See Chapter 1.4.9.1 below.

<sup>12</sup> Most contracts are subject to terms which mirror the implied terms found in the English Sale of Goods Act. However, the precise wording may differ depending on the contract. For example, Clause 1 of NEWBUILDCON provides that:

*"(a) the Builder shall design, construct, test and survey, launch, equip, complete, sell and deliver the Vessel to the Buyer all in accordance with good international shipbuilding and marine engineering practice."*

<sup>13</sup> Unlike Clause 1 of the NEWBUILDCON, the SAJ and AWES forms do not specifically make the builder responsible for design.

<sup>14</sup> See Clause 29 of NEWBUILDCON.

<sup>15</sup> See Clause 21(a) (ii) of NEWBUILDCON.

<sup>16</sup> See Clause 21 (a) of NEWBUILDCON.

<sup>17</sup> See Clause 15 of NEWBUILDCON.

<sup>18</sup> See Clauses 1(b), 28 and 32 of NEWBUILDCON.

### 1.4.3 Price and Payments

In most contracts, once the price is agreed, it remains the agreed price notwithstanding any subsequent movements in market price. However, shipbuilding contracts are relatively long term contracts and are therefore, more susceptible to market and political disruption. Consequently, shipbuilding contracts will often include terms which allow a builder to claim price variation if for example, there has been a substantial increase in the price of raw materials or a substantial movement in currency exchange rates. The contract may also allow price variation if it has been necessary to make substantial changes in specification during the construction.

In most cases, payment is to be made by instalments on completion of different stages of the construction such as:

- before commencing construction;
- on keel laying;
- on completion of hull;
- on launching.

However, since the buyer will be making advance payments he will need to be secured against default on the part of the builder and will usually require the builder to provide a refund guarantee to ensure repayment of instalments.<sup>19</sup>

### 1.4.4 Liquidated Damages

The law of most countries provides that if a party suffers loss or damage as a result of a breach of contract, that party is entitled to be financially compensated by the contract breaker by the payment of damages. However, the onus is on the claimant to prove the quantum of his loss and that can often be a difficult task. Consequently, it has become common for shipping organisations to agree that a breach is to be compensated by the payment of an agreed amount (i.e. liquidated damages) thereby, avoiding the need to prove actual loss. A classic example is the payment of demurrage for exceeding the agreed period of laytime in voyage charters.<sup>20</sup> Such provisions are also beneficial to the contract breaker since, if compensation has been agreed, the party that has suffered loss cannot claim more than the agreed compensation.

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<sup>19</sup> See Chapter 1.4.9.1 below.

<sup>20</sup> For more detailed commentary see of Chapter 4.5.6.1.1 (Charterparty Claims).

For these reasons most shipbuilding contracts include liquidated damages provisions which provide that the buyer will be compensated by an agreed reduction in the price in the event of specified breaches. The specific terms may vary depending on the particular contract, but the following are common terms:

- a limited period of delay for which no compensation is payable;
- an agreed reduction in the price for delays exceeding an agreed period caused by *force majeure* events or similar 'permitted' events;
- an agreed reduction (possibly a greater reduction) in the price for delays caused by other non-permitted events;
- an agreed reduction in the price for failures to meet specification requirements;
- a right given to the buyer to cancel the contract in the event of longer periods of delay or of excessive deficiencies in specification.

For example, the NEWBUILDCON form contains the following provisions for the payment of liquidated damages (in the form of a reduction in the price): Clause 8 (Speed Deficiency), Clause 9 (Excessive Fuel Consumption), Clause 10 (Deadweight Deficiency), Clause 11 (Cubic Capacity Deficiency), Clause 12 (Other Deficiencies) and Clause 13 (Late Delivery for Non-permissible delays).

### 1.4.5 Title to the Ship

Title to the ship should obviously pass to the buyer on delivery of the completed ship and payment of the full price. However, problems may arise during the construction and it may be necessary to decide who has title to the partially constructed ship before it is completed. Therefore, shipbuilding contracts will normally provide either that title in the ship remains with the builder until delivery and payment of the full purchase price<sup>21</sup> or that title in the ship will pass to the buyer during the construction as and when the ship is built subject to the builder's lien<sup>22</sup> for the price. Despite the apparent advantage to a buyer of the second alternative, it is often not a real advantage since the buyer may find it difficult, if not impossible, to obtain possession of the partially constructed ship in the builder's yard. Furthermore, even if he were to succeed in doing so, he would be obliged to bear a major expense to relocate the ship to another yard to complete the construction. Consequently, buyers tend to prefer the first alternative and rely on a refund guarantee to recover any instalments that have been paid.<sup>23</sup>

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21 For example, Clause VII.5 of the SAJ form provides that, "until delivery is effected, title to and risk of loss of the Vessel and her equipment shall be in the Builder, excepting risks of war, earthquake and tidal wave."

22 For more detailed commentary on liens see Chapter 24.3 (Security Enforcement Measures).

23 See Chapter 4.9.1 below.

### 1.4.6 Force Majeure

Shipbuilding contracts usually place strict responsibility on the buyer to pay instalments in full<sup>24</sup> and on time and this obligation is generally unaffected by any *force majeure* or exception clauses. If the buyer fails to pay instalments on time the builder may either suspend services or, in extreme circumstances, terminate the contract.<sup>25</sup>

However, the parties recognise that the ability of the builder to provide a completed ship on time and in accordance with the contract description may be affected by numerous events which are beyond the builder's control. Consequently, shipbuilding contracts usually include detailed clauses which are intended to protect the builder against liability for:

- damage to, or loss of, the ship; and/or for
- delay in the construction of the ship.

#### 1.4.6.1 Damage to, or Loss of, the Ship

Most shipbuilding contracts provide that the risk and title to the ship during the construction process lies with the builder. However, since the buyer and the builder will both have an interest in the continued well-being of the ship during the construction, the contract will normally provide that the builder is to take out standard 'Builder's Risks' insurance for their joint benefit and that the insurance proceeds should be used to complete the construction. For example, the SAJ form provides that the builder is obliged to keep the structure that is being built fully insured under the Japanese Builder's Risk Insurance terms and is required, unless the ship is a total loss, to apply the insurance proceeds to repair the damage to the satisfaction of the Classification Society.<sup>26</sup>

#### 1.4.6.2 Delay in the Construction of the Ship

The event giving rise to the damage may also cause delay to the construction of the ship. Consequently, the contract will normally include a *force majeure* clause which will entitle the builder to demand an extension of the delivery date. Such clauses normally list the qualifying events in detail but provide that the events must have been beyond the builders' control and not caused by his negligence. This reflects the general principle that a party will not, in the absence of clear words, be entitled to the benefit of exemption where the particular event is caused by the negligence of that party.

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<sup>24</sup> For example Clause 17 of NEWBUILDCON emphasises that the buyer is not entitled to rely on any right of set-off.

<sup>25</sup> See Clauses 15(d)(v) and 39(b) and (c) of NEWBUILDCON.

<sup>26</sup> For more detailed commentary see Chapter 26.4 (The Structure of Marine Insurance).

For example, Clause 34 of NEWBUILDCON lists 16 events that will entitle the builder to demand an extension and then sub-paragraph (iii) goes on as follows:

*“Provided that in respect of (i) and (ii) above:*

- (1) such events were not caused by the error, neglect, act or omission of the Builder or its Sub-contractors; and*
- (2) were not, or could not reasonably have been foreseen, by the Builder at the date of the Contract: and*
- (3) the Builder shall have complied with Sub-clause (b) hereunder; and*
- (4) the Builder shall have made all reasonable efforts to avoid and minimise the effects such events have on the delivery of the Vessel.”*

The provisions of the SAJ and AWES are not so precise. Therefore, it is important to read the particular clauses of each contract form closely.

#### **1.4.7 Warranty Period and Terms**

Shipbuilding contracts normally require the ship on completion of construction to undergo trials and inspections before she is accepted by the buyer. If such trials and inspections reveal that the vessel does not satisfy the contract requirements then the buyer is often placed on the horns of a dilemma since the contract may provide that:

*“Acceptance of the Vessel shall be final and binding so far as conformity of the Vessel to this Contract and the Specifications is concerned.”<sup>27</sup>*

In such circumstances, the buyer’s sole remedy, if he elects to take delivery, may be the post-delivery warranty that is normally provided by the builder. Therefore, the precise wording of the contract is important.

The contract will usually provide that the builder’s liability for defects discovered after delivery of the completed ship is to be limited to an agreed period of time in accordance with the terms of a guarantee (or ‘warranty’) which is to replace any other remedies which would otherwise be available at law. For example, under Article IX.1 of the SAJ form, the builder undertakes for one year after delivery to remedy free of charge any defects in the vessel *“which are due to defective material and/or bad workmanship on the part of the Builder or its subcontractors”*.

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<sup>27</sup> Article VI.5 of the SAJ form.

Article IX.4 (a) goes on to provide that *“The Builder shall have no responsibility for any other defects whatsoever in the Vessel than the defects specified in Paragraph 1 of this Article”* and that the Builder is not *“responsible or liable for any consequential or special losses, damages or expenses including but not limited to, loss of time, loss of profit or earnings or demurrage directly or indirectly occasioned to the Buyer by reason of the defects specified in paragraph 1.”*

Finally, Article IX.4(c) specifies that the warranty *“replaces and excludes any other liability, guarantee, warranty and/or condition imposed or implied by law, customary, statutory or otherwise, by reason of the construction and sale of the Vessel.”*<sup>28</sup>

### 1.4.8 Documentation and Delivery

The shipbuilding contract will normally specify the delivery procedures and the documentation that the builder will have to provide on payment of the final instalment of the price. The most usual documents are the following:

- a builder’s certificate or bill of sale in a form acceptable to the authorities in the ship’s flag state confirming that the buyer has title to the ship free of encumbrances;
- any additional documents that may be reasonably necessary to register the ship with her flag state;
- an inventory of all equipment, spare parts, stores, fuel etc., that is supplied with the ship;
- all relevant trading and classification certificates;
- an original warranty guarantee.

### 1.4.9 Securities

#### 1.4.9.1 Security to the Buyer

Shipbuilding contracts will normally require the builder to provide a refund guarantee from some third party trusted by the buyer who will promise to repay the various instalments quickly and without complication when called upon to do so. Most standard forms expressly include such a requirement and provide that such a guarantee must be established before payment of the first instalment. They also go on to provide that the contract may be terminated if such a guarantee is not provided in accordance with the provisions of the contract. For example, Clause 14 of NEWBUILDCON states that:

*“(b) Builder’s Refund Guarantee*

*To secure the Builder’s obligation to refund the Buyer’s pre-Delivery instalments pursuant to this Contract the Builder shall, within the number of days stated in Box 19 (b) (i) after the signing of this Contract and before the date of payment of*

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<sup>28</sup> Similar provisions are found in Clause 37(d) of NEWBUILDCON.



*the first instalment in accordance with clause 15 (a) (i) (Payments – Instalments), provide the Buyer with a Refund Guarantee issued by the bank or party named in Box 32 substantially in the form and substance set out in Annex A (iii) (Refund Guarantee), failing which the Buyer shall have the option to terminate this Contract in accordance with Clause 39 (a) (ix) (Suspension and Termination).”*

However, it is important to ascertain whether the particular standard form of shipbuilding contract that is intended to be used provides for the provision of such a refund guarantee. The SAJ form does not do so and, therefore, it is important for a buyer to ensure that a special clause to this effect is included in the final contract.

Furthermore, it is important to ensure that all necessary formalities are complied with. For example, guarantees provided by local financial institutions in China are not enforceable unless and until the guarantees have been registered with the Chinese financial regulator (the State Administration of Foreign Exchange (SAFE)). Most modern contracts and refund guarantees require the guarantor to confirm that the guarantee satisfies all local regulations.<sup>29</sup> However, whilst breach of such a term might well give the buyer a claim for the same amount against the guarantor for breach of contract or for misrepresentation,<sup>30</sup> the merits of such a claim are uncertain and would not provide the unfettered right to repayment of instalments which was the purpose of the refund guarantee. Consequently, it is good policy for buyers to ensure (preferably by a provision in the shipbuilding contract itself) that the first instalment need not be paid until after the buyer has received satisfactory confirmation that the guarantee has been approved by, and registered with, SAFE. SAFE will normally issue the guarantor with a Certificate of Foreign Security on completion of registration proving that the guarantee has been duly approved and registered.

#### **1.4.9.2 Security to the Builder**

Prompt payment of instalments is important to the builder for cash flow purposes and, should the buyer fail to do so, the builder will normally be entitled to various remedies. For example, NEWBUILDCON has the following provisions:

- Clauses 18 and 39 provide that the builder can claim interest at the agreed rate for late payments.
- Clause 39(c) provides that the builder can suspend work until payment is made if an instalment is more than 15 days late.
- Clause 39(b)(ii) provides that the builder can give the buyer five days' notice of his intention to terminate the contract if an instalment is more than 21 days late, and can terminate if payment is not made within those five days.

<sup>29</sup> See Clause 14(c) of NEWBUILDCON and Clauses 12-14 of the specimen Refund Guarantee in Annex A (iii) to the NEWBUILDCON.

<sup>30</sup> See *Guangzhou Dockyards v ENE Aegiali*, [2011] 1 Lloyd's Rep. 30.

However, in the same way that the buyer may be reluctant to trust the creditworthiness of the builder, the builder may be reluctant to trust the creditworthiness of the buyer and require the buyer to provide a guarantee from a trusted third party guaranteeing performance by the buyer of his obligation to pay instalments at the agreed stages, failing which the builder may be entitled to terminate the contract. For example, Clause 14 of NEWBUILDCON has the following provision:

*“(a) Buyers’ Instalment/Performance Guarantee*

*To secure the Buyer’s obligation to pay the instalments of the Contract Price prior to delivery the Buyer shall within the number of days stated in Box 19 (a) (i) after the signing of this Contract deliver to the Builder an irrevocable and unconditional guarantee issued by the bank or party named in Box 31 substantially in the form and substance set out in Annex A (i) (Instalments) or Annex A (ii) (Performance) stated in Box 19 (a) (ii), failing which the Builder shall have the option to terminate this Contract in accordance with Clause 39 (b) (iv) (Suspension and Termination).”*

Clause 39 then states that

*“(b) Builder’s Termination*

*The Builder shall have the right to terminate this Contract forthwith upon giving notice in the event that:*

- (i) the guarantor providing the Instalment Guarantee or Performance Guarantee on behalf of the Buyer...is deemed insolvent pursuant to Sub-clause (d) below, unless the Buyer can provide a replacement Performance Guarantee acceptable to the Buyer within 30 days and provided that notice of termination is given before an acceptable Buyer’s Instalment or Performance Guarantee is received by the Builder.”*

### **1.4.9.3 Types of Security**

It is important to appreciate that there are fundamental differences between:

- securities which cannot be called upon until it has been proved in law that the primary debtor is in default, and which are subject to all the terms and defences that are available to the primary debtor (i.e. true guarantees in which the liability of the guarantor is secondary to that of the debtor); and
- securities which may be enforced immediately on the happening of an agreed event, or on presentation of an agreed document, without proof that the primary debtor is liable at law and which are not subject to all the terms and defences which are available to the primary debtor (i.e. standby credits in which the guarantor is a primary obligor).

These differences are important since:

- If the security is in the form of a standby credit (a primary obligation), amendments to the shipbuilding contract do not discharge the guarantor from liability under the standby credit. However, if the security is a true guarantee (a secondary obligation) then, unless the guarantee provides otherwise, amendments to the shipbuilding contract may discharge the guarantor from liability under the guarantee.
- Similarly, if the security is in the form of a standby credit, the granting of any indulgence to the beneficiary under the shipbuilding contract (e.g. giving a time extension) does not discharge the guarantor from liability under the standby credit. However, if the security is a true guarantee then, unless the guarantee provides otherwise, the granting of such an indulgence may discharge the guarantor from liability under the guarantee.

These differences proved fatal in the English case of *ABP v Ferryways*<sup>31</sup> since the parties to the underlying contract had agreed subsequently to amend that contract. Consequently, when the beneficiary sought to enforce the guarantee in the light of the bankruptcy of Ferryways, the guarantors refused to pay in view of the amendment to the underlying contract.

In order to avoid these difficulties the various guarantees that are found in Annex A of NEWBUILDCON provide expressly that the guarantor:

*“irrevocably and unconditionally guarantee (but as primary obligor and not by way of secondary obligation only) ...”*

and that:

*“This guarantee shall not be affected by any indulgence or delay allowed to (the beneficiary) nor by any amendment to or variation of the Contract ...”*

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<sup>31</sup> [2009] 1 Lloyd's Rep. 595.

#### 1.4.10 Assignability

Since the buyer may well be obliged to borrow a substantial part of the cost of construction before acquiring title it is very important that the benefit of the shipbuilding contract, the insurance policy and the refund guarantee is assignable to the financiers and that they are in terms that are satisfactory to the buyer's financiers. For example, the guarantees that are found in Annex A of NEWBUILDCON have provisions such as the following:

*"Notwithstanding any provision in the Contract, this Guarantee shall be freely assignable by you and any assignee. Upon assignment, all references in this Guarantee to "you" shall be read as references to the assignee or subsequent assignees."*<sup>32</sup>

Furthermore, for the reasons given above,<sup>33</sup> it is important that the guarantee should comply with and satisfy all requirements of local law to ensure that it is enforceable by the beneficiary.

#### 1.4.11 Law and Jurisdiction<sup>34</sup>

The merits of a claim can depend heavily on the law that governs the contract and the jurisdiction where the claim is to be determined. Consequently, the law and jurisdiction clause of a shipbuilding contract is a vital component of that contract, particularly since it may be necessary in due course to enforce a judgement or arbitration award obtained in that jurisdiction in the country where the defendant or respondent carries on business. For these reasons, parties to shipbuilding contracts generally prefer to agree 'neutral' law and jurisdictions such as that of England and Wales.<sup>35</sup> However, it should be remembered in this regard that judgements of the English court are not necessarily enforceable in countries such as China since there are no reciprocal enforcement treaties between China and the United Kingdom. On the other hand, China is a party to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 and an award made by London arbitrators is enforceable in China pursuant to that convention.<sup>36</sup> Therefore, an arbitration clause may be more beneficial than English court jurisdiction for a claimant in such a situation.

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32 Clause 8 of the Refund Guarantee in Annex A (iii). A similar provision is found in Clause 8 of the Buyer's Irrevocable Letter of Guarantee for the 2nd and 3rd Instalments in Annex A (i).

33 See Chapter 1.4.9.1 above.

34 For more detailed commentary see Chapters 19.5 and 19.10.1 (Law and Jurisdiction).

35 *In Guangzhou Dockyards v ENE Aegiali*, [2011] 1 Lloyd's Rep. 30 it was held that where the shipbuilding contract is subject to English law but the associated guarantee is silent in that respect, the guarantee is implicitly also subject to English law.

36 See Chapter 19.5.1 (Law and Jurisdiction).

On the other hand, if the relevant party were to be domiciled in the European Union then it might be preferable to make the contract and/or securities subject to the jurisdiction of the English High Court since, pursuant to Article 23 of Regulation No. 44/2001 of the European Union, “such jurisdiction shall be exclusive unless the parties have agreed otherwise” and any judgement that may be given by such court will be enforced without reconsideration of the merits in all other EU states pursuant to Article 33 of the Regulation.<sup>37</sup>

It is important to remember that most standard form contracts will have law and jurisdiction clauses of one sort or another which may or may not be advantageous for the particular party. The AWES form leaves it to the parties to decide which law and jurisdiction is to apply whereas the SAJ and CMAC forms provide expressly for Japanese and Chinese law and jurisdiction. The MARAD form envisages that US law and jurisdiction will apply whereas NEWBUILDCON allows the parties to make their own choices for law and jurisdiction, but provides that English law and London arbitration will apply unless the parties opt for another alternative. Therefore, whatever form is used, it is always important to consider various possible alternatives before agreeing the final clause.

## 1.5 Sale and Purchase Contracts<sup>38</sup>

S&P contracts are normally negotiated in much the same way as shipbuilding contracts and, therefore, much of the commentary that is made above in relation to shipbuilding contracts is equally applicable to S&P contracts.

Most S&P contracts are concluded on the Norwegian Sale Form (NSF) 1993 although some contracts are based on the Nipponsale 1993 or 1999 forms.

### 1.5.1 Inspection

In the majority of cases, a buyer will be prepared to conclude the contract only after he has inspected the ship. Such inspection normally encompasses:

- a physical inspection of the ship; and
- an inspection of the vessel’s records.

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<sup>37</sup> See Chapter 19.6.1.1 (Law and Jurisdiction).

<sup>38</sup> For more detailed commentary see *Sale of Ships* by Strong and Herring, Sweet & Maxwell, 2nd edition 2010.

For example, Clause 4 a) of the NSF 1993 provides that:

*“The Buyers have inspected and accepted the Vessel’s Classification records. The Buyers have also inspected the Vessel at/in ... on ... and have accepted the Vessel following this inspection and the sale is outright and definite subject only to the terms and conditions of this Agreement.”*

The scope and extent of the inspections will depend on what the parties have agreed but the physical inspection will normally include all cargo compartments, ballast tanks, hull, decks, machinery spaces and accommodation. The inspection will also normally include the ship’s logs and may involve some testing of structure and equipment.

The inspection of records will almost certainly include the vessel’s classification records including correspondence between the classification society and the ship and may also include inspections of any possible mortgage or encumbrance registers to ensure that the ship is not subject to any maritime liens that would be binding on the new owner after purchase.<sup>39</sup> The buyer can also be expected to have searched other databases such as Equasis to see whether the ship has had problems with Port State authorities.<sup>40</sup>

### **1.5.2 Completion**

The contract normally provides that it will be performed when:

- the vessel is delivered by the seller to the buyer in the condition specified by the contract at an agreed port of delivery; and
- the agreed documents are delivered by the seller to the buyer; and
- the buyer has paid the agreed price to the seller.

To enable the parties to arrange all the necessary formalities for completion the contract will normally provide that the seller is to give the buyer a notice of readiness specifying when the vessel will be ready for delivery to the buyer.

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<sup>39</sup> For more detailed commentary on maritime liens see Chapter 24.4 (Security Enforcement Measures).

<sup>40</sup> See Chapter 22.3.3.5 (Maritime Regulation and Compliance).

### 1.5.2.1 Delivery of the Vessel

The contract will normally provide in one way or another that the sellers must deliver the vessel:

- in the condition that she was in at the time of the prior inspection, fair wear and tear excepted;
- with her present class maintained free of recommendations;
- free from all encumbrances and maritime liens; and
- having satisfactorily passed an underwater inspection.

The contract will normally provide that the underwater parts of the ship will be inspected by her classification society at the agreed delivery port prior to delivery. For example, Clause 6 a) of NSF 1993 provides that:

*“The Sellers shall place the Vessel in drydock at the port of delivery for inspection by the Classification Society of the Vessel’s underwater parts below the deepest load line, the extent of the inspection being in accordance with the Classification Society’s rules. If the rudder, propeller, bottom or other underwater parts below the deepest load line are found broken, damaged or defective so as to affect the Vessel’s class, such defects shall be made good at the Seller’s expense to the satisfaction of the Classification Society without condition/recommendation.”*

However, the parties frequently agree that the vessel shall be inspected initially by a diver approved by the classification society and that she will be drydocked only if this is thought necessary following the diver’s inspection.

If the inspection indicates that the vessel is in a fit condition then the contract will usually provide that the ship is to be delivered to the buyer together with whatever spares and additional equipment that may have been agreed. For example, Clause 7 of NSF 1993 provides that:

*“The Sellers shall deliver the Vessel to the Buyers with everything belonging to her on board and on shore. All spare parts and spare equipment including spare tail-end shafts and/or spare propellers, if any, belonging to the vessel at the time of inspection, used or unused, whether on board or not shall become the Buyer’s property, but spares on order to be excluded.”*

### 1.5.2.2 Delivery of Documents

The contract will also require the seller to deliver to the buyer a substantial number of documents, the purpose of which is to prove that the seller is entitled to sell the ship and that the ship is free of encumbrances and maritime liens that may be prejudicial to the buyer's unrestricted enjoyment of the vessel as a trading vehicle. The contract may also provide that such documents should be made available in a highly formal format. For example, Clause 8 of NSF 1993 provides that the seller must provide the following documents:

- A Legal Bill of Sale recordable in (the country in which the Buyers are to register the Vessel), warranting that the Vessel is free from all encumbrances, mortgages and maritime liens or any other debts or claims whatsoever, duly notarially attested and legalised by the consul of such country or other competent authority;
- A current Certificate of Ownership issued by the competent authorities of the flag state of the Vessel;
- Confirmation of Class within 72 hours prior to delivery;
- Current Certificate issued by the competent authorities stating that the Vessel is free from registered encumbrances;
- A Certificate (or similar official evidence) of Deletion of the Vessel from the Vessel's registry;
- Any additional documents that may reasonably be required by the competent authorities for the purpose of registering the Vessel.

However, a buyer will usually also require evidence that the sale of the vessel has been authorised by the corporation that currently owns the ship. Therefore, the contract may also require the following:

- A Certificate of Goodstanding of the sellers issued by the corporate registry where the selling company is registered;
- A notarised and apostilled certificate identifying the directors and officers of the selling company and of any board or shareholders' resolutions authorising the sale, accompanied by copies of the company memorandum and articles of association;
- An original notarised and apostilled power of attorney of the sellers authorising the officer executing the Bill of Sale, Protocol of Delivery and all other documents that are necessary to complete the sale.



### 1.5.2.3 Payment of the Price

The contract will usually provide that a percentage of the agreed price (normally 10 per cent) will be paid within an agreed number of days of concluding the contract and that the balance will be payable on completion. However, the contract may give the buyer the right in some cases to withhold an agreed percentage for a period of a few months after completion to ensure that the ship is not in fact subject to encumbrances or maritime liens.

The method of payment will depend on what the parties have agreed but whichever method is chosen, care must be taken to ensure that the payment procedures must dovetail with whatever measures that are necessary to either extinguish or create any mortgage rights that may be affected by the sale.

## 1.5.3 Breaches of Contract

### 1.5.3.1 Breaches by the Seller

The main duty of the seller is to deliver the ship:

- on time;
- in accordance with the terms of the contract; and
- free of encumbrances.

#### 1.5.3.1.1 Delivery on time

The time of performance is not normally a fundamental term in contract law so that the innocent party's remedy is normally restricted to claiming damages for any loss that he proves that he has suffered as a result of the delayed delivery. However, there is nothing in principle to prevent parties from agreeing that if the ship is not delivered by an agreed time, the innocent party is entitled to cancel the contract. Consequently, Clause 14 of NSF 1993 provides that:

*"Should the Seller fail to give Notice of Readiness in accordance with Clause 5 a) or fail to be ready to validly complete a legal transfer by the date stipulated in line 61 the Buyers shall have the option of cancelling this Agreement ..."*

The buyer may also claim damages for any losses that they have suffered if they prove that the failure to deliver on time was the result of the seller's negligence and was not caused by circumstances beyond their control. Indeed, it is likely that the buyer could also claim damages in such circumstances even if he chose not to exercise his option to cancel.<sup>41</sup>

<sup>41</sup> In this regard, the position is similar to the right that is given to voyage charterers to cancel the charter if the ship is not ready to load by an agreed time and date. See Chapter 4.4.3.2.1 (Charterparty Claims).

#### 1.5.3.1.2 *Delivery in Accordance with the Terms of the Contract*

Clause 11 of the NSF 1993 provides that:

*“The Vessel with everything belonging to her shall be at the Seller’s risk and expense until she is delivered to the Buyers but subject to the terms and conditions of this Agreement she shall be delivered and taken over as she was at the time of inspection, fair wear and tear excepted. However, the Vessel shall be delivered with her class maintained without condition/recommendation, free of average damage affecting the Vessel’s Class, and with her classification certificates and national certificates, as well as all other certificates the Vessel had at the time of inspection, valid and unextended without condition/recommendation by Class or the relevant authorities at the time of delivery.”*

This provision requires the seller to deliver the ship in the same condition as she was in at the time of the earlier inspection subject only to fair wear and tear. However, the precise parameters of the phrase ‘fair wear and tear’ are notoriously difficult to pin down. The phrase refers to the kind of deterioration that is caused by normal trading activity. In normal circumstances, the ship is unlikely to suffer a substantial degree of such damage during the relatively short time between inspection and delivery to the buyers. However, if the vessel is allowed to complete a number of voyages in that period and suffers some degree of grab damage whilst loading and discharging, arguments can easily arise as to whether such damage can truly be said to be ‘fair wear and tear’ which absolves the sellers from liability.

Secondly, the ship’s class status and her status for the purposes of the various compulsory conventions<sup>42</sup> that regulate maritime safety must remain in an unimpaired condition at the time of delivery.

#### 1.5.3.1.3 *Delivery free of Encumbrances*

It is a traditional characteristic of maritime law that certain types of claim can follow the ship into the hands of a buyer and make the buyer responsible for those claims notwithstanding the fact that the claims have been caused by the prior owners. In such circumstances, the claimant is also entitled to arrest the ship in her new ownership and require the new owner either to pay the claim or to put up security for any judgement that may be rendered against the new owner in due course. If the new owner fails to pay the claim or to put up satisfactory security, the claimant is entitled to apply to the court of the country where the ship has been arrested for

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<sup>42</sup> For more detailed commentary see Chapter 22.3.1 (Maritime Regulation and Compliance).

an order that the ship be sold so that the proceeds of sale can be used to settle the claim.<sup>43</sup> Therefore, it is very important for a buyer to ensure that the ship is free of encumbrances and maritime liens at the time of delivery.

In some countries, the flag state authorities record details of any such claims in a public register and, therefore, the buyer can protect himself to some degree by inspecting such a register before agreeing to buy the ship. However, not all countries operate such a scheme, and it is possible that an encumbrance or maritime lien may have been incurred and remains undetectable in a country pending the arrival and subsequent arrest of the ship in that country in due course. Consequently, the buyer will normally require the seller to confirm that the ship is in fact free of such difficulties.

Clause 9 of NSF 1993 provides that:

*“The Sellers warrant that the Vessel, at the time of delivery, is free of all charters, encumbrances, mortgages and maritime liens or any other debts whatsoever. The Sellers hereby undertake to indemnify the Buyers against all consequences of claims made against the Vessel which have been incurred prior to the time of delivery.”*

Whilst this clause imposes a duty on the seller to indemnify the buyer, that indemnity may not in fact be of much practical value if the ship is owned by a one-ship company which is then dissolved and the proceeds of sale distributed to its shareholders. Therefore, a buyer will normally wish to have additional security, but the prospects of doing so depend very heavily on the price that is offered, the state of the market and the financial standing of the seller. Nevertheless, the buyer may consider the following:

- request the seller to provide a guarantee of performance from a trusted third party; or
- purchase maritime lien insurance; or
- retain a percentage of the sale proceeds for a period to see whether claims are made.

#### **1.5.3.1.4 Damages**

In normal circumstances, the damages that are payable to a purchaser of goods who has not received the goods is the difference between the agreed contract price and the price that he may be obliged to pay to another seller to obtain the same goods. However, since ships are individual, it may not be possible to obtain an exact substitute if the seller fails to deliver the promised ship. Therefore, it may be difficult

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<sup>43</sup> For more detailed commentary see Chapter 24.4 (Security Enforcement Measures).

for the buyer to prove his exact loss. Nevertheless, unlike shipbuilding contracts, S&P contracts do not normally provide for the payment of liquidated damages in the event of breach.<sup>44</sup>

Should the ship be delivered, but not in the condition specified in the contract, the grounds for complaint are restricted by the fact that, subject to some safeguards, the basic nature of the S&P contract is 'caveat emptor', i.e. buyer beware. However, if the buyer can prove that there is a breach, the buyer will normally be entitled to claim damages for the reasonable cost of repairs and for any detention during the period of the repairs.

### 1.5.3.2 Breaches by the Buyer

The main duties of the buyer are:

- to pay the agreed price at the agreed time; and
- to take delivery of the ship at the agreed location and at the agreed time.

In the same way that the buyer is given the right to cancel the contract if the ship is not delivered by the agreed time, S&P contracts normally entitle the seller to cancel if the buyer does not pay the deposit or the balance of the price in the agreed time. For example, Clause 13 of NSF 1993 provides that:

*"Should the deposit not be paid in accordance with Clause 2, the Sellers have the right to cancel this Agreement, and they shall be entitled to claim compensation for their losses and for all expenses incurred together with interest.*

*Should the Purchase Price not be paid in accordance with Clause 3, the Sellers have the right to cancel the Agreement, in which case the amount deposited together with interest earned shall be released to the Sellers. If the deposit does not cover their loss, the Sellers shall be entitled to claim further compensation for their losses and for any expenses together with interest."*

The clause also mirrors the comments made above in Chapter 1.5.3.1.1 in relation to the right of the buyers to claim damages as well as, or instead of, cancelling the contract.

If the buyer fails to take delivery of the ship at the agreed location and at the agreed time, the seller may incur additional costs and expenses such as port dues, additional fuel costs etc., in keeping the ship pending acceptance by the buyers. The sellers would normally be entitled to recover such costs as damages from the buyers.

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<sup>44</sup> See Chapter 1.4.4 above.

### 1.5.4 Law and Jurisdiction

Law and jurisdiction is just as important in the context of S&P contracts as it is in the context of shipbuilding contracts and the comments made in Chapter 1.4.11 above are equally applicable to S&P contracts.

## 1.6 Insurance

The costs that may be incurred in prosecuting or defending claims under shipbuilding contracts or S&P contracts can be very large. Cover for such costs is normally available under the Defence Rules of the P&I clubs that are members of the International Group provided that the ship has been entered with the club at the time that the relevant building or sale contract is agreed.<sup>45</sup> The cover that is available is discretionary and, consequently, the Defence insurers will normally expect to be kept closely informed of the merits and will wish to monitor developments closely. Cover will be granted and/or maintained only if the insurers consider that a prudent uninsured would have considered it worthwhile to pursue the matter even if insurance cover had not been available.

## 1.7 Case Management

Shipbuilding and S&P cases require a substantial degree of technical and legal expertise and should not be treated lightly. In both cases, technical experts will be required not only to inspect and monitor the physical state of the ship but also to have expert knowledge of the terms and conditions and requirements of classification societies and other regulatory bodies. In the case of shipbuilding contracts it will normally also be necessary for an experienced technical person to monitor the construction process at the builders' yard throughout the period of construction to ensure that any difficulties and disputes are resolved quickly.

Finally, if the seller or buyer wishes to secure the support of his Defence club for the costs that may be incurred in litigating any dispute that may arise under such contracts, the insurers must be notified at an early stage so that they can advise on possible areas of difficulty. It may also be necessary to instruct experienced lawyers who can advise on the documentary and other requirements of the contract and who have knowledge of the formalities that are normally required by flag state authorities, mortgagees, insurers etc., in a number of different countries. Thereafter, the Defence insurers should be kept closely advised of all developments and any failure to do so may result in cover being withheld.<sup>46</sup>

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<sup>45</sup> See *Gard Guidance to the Statutes and Rules*, Guidance to Rule 66 (Cases pertaining to acquisition or disposal of the Ship).

<sup>46</sup> See Chapter 1.6 above.

## 1.8 Case Studies

### Case Study 1

A vessel was sold under an S&P contract which provided that:

*“1. The vessel with everything belonging to her shall be at Seller’s risk and expense until she is delivered to the Buyers, but subject to the conditions of this contract, she shall be delivered and taken over as she is at the time of the inspection fair wear and tear excepted.*

*However the vessel shall be delivered with present class free of recommendations. The Sellers shall notify the Classification Society of any matters coming to their knowledge prior to delivery which ... would lead to the withdrawal of the vessel’s class or to the imposition of a recommendation relating to her Class.*

2. *The Vessel shall be delivered with present Class fully maintained free of recommendations, free of average damages affecting Class. The Machinery Continuous Survey Cycles are to be up to date at the time of delivery. The Class Certificates shall be valid, clean and unextended, the National and International Trading Certificates according to the Vessels present flag are to be clean, valid and unextended. All such Class/Trading Certificates to have validity of at least six months from delivery date.*

*The Sellers shall maintain the vessel to their present standards and deliver her in same basic condition as found and accepted at the time of inspection, fair wear and tear excepted.”*

It was held that the combined effect of those clauses was to entitle the buyers to three cumulative rights as to the vessel’s condition on delivery, namely, that she should be:

- i** in the same condition (fair wear and tear excepted) as she was on inspection; and
- ii** in class free of recommendations; and
- iii** free of average damages affecting class.

The chronology of events was as follows:

- March/April 1986 – the last Class survey of the engine room automation equipment before the contract;
- 9/10 May 1987 – the vessel was inspected by the buyers;
- 14 May 1987 – the S&P contract was signed;
- 18 May 1987 – the engine room automation equipment was surveyed by Class;
- 26 May 1987 – the vessel delivered to the buyers.

The buyers complained after the vessel was delivered to them that she suffered from a number of deficiencies. However, arbitrators held that since the sale was on an 'as she is at the time of inspection' basis, and since the defects were, or should have been, apparent at the time of inspection, the buyers' claims for such alleged deficiencies would not succeed.

However, the buyers also complained that the engine room automation system had suffered recurrent problems over some years and that, whilst the prior owners knew about these problems, they had not brought them to the attention of her classification society. Consequently, the classification society had not discovered the problem during their surveys and had not issued any recommendations. It was held by the English court on appeal that the sellers were obliged under the contract to inform the classification society before delivery of all matters affecting class whenever such matters might have come to their knowledge whether before or after a class survey. Consequently, the buyers succeeded in claiming damage on this basis.

### Case Study 2

A shipbuilding contract gave the buyer a right to cancel a contract for the construction of two vessels in the event that the contractual delivery date, as extended by any permissible delay, was missed. The sea trials date was missed by seven days on one vessel and one day on the other vessel and the buyer exercised its right to cancel both contracts. The contract also provided that if the buyer were to exercise its right to cancel, the builder was obliged to repay all instalments of the contract price that it had received up to that point. Pursuant to the terms of the contracts, the right to repayment of instalments to the buyer was secured by a refund guarantee provided by a bank. The refund guarantee obliged the bank to pay unless the builder commenced proceedings against the buyer challenging the right to cancel.

The builder did so and argued that the short delays had been caused by a number of design changes necessitated by a change in the safety regulatory requirements of the proposed flag state and that, consequently, the delay was one of the 'permissible delays' envisaged by the contract. The builder referred to the following clause in the shipbuilding contract:

*"The vessel ... shall be designed, constructed, launched, equipped, completed and delivered by the Builder in accordance with the provisions of this Contract and the specifications and General Arrangement Plan ..."*

and argued that the builder had not contracted to complete any of the required modifications within the agreed delivery period and was, therefore, entitled to an extension of the delivery time. The court rejected this argument since firstly, the flag state did not in fact require any material amendments and since, secondly, although the basic design was set out in the specification and GA plan, this was nevertheless, a design *and* build contract and that, insofar as the design needed to be developed in order to meet contractual requirements, it was the builder's responsibility to do so. Therefore, it was held that the builder could not claim the benefit of any 'permissible delay' since the delay had in fact been caused by the builder's own fault. Consequently, the bank was obliged to repay the instalments under the refund guarantee.



## Chapter 2

# Bunkers Claims<sup>1</sup>

### 2.1 Introduction

The price of oil products has risen sharply in recent years and this has resulted in a sharp increase in the number of claims that are made in relation to bunkers. The most common issues that arise are the following:

- Damage to the ship's machinery,
- Damage to the environment,
- Responsibility for payment for bunkers,
- The ownership of bunkers,
- Shortage of bunkers,
- Fines for Emission Control Area (ECA) violations.

These issues are relevant whether or not the ship is chartered. In normal circumstances the owner of a ship that is voyage chartered or operating as a liner vessel has the responsibility of providing the ship with the bunkers that are necessary for the operation of the vessel and disputes normally arise directly between the shipowner and the bunker supplier.<sup>2</sup> However, if the ship is time or bareboat chartered, the charterers have the duty to take over and pay for any quantities of bunkers that are already on the ship when she is delivered to them and to purchase any further bunker quantities that may be necessary during the charter period. Subsequently, when the vessel is redelivered to the shipowners at the end of the

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1 For more detailed commentary see the joint BIMCO and International Bunker Industry Association (IBIA) *Bunkering Guide and Bunker Claims Prevention: A Guide to Good Practice* by Bracken, Fisher and Salthouse, 3rd edition 2011.

2 However, if the voyage charter is subject to the BIMCO Bunker Supply and Payment Clause for Voyage Charters (Tank Vessels), charterers have the right to supply such bunkers provided that the price, condition and specification of the bunkers meets the standards set by other suppliers at that time. Charterers are reimbursed by the shipowners for the cost of such bunkers by deduction of an agreed amount from freight.

charter period, the charterers have the right to be reimbursed for the value of any bunkers that remain on board at that time. Consequently, when the ship is time or bareboat chartered, bunker claims may also involve the time or bareboat charterers.

## 2.2 Damage to the Ship's Machinery

Marine diesel engines can be designed to be used with different types of fuel such as MGO (marine gas oil), MDO (marine diesel oil), IFO (intermediate fuel oil) or HFO (heavy fuel oil) and the price of such products is normally quoted in bunker sale contracts according to their maximum viscosity and in accordance with an agreed quality standard. Historically, the lack of quality standardisation meant that many categories of fuels of variable quality were offered for sale at various locations around the world. However, this problem has been minimised in recent years due to the advent of an internationally recognised quality standard. Therefore, bunker oils are now normally sold subject to the parameters specified in the ISO 8217 standard (latest version 2010). Nevertheless, damage may still be caused to a ship's machinery either because unsuitable bunkers are provided or because the bunkers that have been provided are 'off-spec' normally as a result of the presence of some contaminant. Claims arising as a result of such incidents can be very large involving the possible salvage of the ship and cargo if an engine breakdown occurs during the course of a laden voyage, liability to the cargo owners, the repair of the machinery and the loss of income during the repair period. Industry statistics indicate that a large proportion of all machinery breakdowns are caused by either fuel or lubricating oil problems.

## 2.3 Damage to the Environment

Liability for bunker pollution from laden tankers is regulated by the CLC/Fund regime which provides that liability is to be borne only by the shipowner whereas liability for bunker pollution from unladen tankers or from non-tankers is regulated by the Bunker Convention which provides that liability is to be borne not only by the shipowner but also by the "*bareboat charterer, manager and operator of the ship*" all of whom are jointly and severally liable under the convention.<sup>3</sup>

Ships must also comply with Regulations 14 and 18 of Annex VI of MARPOL<sup>4</sup> and the related EU Directive 2005 33/EC and US Environmental Protection Agency regulations which establish various emission control areas (ECAs) and the use in such areas of marine fuel which has a specified maximum sulphur content.<sup>5</sup> Failure to do

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3 Further commentary on bunker pollution issues can be found in Chapters 12.4.1.1.1 and 12.4.1.1.2 (Pollution).

4 For more detailed commentary see Chapter 22.3.2.2.1 (Maritime Regulation and Compliance).

5 Practical guidance relating to the management of the shipowner's duties under these regulations can be found in *Practical Guidelines for handling MARPOL 73/78 Annex VI Regulations 14 and 18* published by Lloyds' Register FOBAS.

so may restrict the vessel's ability to trade within the emission control zones that have been established pursuant to these regulations<sup>6</sup> and may result in substantial fines if breaches of the Regulations are discovered.

On 1 January 2015 the maximum permissible sulphur levels in the fuel of ships sailing in designated ECAs must be reduced from 1.0 per cent to 0.1 per cent by weight. To comply with these regulations shipowners must either:

- burn LNG in the ship's engines; or
- use ultra-low sulphur marine gas oil; or
- use heavy fuel oil provided that the ship has been fitted with an exhaust gas cleaning system or scrubber.

## 2.4 Claims against the Bunker Supplier

In general terms the bunkers that are provided must be fit for purpose in the sense that they can be burned in the ship's machinery in order to provide the normally required degree of propulsion without causing any damage to that machinery. However, it must be appreciated that ships' machinery can be very different and that the ISO standard does not provide a standard for all relevant bunker characteristics and contaminants. Section 4 of the General Requirements of ISO 8217 specifications merely states generally that fuels should not include any added substances or chemicals that *"jeopardises the safety of ships or adversely affects the performance of the machinery; or is harmful to personnel; or contributes overall to additional air pollution."* Therefore, the purchaser has the duty to ensure that the particular grade of fuel that is ordered is fit for use by the vessel. This is particularly important if the ship's machinery has some special feature or characteristic, since any omissions in this regard will probably mean that the bunker suppliers will have no liability for any damage that may be caused by burning the bunkers in the ship's engines.

Furthermore, although the MARPOL Annex VI Regulations 14 and 18 and the related EU and US regulations specify that the bunkers that are burned in the various emission control areas (ECAs) must not exceed a specified maximum sulphur content, it is by no means certain that all bunker suppliers around the world will be able to provide bunkers which satisfy these new tests. Consequently, even greater

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<sup>6</sup> These areas include the North Sea and English Channel, the Baltic Sea, the Mediterranean Sea, the East and West coasts of the USA and Hawaii, Singapore and Australia and are likely to include other areas with the passage of time.

care will need to be taken when ordering bunkers to ensure that the supply order specifies bunkers that meet these enhanced requirements and that they are ordered from suppliers that are able to comply with such requirements.<sup>7</sup>

If the shipowner has a contractual relationship with the supplier then the liability of the supplier will arise in contract subject to the terms of that contract. However, even if there is no contractual relationship between the supplier and the shipowner, the former may, nevertheless, be liable to the shipowners in tort for any damage that the bunkers may cause to the ship's machinery as a result of the supplier's negligence. If the bunkers have been ordered either by the shipowners themselves or by a bunkering broker on their behalf, liability will lie in contract. However, if the bunkers have been ordered by the time charterers or by a bunkering broker on their behalf, the liability of the suppliers to the time charterers will lie in contract subject to the terms of that contract, but the supplier may also have liability in tort to the shipowner since there would be no contractual relationship in such circumstances between them and the shipowner.

### **2.4.1 Claims in Contract**

Bunkers are supplied in many countries around the world but there are no international conventions which regulate the terms of bunker supply contracts. Therefore, a purchaser will often have little choice but to accept supply from a local supplier pursuant to that supplier's terms of business. Claims against the supplier are therefore, often complicated by the following difficulties:

- The relevant jurisdiction and law;
- The status of the supplier as principal or agent; and
- The supplier's terms of business.

#### **2.4.1.1 The relevant Jurisdiction and Law**

The terms of business of many bunker suppliers provide that claims and disputes are to be resolved by the courts of the country where the suppliers normally carry on business and in accordance with the law of that country. The terms of business of other suppliers may provide for more neutral dispute resolution measures (such as London arbitration in accordance with English law), but may also go on to emphasise that such law and jurisdiction is non-exclusive in the sense that the bunker supplier has the right to opt for some other jurisdiction of its choice either to

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<sup>7</sup> To assist the industry BIMCO have produced the BIMCO Standard Bunker Contract which provides a comprehensive set of terms and conditions for the sale of marine fuels and provides for bunker sampling and bunker delivery notes that are in accord with the new MARPOL Annex VI regulations. However, it is not obligatory to use this contract or any of its terms and conditions.

defend claims or to pursue claims. In many instances, the law of the country where the supplier carries on business may provide the supplier with substantial protection against claims.

#### **2.4.1.2 The Status of the Supplier as Principal or Agent**

In many instances, the bunkers that are supplied to the ship may be provided through a string of bunker traders and the final bunker supply contract may be concluded with an organisation which has either bought the bunkers from another supplier or trader or which may be acting as an agent for another supplier. The distinction is crucial in the event of a claim since if the final supplier is in fact acting as agent, the claim will generally lie not against that supplier but against whoever is the principal of that supplier.

#### **2.4.1.3 The Supplier's Terms of Business**

Practically all bunker suppliers have terms which contain very restrictive contractual liabilities which exclude the applicability of any implied terms which might otherwise be applicable and either exclude liability totally or limit liability to the value of the bunkers supplied or specify that unless a claim is brought within a very short time limit, liability is excluded. One such example is the following:

*"Notice of any claim of whatsoever nature arising, made by the buyer against the seller shall be given in writing fully documented with all supporting documents to the seller at their address and be received by them within 7 days from the date on which the delivery was completed ... Unless the buyer gives notice of any claim pursuant to this clause, within the time limit, all claims by the buyer of whatsoever nature shall be automatically extinguished and absolutely time barred and waived against the seller ..."*

In most cases, it will be very difficult for the purchaser to comply with such time limits since the ship may not even start to use the bunkers until much later and it may not be possible in any event to obtain test results within such a short period. Furthermore, many bunker supply contracts provide that samples will be analysed locally at the port of supply and that the results of such an analysis will be conclusive and binding between the parties.

The supplier's terms of business will also frequently provide that the quantity of bunkers is to be measured either in the shore tank or in the supply barge and that such measurement is to be conclusive and binding on both parties.

### 2.4.2 Claims in Tort<sup>8</sup>

The law of most countries places a duty of care on suppliers of goods to ensure that the products that they supply do not cause damage or loss whether those products are supplied under contract or not. Therefore, if the ship's machinery has been damaged by the bunkers that have been supplied, the supplier may have a liability to the shipowner in tort. However, the claimant must be able to prove that the damage arose as a result of the negligence of the supplier and in this respect, the supplier is expected to have only that degree of knowledge that a reasonably prudent and experienced supplier would normally have as to the suitability of the bunkers for use in the particular ship's machinery. Therefore, if the ship's machinery has some special feature or characteristic which is not communicated to the suppliers, the suppliers may not be liable for any damage that has been caused by the supply of unsuitable bunkers since they could not be expected to be aware of the need for additional care and attention in such circumstances.

In most cases, claims in tort can normally be pursued against the supplier only in the country where the supplier carries on business and therefore, the merits of the claim depends on the readiness of the local courts and legal system to provide a remedy in such circumstances. In some instances, the law of another country may allow a claim to be brought in the courts of that country provided that the damage was suffered in that country (as, for example, is the case between the countries of the European Union). However, that alternative option is not often of much practical advantage in the case of damage caused by the use of bunkers since the damage may be progressive as the ship moves from country to country.

Finally, it is still the law in the United Kingdom and some other common law countries that a claim can be brought in tort only when physical damage has been caused. Therefore, a shipowner might not be able to claim damages against the supplier in tort for any delay to the ship that may be necessitated by the need to carry out investigations as to the suitability of bunkers before they are used in the ship's machinery, since no physical damage would yet have been caused in such circumstances. Similarly, there may be no liability in tort if there is no physical damage to the ship but her trading ability has been restricted due to the fact that the bunkers do not meet the enhanced requirements of the MARPOL Annex VI Regulations 14 and 18.

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<sup>8</sup> More detailed commentary on tortious liability can be found in Chapter 14 of the *Gard Handbook on P&I Insurance*. See also *Clerk & Lindsell on Torts*, 20th edition 2010, Sweet & Maxwell.

## 2.5 Claims against Time or Bareboat Charterers<sup>9</sup>

Most time or bareboat charters oblige the charterers to provide and pay for bunkers during the charter period as and when the ship has need for such bunkers.<sup>10</sup>

### 2.5.1 Quality Claims

Because of the importance of ensuring that the ship is provided with the correct grade and quality of bunkers many time and bareboat charters will now include detailed provisions such as the following:

*“Charterers guarantee that the bunkers that they will supply to the vessel will be of minimum standard RME25 for IFO 180 cst.”*

Furthermore, in view of the enhanced requirements of Regulations 14 and 18 of Annex VI of MARPOL and other regulations relating to fuel sulphur content emission limits, BIMCO has issued a Revised Bunker Fuel Sulphur Content Clause 2005 for use in time charters which is intended to provide a clearly worded and balanced provision to help owners and charterers comply with these requirements. The clause obliges charterers to provide the vessel with fuels of the necessary sulphur content to allow the vessel to trade within the emission control zones ordered by the charterers and to use bunker suppliers that operate in accordance with the regulations.

If the charterparty includes such provisions, the charterers will be liable if the bunkers that are provided do not meet the contractual description and damage is caused to the ship's machinery or the trading area that is available to the ship is restricted. It also follows that the charterers cannot place the vessel off-hire if the supply of such bunkers results in delay to the ship.<sup>11</sup>

Even if the charter does not contain such an express provision the time or bareboat charterers are under an absolute obligation to ensure that the bunkers that they supply must be of reasonable quality and suitable for the type of machinery that is fitted to the particular ship. However, if the ship's machinery has some special feature or characteristic which is not communicated to the time or bareboat charterers then the latter will not normally be liable for any damage that may be caused to the ship's machinery by the supply of bunkers which are not fit for use in that particular machinery.

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<sup>9</sup> Such claims may also be made against voyage charterers if the voyage charter includes the BIMCO Bunker Supply and Payment Clause for Voyage Charters (Tank Vessels) referred to in footnote 2.

<sup>10</sup> See Chapter 2.6 below.

<sup>11</sup> Further commentary on off hire issues can be found Chapter 4.5.1.1.2 (Charterparty Claims).

Because of the protective clauses which are normally incorporated in the standard trading conditions of most bunker suppliers, shipowners will normally find it easier to bring claims against the time or bareboat charterer under the terms of the charter than against the supplier under the bunker supply contract. Consequently, should the charterer be found liable to the shipowner for such a claim the charterer may have a difficult task in seeking redress from the supplier since it is very unlikely that the terms of the charter and the bunker supply contract will contain back-to-back terms.

### 2.5.2 Quantity Claims

Time and bareboat charters normally include clauses such as the following which provide that the charterers will redeliver the vessel with the same quantity as had originally been on board on delivery to the charterers:

*“The Charterers on delivery, and the Owners on redelivery, shall take over and pay for all bunkers remaining on board the vessel. On delivery quantity of bunkers on board shall be abt 300/100 RME180/DMB respectively. The vessel to be redelivered with about the same quantities of bunkers, however its quantity shall be sufficient to reach major bunkering port ...”*

Consequently, the charter will frequently provide that there should be a bunker survey on delivery and redelivery and if it is found that the vessel has been redelivered with less than the correct quantity of bunkers, the charterers are obliged to compensate the shipowners for the deficiency either at the agreed bunker price (if this is expressly stated in the charter) or at the market price at (or at the nearest bunkering port to) the redelivery port.

Where there is a clause in the charter which provides that an agreed quantity of bunkers are to be delivered and redelivered at agreed prices, charterers may be tempted in the event that the agreed price proves to be substantially higher than the actual market price on redelivery, to redeliver the vessel with a substantially greater quantity of bunkers than was on board on delivery in order to profit from the difference in price. However, the shipowners are not bound to accept delivery of such a greater amount and are not bound to pay the agreed higher price for the excess amount.



### 2.5.3 Safe Bunkering Locations<sup>12</sup>

Time charterers will normally provide that the time charterers must employ the ship 'between safe ports'. This duty includes the duty to ensure that any bunkering location to which the ship is sent to bunker (whether at a berth or alongside a bunker barge) will be safe for the ship. Therefore, the principles that apply to the use of safe ports generally also apply to the safety of bunkering locations.

### 2.6 Claims against the Shipowners<sup>13</sup>

Under a bill of lading or voyage charter, the responsibility of providing bunkers falls on the shipowner. Under a time charter, the responsibility falls on the time charterer. However, since the day to day operation of a time-chartered vessel lies with the shipowner through the medium of the crew, the shipowner has the duty to keep the time charterer informed as to when the vessel will need a bunker supply and as to the quantity of bunkers that will be required. In either case, should the shipowner fail to honour its obligations, the shipowner may be in breach of its obligation to maintain the ship in a seaworthy condition and the cargo owner or charterer may be able to claim damages for any losses that it has suffered, e.g. liability for delayed delivery of the cargo. The time charterer may also be able to place the vessel off-hire if time is lost as a result of the lack of bunkers.

Furthermore, bunkers are expensive. Therefore, when bunkers that are owned by someone other than the shipowners, e.g. time charterers or unpaid suppliers, are lost or damaged after they have been delivered to the ship, claims can be made against the shipowners either in contract or in tort.

Claims brought by charterers are likely to be brought in contract under the terms of the charter. The shipowners' liability for such claims is unlikely to be governed by the Hague, Hague-Visby or Hamburg Rules even if such rules are incorporated into the charter by agreement since such rules regulate the carriage of cargo and bunkers do not constitute cargo. Nevertheless, the shipowners have the duty to properly care for bunkers under the common law and will be liable if they are negligent in that regard unless they are protected by an exception clause in the charter.

The terms of most bunker suppliers provide that risk passes from the supplier to the ship when the bunkers are received on board. Therefore, if the bunkers are lost or damaged thereafter, the suppliers are more likely to demand payment for the contractual price of the bunkers rather than claim damages for loss or damage to the bunkers. However, if full payment has not been made on delivery, the suppliers

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<sup>12</sup> For further commentary on safe ports see Chapter 13 (Safe Ports Claims).

<sup>13</sup> For more detailed commentary on charterparty claims see Chapter 4 (Charterparty Claims).

may also have an alternative remedy since they will probably still retain title to the bunkers,<sup>14</sup> in which case, the shipowners will have the duty as bailees of the bunkers to care for them and will be liable in tort if they fail to do so.

## **2.7 Responsibility for Payment for Bunkers**

The supplier of bunkers faces difficulty if bunkers are supplied on credit terms or on any terms other than payment against supply since, once the bunkers are delivered on board a ship, they are no longer within the physical control of the supplier and may, furthermore, be consumed by the ship. The issue may be further complicated in the case of a time or bareboat chartered ship since the bunkers may have been ordered by the charterer but delivered to the ship (which is owned by a third party, i.e. the shipowners). In such circumstances the supplier may wish to rely on the following remedies:

- A lien on the ship;
- Attachment of the bunkers,
- A retention of title (Romalpa) clause.

### **2.7.1 A Lien on the Ship**

#### **2.7.1.1 A Maritime Lien<sup>15</sup>**

The law of some (but not all) countries provides an unpaid bunker supplier with a maritime lien on the ship to which the bunkers have been supplied. A maritime lien is a right to bring *in rem* proceedings against a vessel which attaches automatically when the bunkers are supplied and which remains in force despite any subsequent sale or transfer of that property. Therefore, if the bunker supplier is not paid he may arrest the ship to demand payment if the bunkers were supplied to the ship even though the bunkers were ordered by the time or bareboat charterers for their own account. This can leave the shipowner having no option but to satisfy the claim of the bunker supplier and then seek recovery from the charterers. In circumstances where the charterer has not paid for the bunkers, they may well be unwilling or unable to satisfy the shipowner's claim.

The question of whether an unpaid bunker supplier has the right to exercise a maritime lien on the vessel in order to enforce payment varies from country to country and a bunker supplier must take care to ensure that a ship is arrested in a country where the right to such a maritime lien is recognised and enforced. The right to a maritime lien is recognised under the law of countries such as Argentina, Belgium and Brazil which have ratified the 1926 Convention on Maritime Liens and Mortgages and by some (but not all) countries that have ratified the 1952 Arrest Convention. The law of the United States and Canada also provides for a maritime lien

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<sup>14</sup> See Chapter 2.7.3.

<sup>15</sup> Further commentary on maritime liens can be found in Chapter 24.4 (Security Enforcement Measures).

if the bunkers were supplied in the USA or Canada or under a contract which is subject to US or Canadian law. However, there is no such right under the law of England and Wales. For this reason, the terms and conditions of many suppliers are either subject to US law or entitle the supplier to opt for US law in the event that they bring a claim for payment. In such circumstances, ships may be vulnerable to arrest either in those countries or in other countries such as Panama which recognises and enforces maritime liens on such a basis irrespective of whether a maritime lien would be available under the local law.

### 2.7.1.2 A Statutory Lien<sup>16</sup>

Many countries do not recognise and enforce a maritime lien either pursuant to the law that governs the contract or their own local law. Nevertheless, the unpaid bunker supplier may be entitled to arrest a ship to enforce payment in such countries pursuant to the *in rem* jurisdiction of the particular country. For example, such rights are available in the United Kingdom pursuant to Section 20 of the Supreme Court Act 1981 which gives the right to arrest a ship in the United Kingdom in respect of:

*“(m) any claim in respect of goods or materials supplied to a ship for her operation or maintenance.”*

However, such rights are normally subject to the following deficiencies:

- There is a right to arrest the ship (or a sister ship) only if the bunkers were ordered by the shipowner or the bareboat charterers. Therefore, there is no right to arrest the ship (or a sister ship) if the bunkers were ordered for the account of the time charterer;
- The statutory lien does not survive a change of ownership of the vessel unless proceedings were commenced before the change of ownership.

### 2.7.1.3 The Charterers' Obligation not to Allow a Lien to be Enforced against the Ship

The provisions of some charters expressly prohibit the charterers from allowing a lien to be enforced against the ship. For example Clause 18 of the NYPE 1946 charter provides that:

*“Charterers will not suffer, nor permit to be continued, any lien or encumbrance incurred by them or their agents, which might have priority over the title and interest of the owners in the vessel.”*

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<sup>16</sup> Further commentary on statutory liens can be found in Chapter 24.5 (Security Enforcement Measures).

Clause 23 of the NYPE 93 is even more specific in that it provides that:

*“The Charterers undertake that during the period of this Charter Party, they will not procure any supplies or necessaries or service including any port expenses and bunkers on the credit of the Owners or in the Owners’ time.”*

Therefore, if the charterers order bunkers on terms which by contract or law provide the bunker suppliers with the right to exercise a lien on the ship, the charterers are obliged to take active steps to release the lien and are liable to the shipowners in damages for any losses that the shipowners may suffer as a result of their failure so to do. In particular, if the ship is arrested by suppliers of bunkers ordered by the charterers or their agents, the charterers are obliged to put up security to release the ship. In practice, however, charterers who fail to pay for bunkers ordered by them may not be in a position to meet their obligations to owners.

### **2.7.2 Attachment of the Bunkers<sup>17</sup>**

The various international conventions that regulate arrest are restricted to the arrest of ships and there are no international conventions that regulate the arrest of bunkers. However, it may be possible under the local law of some countries to arrest or otherwise detain bunkers, e.g. by freezing order in the United Kingdom. However, since such an order is essentially an equitable remedy, courts are normally hesitant to do so since such procedures can often prejudice the rights of third parties. For example, if time charterers do not pay for bunkers that have been delivered to a ship pursuant to their order, the arrest or detention of the bunkers is likely to affect the operational freedom and other rights of the shipowner and any other sub-charterer or cargo owner. Therefore, even if the court was minded to grant an attachment order, it might do so subject to the condition that the bunker supplier must pay for the discharge of the bunkers and for their storage ashore or in a barge pending the resolution of the dispute.

### **2.7.3 Retention of Title (Romalpa) Clauses**

Most supply contracts will contain clauses which are intended to protect the supplier’s rights should the purchaser become bankrupt prior to paying for the bunkers. Such clauses provide that the supplier will retain ownership of the bunkers until payment has been made even after the bunkers have been delivered on board a vessel owned by a third party. Consequently, the bunkers do not form part of the bankrupt’s estate in bankruptcy and can be recovered by the supplier if payment is not made. The following clause is a representative clause:

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<sup>17</sup> Further commentary on arrest orders and freezing orders can be found in Chapters 24.6.1 and 24.6.2 (Security Enforcement Measures).

*“Risk in the Marine Fuels shall pass to the Buyers once the Marine Fuels have passed the Sellers’ flange connecting the Vessel’s bunker manifold with the delivery facilities provided by the Sellers. Title to the Marine Fuels shall pass to the Buyers upon payment for the value of the Marine Fuels delivered, pursuant to the terms of Clause 8 hereof. Until such time as payment is made, on behalf of themselves and the Vessel, the Buyers agree that they are in possession of the Marine Fuels solely as Bailee for the Sellers. If, prior to payment, the Sellers’ Marine Fuels are commingled with other marine fuels on board the Vessel, title to the Marine Fuels shall remain with the Sellers corresponding to the quantity of the Marine Fuels delivered. The above is without prejudice to such other rights as the Sellers may have under the laws of the governing jurisdiction against the Buyers or the Vessel in the event of non-payment.”*

Such clauses are normally enforceable, but complications can arise when the bunkers have been mixed with bunkers ordered from other suppliers or have been partly consumed prior to a demand being made for their return. Where bunkers have been commingled on the ship with bunkers provided by other suppliers the usual rule is that the supplier and the ship (or other supplier if they are also unpaid) own the commingled bunkers jointly in the proportions that each separately supplied quantity bears to the total commingled quantity.

In one case<sup>18</sup> the English court was asked to rule on a claim made by bunker suppliers following the bankruptcy of the time charterers that the shipowners were obliged to pay the suppliers for the value of bunkers that had been consumed on board both before and after the charter was terminated. The court held that the shipowners were not obliged to do so since firstly, they had obtained the bunkers in good faith from the time charterers without notice of the bunker suppliers’ lien or retention of title clause. However, this is an unusual case and it must be presumed that in the majority of cases a shipowner will be presumed to know that there is likely to be a retention of title clause in most bunker supply contracts that may be concluded by a time charterer.

The suppliers also argued that since the shipowners were bailees<sup>19</sup> of the goods they had a duty to safeguard and look after the goods for the benefit of the goods owners (i.e. the suppliers) and that the shipowners were, therefore, in breach of their obligations since they had consumed the bunkers. However, the shipowners argued that they had not purchased the bunkers themselves and were in fact merely sub-bailees of the bunkers from the time charterers, and that the suppliers should have been aware of the fact that the shipowners would have agreed to become

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<sup>18</sup> *The Fesco Angara*, [2011] 1 Lloyd’s Rep. 61.

<sup>19</sup> Further commentary on issues relating to bailment can be found in Chapter 3.3 (Cargo Claims).

such sub-bailees (i.e. to accept delivery of the bunkers on board) only on the basis that the time charterers would assume responsibility for paying for the bunkers. Therefore, by agreeing to deliver the bunkers to the ship with such knowledge, the suppliers must have accepted that the sub-bailment to the shipowners would be on terms that payment would be made by the time charterers. As a result, the suppliers could not thereafter look to the shipowners for payment. Therefore, suppliers may be prevented (the legal term is 'estopped') in many cases from relying on their rights under lien clauses and retention of title clauses. However, it must be appreciated that this case was decided on common law principles and that such a result would not necessarily follow under other systems of law. Furthermore, when bunkers are ordered by intermediary parties such as brokers or managers the suppliers may not in fact know whether the bunkers are being ordered by the shipowners or the charterers as principals.

## **2.8 Ownership of the Bunkers**

Comment has already been made above on the fact that although the bunkers may be physically located on board a particular ship, the bunkers may nevertheless be owned by an unpaid supplier (pursuant to a retention of title (Romalpa) clause) or by the time or bareboat charterers. Ownership is important in the following circumstances:

- Bankruptcy;
- Title to sue for loss of, or damage to, bunkers; and
- Liability for contribution to salvage or general average.

In the event of bankruptcy the trustees in bankruptcy have the duty to identify and take over all assets of the bankrupt company in order to maximise the amount of assets that are available to satisfy creditors and shareholders. Therefore, if the bunkers are owned by time charterers who owe hire and other sums to the shipowners, the trustees in bankruptcy of the time charterers are entitled to take possession of the bunkers leaving the shipowners to pursue their claim in the bankruptcy proceedings in competition with all other non-secured creditors.

In the event of salvage<sup>20</sup> or general average,<sup>21</sup> the party that has incurred loss or expenditure is entitled to receive contribution from the owners of all property that was at risk (including the owners of the bunkers.)

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<sup>20</sup> Further commentary on issues relating to salvage can be found in Chapter 14 (Salvage Claims).

<sup>21</sup> Further commentary on issues relating to general average can be found in Chapter 10 (General Average).

## 2.9 Insurance

### 2.9.1 Hull and Machinery<sup>22</sup>

Damage to the ship caused by the supply of deficient bunkers may be caused directly, i.e. damage to the ship's engine, or indirectly, i.e. engine malfunctioning leads to loss of power causing the ship to run aground and damage the hull. Such damage is normally covered by hull and machinery insurers subject to the agreed policy deductible. However, insurers will normally require the assured to have acted as a prudent uninsured and to have taken all avoidance and protective measures that could reasonably be expected such as, for example, taking representative fuel samples for analysis by shore laboratory and ensuring that the fuel is properly stored and treated on board. Furthermore, hull and machinery insurers will not cover claims for pure delay.

### 2.9.2 P&I<sup>23</sup>

The shipowner's liability for loss of or damage to bunkers owned by third parties is covered by the ship's P&I club under the general provision for cover of liability for loss of or damage to property owned by third parties<sup>24</sup> whereas the liability of charterers for damage to the ship's machinery and/or to the ship's hull caused by deficient bunkers owned and/or supplied by or on behalf of the charterers is covered by the charterers' P&I liability insurers.

The shipowner's liability for pollution caused by the discharge or escape of bunkers is normally covered by the shipowner's P&I club.<sup>25</sup>

### 2.9.3 Defence Cover<sup>26</sup>

Since shipowners are not normally entitled to recover costs incurred by them in relation to delay, detention or deviation from either hull and machinery or P&I insurers, the owners will normally have to claim such costs directly from the supplier or the time charterers. However, legal costs incurred by them in order to do so may be recoverable under the Defence cover subject to the discretion of the Defence club management.

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<sup>22</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>23</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 38 (Pollution)).

<sup>24</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 39 (Loss of or damage to property)).

<sup>25</sup> For more detailed commentary see Chapter 12.7.1 (Pollution Claims).

<sup>26</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV Rule 65 (Defence Cover)).

### 2.9.4 Charterers' Liability Insurance<sup>27</sup>

Time charterers' liability for damage that may be caused to machinery by the supply of bunkers may also be covered by charterers' liability insurers depending on the extent of cover that has been taken.<sup>28</sup> Charterers' liability insurers will also normally cover the assured's liability for any delay that may have been caused to the ship as a result of the bunker supply. However, if the charter provides that the ship should remain on hire during this period, the charterer's liability insurance does not provide cover and the shipowner's remedy is to claim the hire from the charterers and to claim the legal and other costs in doing so under the Defence Cover.

The liability of the charterers for pollution caused by the discharge or escape of bunkers pursuant to the Bunker Convention<sup>29</sup> is normally covered by the charterers' P&I liability insurers. However, if charterers incur liability for bunker pollution under laws other than the Bunker Convention in their capacity as owner of the polluting substance (rather than in their capacity as charterer) they may not be covered under a standard P&I policy but may be covered if they have taken out extended cover.

## 2.10 Claims Management

Claims management concerns can encompass a number of different issues falling under the following headings:

- Contract terms;
- Operational safeguards; and
- Evidence.

### 2.10.1 Contract Terms

It will be clear from the commentary above that the terms and conditions that can normally be found in contracts with bunker suppliers are very onerous insofar as the purchaser is concerned. Therefore, reference should be made to the BIMCO Standard Bunker Contract which is a far more balanced contract and which purchasers should consider using whenever possible.

It is also important that clauses are included in bunker supply contracts and charterparties to ensure that any bunkers that may be supplied will comply with the low sulphur requirements of MARPOL. In particular, parties are referred to the BIMCO Bunker Fuel Sulphur Content Clause for Time Charter Parties 2005 which is intended to provide a balanced framework for the relationship of shipowners and time charterers in this regard.

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<sup>27</sup> For more detailed commentary see Chapter 26.3.2 (The Structure of Marine Insurance).

<sup>28</sup> For example, Gard's Comprehensive Charterers P&I Cover includes charterers' liability for physical damage to the ship and for the cost of de-bunkering if this is necessary in order to avoid damage to the ship. See <http://www.gard.no/ikbViewer/Content/67630/SCC%20Brochure.pdf>.

<sup>29</sup> See Chapter 12.4.1.1.2 (Pollution Claims).



In many cases the readiness of insurers to assist may be affected by whether or not the assured has taken reasonable steps to ensure protection by the use of such clauses.

### 2.10.2 Operational Safeguards

Much helpful guidance can be found in the Gard booklet *Bunkers and bunkering – a compilation of Gard bunker related articles* and the various Circulars that are periodically produced by the International Group of P&I Clubs. Reference should also be made to the *Gard Guidance to Masters* at paragraphs 2.13.1 and 2.13.2 and to the joint BIMCO and International Bunker Industry Association (IBIA) *Bunkering Guide* and *Bunker Claims Prevention: A Guide to Good Practice* by Bracken, Fisher and Salthouse, 3rd edition 2011.

### 2.11 Case Study

Gard's assured, a time charterer, orders bunkers to be supplied to the vessel as required under the charterparty. The analysis shows inorganic acid in the bunkers. The testing results are available only after the vessel has left the bunkering port and, due to a seven day notice provision in the bunkering contract, the bunker supplier has refused to arrange for debunkering and replacement. Gard appoints an expert to assist who confirms that inorganic acid can damage the vessel engines and is in violation of the specification in the charter bunker clause. In order to avoid liability under the charterparty for damage to the engine, Gard will cover the Member's extraordinary costs of removal and replacement of the fuel as well as the expert costs. Extraordinary costs are those costs reasonably incurred by the Member to remove off-spec bunkers and replace them with sound bunkers including cleaning of affected areas and lawful disposal costs of tainted bunkers and any cleaning materials. The economic value of the bunkers removed and the economic value of the replacement fuel are not covered. In the event that the discovery of the off-spec bunkers occurs after there has been engine damage, Gard will also cover the charterer's liability for damage to the vessel and the liability for loss of hire (if any) incurred during the repair period. In either event, Gard will be subrogated to the claim against the bunker supplier and will assist the Member in evaluating and, if deemed appropriate, pursuing a claim against the bunker supplier.

Reference is also made to Gard News, Issue No. 174 (2004) and to the article entitled *Off-spec bunkers – Some practical cases*.



## Chapter 3

# Cargo Claims<sup>1</sup>

### 3.1 Introduction

It is inevitable that ships will face cargo claims at some point in time. The most common types of claim relate to the following:

- Damage to the cargo;
- The loss of part or all of the cargo;
- The delivery of the cargo to the wrong recipient;
- Delay to the cargo;
- The extra costs of discharging and/or storing damaged cargo;
- The costs of the disposal, on-shipment or transshipment of cargo;
- Cargo's proportion of salvage or general average.

Cargo claims may also be brought even when the cargo is not in fact lost or damaged or delayed. This usually occurs when the documents evidencing the shipment of the cargo misdescribe some aspect of the cargo (e.g. the quantity, weight or apparent order and condition of the cargo) and the cargo that is received differs from that description even though there has in fact been no event during the carriage to which damage or loss can be attributed. In such circumstances, the misdescription may be held to be a misrepresentation by the carrier and the claim relates to the financial loss suffered by the receiver of the cargo as a result (e.g. where the receiver as buyer has relied on the accuracy of the cargo description made by the carrier and has paid the seller for more cargo than that which has actually been shipped). This is a notoriously common problem in the case of bulk cargoes since some degree of measurement difference is often inevitable and many claims are made based on the allegation that the discrepancy is greater than that which is considered normal and customary in the trade.

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1 This section should be read in conjunction with the commentary that can be found in Chapters 18-21 of the *Gard Handbook on P&I Insurance*, 5th edition 2002 and in Part II Chapter 1 *the Gard Guidance to the Statutes and Rules* (Guidance to Rule 34 (Cargo Liability)).

Finally, claims are sometimes brought wrongly when the quantity of cargo which is delivered by the ship is less than the quantity shipped, but the apparent 'loss' is not due to any fault or negligence on the part of the carrier but due to the inherent nature of the cargo. Some cargo loss inevitably occurs during the carriage of certain cargoes, for example evaporation loss from some oil cargoes. In such circumstances, the carrier is not liable but has a defence under the common law or the Hague, Hague-Visby or Hamburg Rules, whichever is applicable to the particular carriage. Furthermore, such claims are not normally covered under the standard cargo insurance policies since the losses are inevitable and not caused by a fortuitous peril.

Claims are normally made only against the ship which has carried the relevant cargo but can also be made against another ship if the loss or damage can be attributed to the negligence of that other ship (for example, in the event of a collision, when the cargo on ship A has been damaged by the negligence of ship B.) In the event that claims are made against the carrying ship the claim is normally brought under a contract for the carriage of the cargo. However, if the shipowner is not the carrier under that contract of carriage (for example, where the contractual carrier is the charterer or some other non vessel owning carrier (NVOCC)) the claim can be brought in contract against whoever is the carrier under the contract of carriage and/or against the shipowner in tort (i.e. negligence). However, in the event that claims are brought against the non-carrying ship, those claims can only be brought in tort since there will be no contract of carriage between the non-carrying ship and the damaged cargo.

It is normally very important to establish whether the claim is brought under a contract or in tort since a claim brought in contract may be subject to certain contractual and/or statutory defences that apply to the contract (e.g. exclusion clauses, time bars or package limits of liability). If the claim is brought in tort, the carrier may not have the benefit of any contractual defences unless the carrier is able to rely on the protection that is given by special clauses such as the Himalaya Clause or the Circular Indemnity Clause or the doctrine of bailment on terms (See Chapter 3.3.1 below).

## 3.2 Contractual Liability

Cargo claims can arise under many forms of contract that are regularly used in the shipping industry. However, contractual liability can arise either directly between a carrier and a cargo claimant (for example, as between a carrier and a cargo receiver under a bill of lading) or by way of indemnity as between a carrier who has settled such a claim and another party under another contract (for example, as between the carrier and the other party to whatever charterparty contract<sup>2</sup> there may be between them.) The commentary below considers this issue in relation to the most common forms of contract that are used in the shipping industry.

### 3.2.1 Time Charters<sup>3</sup>

It is extremely unlikely that cargo claims will be made by time charterers against shipowners since time charterers are not usually the owners of the cargo. Nevertheless, the issue may arise under a time charter on an indemnity basis. Cargo claims will normally be made initially by third party cargo owners under contracts of carriage such as bills of lading against whoever is the carrier under that contract. Depending on whether the carrier is the shipowner or the time charterer either party may then wish to claim an indemnity *inter se* under the terms of the time charter.<sup>4</sup>

### 3.2.2 Voyage Charters<sup>5</sup>

In the case of a voyage charter, it is possible that the receiver of the cargo may be the voyage charterer (e.g. where the cargo is bought on FOB (free on board) terms) in which case the duty of chartering the vessel to carry the goods lies on the buyer and the governing contract of carriage between the shipowners and the receivers would be the voyage charter not the bill of lading. Consequently, the cargo claim would be brought under the terms of the voyage charter not the bills of lading, which would be mere receipts for the goods, and would be determined in accordance with the terms of the voyage charter. Therefore, no question of indemnity can subsequently arise as between the shipowners and the voyage charterers.

However, where the receiver of the cargo is not the voyage charterer (e.g. where the cargo is bought on CIF (Cost, Insurance, Freight) terms) the duty of chartering the vessel to carry the goods lies on the seller and the governing contract of carriage between the shipowners and the receivers would be the bill of lading not

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2 A more detailed commentary on the rights and obligation of parties under charterparties can be found in Chapter 4 (Charterparty Claims).

3 For a more detailed commentary see Chapter 18.2.4 of the *Gard Handbook on P&I Insurance and Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

4 This issue is considered further in Chapter 3.4 below.

5 For a more detailed commentary see Chapter 18.2.3 of the *Gard Handbook on P&I Insurance and Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2005, Chapters 11, 18, 72 and 85.

the voyage charter. Therefore, the likelihood is that the cargo claim will be made in the first instance under the bills of lading and the question of indemnity will arise thereafter between the shipowners and the voyage charterers. However, it is extremely unlikely that the voyage charterers would be a carrier under the bill of lading and accordingly, any subsequent indemnity claim would normally be made by the shipowners against the voyage charterers and not vice-versa.<sup>6</sup>

### 3.2.3 Booking Notes<sup>7</sup>

A booking note can take many forms. However, it is usually a contract which records the agreement of parties to reserve space on a vessel for the future carriage of a cargo which does not need the whole or most of the carriage capacity of the vessel. It will usually set out the terms of the agreement and will usually provide that the carriage will be subject to the terms of the carrier's standard bill of lading terms. Finally, it will also usually provide that the booking note will be superseded (i.e. replaced) by the terms of an agreed form of bill of lading once the cargo has in fact been shipped in due course. Therefore, cargo claims are likely to be pursued under the bill of lading form that has superseded the booking note. However, if the parties to the booking note and bill of lading are different complications can arise and claims could be made under both contracts.

### 3.2.4 Bills of Lading<sup>8</sup>

The majority of cargo claims are pursued under bills of lading although some are made under sea waybills.<sup>9</sup>

There are two different types of bills of lading:

- Bills of lading which are normally described as 'negotiable' or 'to order' (These terms mean the same but the term 'to order' bill will be used for the sake of convenience in this commentary); and
- Straight bills of lading.<sup>10</sup>

The fundamental difference between the two types of bills of lading is that the 'to order' bill qualifies the identity of the receiver of the cargo by adding the words 'to order', e.g. 'to order of the shipper' or 'to order of X' or 'to X, to their order' or

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<sup>6</sup> This issue is also considered further in Chapter 3.4 below.

<sup>7</sup> For a more detailed commentary see *Bills of Lading* by Aikens, Lord and Bools, 2006 Informa, paras 2.35 and 7.7 to 7.16.

<sup>8</sup> For a more detailed commentary see Chapter 18.3 of the *Gard Handbook on P&I Insurance and Bills of Lading* by Aikens Lord and Bools, 2006, Informa.

<sup>9</sup> See Chapter 3.2.7 below.

<sup>10</sup> See Chapter 3.2.5 below.

simply 'to order' whereas a straight bill of lading identifies the receiver without using the words 'to order', e.g. 'to X'. The absence of the words 'to order' imposes an important restriction on the transferable nature of the bill of lading.<sup>11</sup>

A 'to order' bill of lading is a far more complex document than a charterparty. It is:

- a receipt for the goods;<sup>12</sup> and
- good evidence of a transferable contract of carriage;<sup>13</sup> and
- a negotiable document of title in the sense that the transfer of it enables the holder of it to obtain delivery of the cargo from the ship.<sup>14</sup>

It is this combination of features which has made the 'to order' bill of lading the fulcrum of international trade. Most international contracts for the sale of goods provide that as the goods are sold from seller to buyer the bill of lading (as a transferable contract of carriage) is also transferred from seller to buyer thereby creating a contract between the carrier and each successive lawful holder of the bill as the bill is passed from holder to holder. The right to sue the carrier is transferred from holder to holder in the sense that the transferor loses and the transferee gains that right with the transfer of the bill. It also means that the holder has the right to sue the carrier under the bill for loss or damage that has occurred at any time during the transit and not only for loss or damage that has occurred after he has become a holder. Therefore, if the goods have been lost or damaged during the carriage then, although the ultimate receiver of the goods will normally be obliged to pay the seller of the goods pursuant to the terms of the contract of sale for the full shipped quantity of cargo, he is given the right as the lawful holder of the bill of lading to bring a claim against the carrier for any loss or damage that may have occurred at any time during the voyage since it is then the receiver who has in fact suffered the loss caused by any breach by the carrier of the contract of carriage.

When the bill of lading is made to the order of a named party (e.g. 'to order of X') the bill may be transferred from X to Y and thereafter from Y to Z etc., by the endorsement of the bill by X in favour of Y and by Y in favour of Z etc., together with the physical delivery of the bill from X to Y and from Y to Z etc. However, where the bill is simply made out 'to order' without any named party (i.e. a 'bearer bill'), transfer is effected simply by physical delivery of the bill from X to Y and from Y to Z etc., without any endorsement.

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<sup>11</sup> This distinction is explained further in Chapters 3.2.4.3 and 3.2.5.

<sup>12</sup> See Chapter 3.5.1.1.

<sup>13</sup> See Chapters 3.2.4.1 to 3.2.4.3.

<sup>14</sup> See Chapter 3.2.9.2.3.

A bill that is made out 'to order of X' can be converted into a bearer bill if X endorses the bill with the words 'to order' rather than 'to order of Y'. Thereafter, the bill is transferable as a bearer bill in the manner described above. Similarly, a bearer bill can be converted into a bill that is made to the order of a named party if the holder endorses the bill in favour of a specific party (e.g. 'to order of Y'). Thereafter the bill is transferable from Y to Z etc., in the manner described above.

When considering the pursuit of cargo claims under bills of lading it is normally necessary initially to consider three issues:

- Who is the carrier under the bill of lading;
- What are the terms of the bill of lading; and
- Who has the right to sue the carrier?

#### **3.2.4.1 Who is the Carrier under the Bill of Lading?**

For the reasons given above in Chapter 3.1 it is important to establish who is the carrier under the bill of lading since this will determine whether a claim is to be made in contract or in tort.

The fact that goods are carried on a particular ship does not necessarily mean that the shipowner is the carrier under any bills of lading that may have been issued for that cargo. Ships are often chartered either in full or in part to other parties who will then use the carrying capacity that they have thereby acquired to carry cargoes on that ship for their own customers. Such charterers may for commercial reasons wish to act as carriers under any bills of lading that may have been issued for such cargoes. This can occur in most trades but is particularly prevalent in the case of the container trade where container operators charter space on each other's ships but issue their own bills of lading for any cargoes that may be carried on a ship owned by another operator.

Where the bill of lading names the carrier expressly then that party is usually to be treated as the carrier for the purposes of any cargo claims that may be brought under that bill of lading. However, difficulties can often arise in the case of chartered ships when the particular form of bill of lading that is used does not expressly identify the carrier and it is unclear from the rest of the bill whether the carrier is to be the shipowner or the charterer. This can be so even if the form of the bill of lading that is used is the charterers' own house form. In the final analysis, the question is one of fact based on all the relevant circumstances. However, in the first instance, the question must be answered simply by a consideration of the provisions of the bill of lading without consideration of surrounding factors such as the terms of any charterparty pursuant to which the bill has been issued. Reference is made to surrounding factors only if the identity of the carrier is not clear from the provisions of the bill itself.



When considering the terms of the bill of lading the following presumptions will normally apply:

- The carrier is not necessarily the party which actually signs the bill but the party on whose behalf the signature was made;
- Bills of lading signed by the Master personally or by someone else (even the charterers or their agents) with authority to sign on behalf of the Master bind the shipowners (or where the ship is bareboat chartered, the bareboat charterers) as carriers;
- Bills of lading signed by the charterers personally or by someone else for or on behalf of the charterers which make it clear that the signature is not intended to bind the Master, bind the charterers as carrier.

However, the issue may be further complicated by clauses (usually on the back of the bill of lading) which are intended to clarify the issue but often succeed in complicating it. Such clauses (normally called 'Identity of Carrier' clauses) may provide as follows:

*"The contract evidenced by this Bill of Lading is between the Merchant and the Owner of the vessel named herein (or substitute) and it is therefore agreed that said shipowner only shall be liable for any damage or loss due to any breach or non-performance of ... the contract of carriage."*

The complication may arise when that clause clashes with other indications of the bill of lading (e.g. the bill is on the charterers' own form or includes the charterers' logo or appears to be signed for or on behalf of the charterers) which suggest that the carrier is someone other than the shipowners. However, in such circumstances, priority is to be given to the signature on the face of the bill and the typed or stamped words next to it. If these words make the identity of the carrier clear that conclusion is not to be overridden by printed terms on the back of the bill.

Despite these rules and presumptions the question of who is the carrier under the bill of lading can be a notoriously difficult one and legal advice should be taken at an early stage since the answer to the question may well determine the future strategy that should be followed in handling the claim.

#### **3.2.4.2 What are the Terms of the Bill of Lading?**

Under the common law a contract of carriage is concluded once the parties have agreed the terms of carriage. Therefore, a contract can be an oral contract and is perfectly enforceable subject to proving the terms of the agreement. However, proof can be difficult to establish in such circumstances and consequently, parties will invariably record the terms of the contract in writing. In such circumstances, the written document does not *per se* have the status of *the contract* but is in reality

merely evidence of the terms of the earlier oral agreement. In most cases, that distinction is merely academic, but it can become relevant if one party alleges that the written contract has not properly recorded the terms that have actually been agreed and applies for rectification of the contract.<sup>15</sup>

A carrier and a cargo interest will usually have agreed the terms of carriage before commencement of loading and the bill of lading (which will not be issued normally until after loading is complete) is in effect merely evidence of that earlier contract. However, since a bill of lading is a contract that is intended to be transferred to a third party (i.e. a consignee or endorsee) who will not be aware of the precise terms agreed before loading by the carrier and the shipper, the common law provides that whilst the bill of lading is merely *prima facie* evidence of the contract of carriage whilst it remains in the hands of the shipper, and can be rectified if needs be, it becomes conclusive evidence of the terms of carriage once it has been transferred to a third party who has relied on the written terms, and cannot thereafter be rectified. In other words, once the bill of lading has been transferred, it is then considered to be *the contract*.

Whilst there are many different forms of bill of lading they tend to fall into one of two basic types:

- 'Long' form bills which include all the relevant terms in the one document; and
- 'Short' form bills which purport to incorporate the terms of another document.

An example of a 'long form' bill is the Conlinebill which sets out all the relevant terms of carriage on the front and reverse of the same document whereas an example of a 'short form' bill is the Congenbill which is intended to incorporate the terms of the charterparty pursuant to which it has been issued and which provides that:

*"... All terms and conditions, liberties and exceptions of the charter ... including the Law and Arbitration Clause are herewith incorporated."*

The aim of the incorporation clause is to make the liability of the carrier under the bill commensurate with his liability under the pre-existing charterparty, thereby ensuring that the shipowner does not become subject to any additional liability under the bill of lading. However, this aim is often defeated by one or both of two separate difficulties:

- the use of insufficiently precise words of incorporation; and/or
- the effect of the Hague or Hague-Visby Rules.

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<sup>15</sup> For more detailed commentary see Chapter 23.6 (Remedies).

The incorporation difficulty is a notorious one in that different countries follow different rules. The usual rule under the common law is that unless the incorporation clause in the bill of lading refers expressly to a particular clause in the charterparty, a general reference (e.g. to 'all clauses of the charter') will not succeed in incorporating a clause which requires the words of the clause to be changed in order to make sense in the context of the bill of lading. Therefore, a general reference will not successfully incorporate into the bill of lading a clause of the charterparty which provides that a payment is to be made by 'charterers' since, in order to make sense in the bill of lading, it would be necessary to change 'charterers' to 'receivers'. However, if the incorporation clause refers expressly to a particular clause (e.g. to 'all clauses of the charterparty including the law and arbitration clause'), the arbitration clause in the charter may be successfully incorporated into the bill of lading despite the fact that in order to do so, it may be necessary to change the reference in the arbitration clause from 'charterers' to 'receivers'.

However, whilst this is the approach adopted by common law countries, other countries may be more reluctant to countenance any form of incorporation if the claim is brought by anyone other than the shipper or charterer on the grounds that a third party transferee was probably unaware of the terms of the charter and therefore, had not agreed to that particular arbitration or jurisdiction clause. This can result in difficult jurisdictional arguments when a claim is made.<sup>16</sup>

Secondly, whilst charterparties are subject to unfettered freedom of contract principles, the terms of bills of lading are normally severely regulated by a regime of various compulsory international conventions.<sup>17</sup> Therefore, a clause which is perfectly effective in the context of a charterparty may be void in the context of the bill of lading due to the compulsory application to such bills of lading of the Hague or Hague-Visby Rules. For example, Clause 2 of the Gencon charter provides that the owner is liable only if "... loss, damage or delay has been caused by **personal want of due diligence on the part of the carrier...**" There is "**personal want of due diligence**" only if there has been negligence on the part of the higher management of the carrying company. Such a clause is perfectly effective in the context of the charterparty. However, if such a clause is incorporated into a bill of lading it will come into conflict with the Hague or Hague-Visby Rules which provide that the carrier is liable if there is want of due diligence on the part of *any* of the carrier's

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<sup>16</sup> See Chapter 3.6 but for a more detailed commentary on issues that arise in relation to jurisdiction see Chapters 24 (Security Enforcement Measures) and 19 (Law and Jurisdiction).

<sup>17</sup> The provisions of the various international conventions which regulate the carriage of goods by sea are considered in Chapter 3.2.9 below.

servants or agents or independent contractors. Consequently, Clause 2 of the Gencon charter will be rendered void in the context of the bill of lading by Article III Rule 8 of the Rules.

However, even though these various international conventions do not apply compulsorily to charterparties, most charterparties will nevertheless incorporate one or other of such conventions by agreement through the medium of a Paramount Clause, in which case the liability of the carrier under the bills of lading and the shipowner under the charterparty may in fact be commensurate.

#### **3.2.4.3 Who has the Right to sue the Carrier?**

This issue is relevant since bills of lading are transferable contracts and may be transferred many times during the course of a voyage. For example, the shipper may transfer the bill to A on Monday, the cargo may be damaged on Tuesday, and A may transfer the bill to B on Wednesday who then transfers it to C on Thursday and the cargo is finally delivered to C on Friday. The original party to the bill of lading contract was the shipper, whilst A was the party to the contract on Tuesday when the cargo was damaged and C was the contractual party when it was finally delivered on Friday. Therefore, who has the right to sue the carrier – is it the shipper, or A, or C?

Most countries adopt a pragmatic approach to the question and the party that has the right to sue the carrier is normally the party that has suffered a financial loss as a result of the carrier's breach of contract. Therefore, in the example given above, it is likely to be C who has the right to sue since although A was party to the bill of lading on Tuesday when the cargo was damaged, it is likely that A has subsequently been paid in full for the cargo under the sale contract to B who has likewise been paid in full by C who is, consequently, the party that has suffered the loss. The fact that C was not a party to the bill of lading contract on Tuesday is not relevant since he has subsequently become a party to it on Thursday and has acquired the right under the bill to sue the carrier for any breach of contract that has occurred at any time during the carriage even if that was before C became a party to the contract.

The precise basis for this pragmatic approach differs from country to country. Some countries such as the United Kingdom have adopted a statutory approach in the form of the Carriage of Goods by Sea Act 1992 (COGSA 1992) whereby the right to sue the carrier is transferred from one bill of lading holder to the next as and when the bill of lading is transferred whereas other countries follow more traditional common law principles. However, notwithstanding the pragmatism of the approach, there are still technical problems which can affect the right of a claimant to sue the carrier and it is always necessary to consider, and if necessary, take legal advice as to whether a particular claimant does indeed have the right to bring the claim.

### 3.2.5 Straight Bills of Lading<sup>18</sup>

A straight bill of lading is similar to an 'to order' bill of lading in that it is also:

- a receipt for the goods; and
- good evidence of the contract of carriage of the goods; and
- a document of title in the sense that it enables the holder of it to obtain delivery of the cargo from the ship.

However, it differs from a 'to order' bill of lading in that it can only be transferred once from the shipper to the named receiver and cannot be transferred by the named receiver to anyone else. Therefore, if cargo is made deliverable 'to X', the shipper can transfer the bill to X but X cannot transfer the bill on to any other party. However, since the bill can be transferable once it must be produced to the carrier before delivery of the cargo in order to prove title to the goods. Accordingly, a straight bill of lading is considered in most countries to be a document of title and many standard forms of bills of lading make this clear by printed words that emphasise that delivery of the cargo must be made against production of the original straight bill.

### 3.2.6 Electronic Bills

Whilst the traditional form of bill of lading has been very successful over many centuries in formulating and facilitating international trade and the international carriage of goods, stresses are being experienced today because of the paper nature of the bill. Recent cases have demonstrated the relative ease with which forged or counterfeit bills can be produced. However, the most serious disadvantage arises from the legal need to surrender the original paper bill to the carrier in order to obtain delivery of the cargo at the port of discharge or to produce the original paper bill to satisfy customs or other authorities. In many cases, the need to convey the bills from seller to the buyer's bank and then on to the buyer can be very time consuming, particularly if there is a chain of cargo sales during the voyage. Conversely, the operational speed of ships has increased with the result that the ship often arrives before the documents. This results in substantial cost either in the form of hire or demurrage whilst the ship is kept waiting for the documents or by use of courier services or by provision of letters of indemnity or other securities to persuade the carrier to deliver the cargo without surrender of the bill.<sup>19</sup> Therefore,

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<sup>18</sup> See paras 2.44-2.48 of *Bills of Lading* by Aikens Lord and Bools, 2006, Informa.

<sup>19</sup> For more detailed commentary see Chapter 20.2.1 (Letters of Indemnity).

the industry has endeavoured for many years to see how it can replace the paper bill of lading with an electronic alternative which it is hoped will save substantial cost to the various stakeholders.<sup>20</sup>

It is now technologically possible to produce electronic bills that have substantial security safeguards and the sufficiency of electronic signatures as alternatives to manual signatures has been accepted by the laws of many countries.<sup>21</sup> However, there are currently no international conventions or laws which regulate the use of electronic bills.<sup>22</sup> Accordingly, the industry has been hesitant to embrace the concept fully since there is no guarantee of any recourse if difficulties arise. However, there are a few commercial organisations which provide a service to the industry that enables its members to trade with electronic bills on payment of a fee.<sup>23</sup> However, these schemes can work only if every party involved in the carriage is a member of the organisation since the regulation of the trade is effected by contractual agreement rather than by external governmental control through conventions and laws. Each member must agree to abide by the rules of the organisation which will regulate each member's rights and obligations. Consequently, if it is not known in advance whether all parties will be members of the scheme, it may be difficult to use it.

Because of the uncertainties that currently exist, the International Group of P&I Clubs was originally hesitant to provide cover for liabilities, losses, costs and expenses that arise from the use of an electronic trading system. However, such clubs have now agreed that liabilities arising in respect of the carriage of cargo under such systems can be covered subject to the restrictions that apply to traditional paper-based trading activities provided that the relevant system has first been approved by the International Group. The two systems that are currently approved by the Group are those administered by Electronic Shipping Solutions (the ESS system – version DSUA v. 2009.3) and that administered by Bolero International Ltd (the Bolero system – Rulebook/Operating Procedures September 1999).

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20 The United Nations Conference on Trade and Development (UNCTAD) has estimated that the use of paper documents is estimated to cost between 5 and 10 per cent of the value of all goods that are traded within a year or approximately USD 420 billion per annum. See The United Nations electronic Trade Documents (UNeDocs) Project a synopsis of which can be accessed at: [http://www.unece.org/fileadmin/DAM/trade/workshop/wks\\_capblid/unedocs\\_summary.pdf](http://www.unece.org/fileadmin/DAM/trade/workshop/wks_capblid/unedocs_summary.pdf).

21 See, for example, EU Electronic Signatures Directive 1999/93/EC.

22 The Hague, Hague-Visby and Hamburg Rules regulate 'documents'.

23 The most well known are the Bill of Lading Electronic Registry Organisation (BOLERO) and Electronic Shipping Solutions – Databridge (ESS.)

The Rotterdam Rules, if adopted by the industry, will allow electronic bills (or 'electronic transport documents' as they are called under the Rules) to be used and to have the same effect as traditional paper bills. Article 8 of the Rules provides that:

*"Subject to the requirements set out in this Convention:*

- (a) Anything that is to be in or on a transport document under this Convention may be recorded in an electronic transport document, provided that the issuance and subsequent use of an electronic transport document is with the consent of the carrier and the shipper; and*
- (b) The issuance, exclusive control, or transfer of an electronic transport record has the same effect as the issuance, possession, or transfer of a transport document."*

### 3.2.7 Sea Waybills<sup>24</sup>

Sea waybills are similar to bills of lading but with one important difference – they are not transferable contracts. A sea waybill is:

- a receipt for the goods; and
- good evidence of the contract of carriage of the goods; but is
- not a document of title since it is not transferable and need not therefore, be produced to the carrier before delivery of the cargo in order to prove title to the goods.

Therefore, during the currency of the voyage the sea waybill remains a contract between the carrier and the shipper and the carrier must comply only with instructions given by the shipper. However, the waybill will normally specify the name of the party to whom the cargo is to be delivered and therefore, unless the shipper subsequently declares otherwise, the carrier will be entitled to deliver the cargo to that party without requiring that party to surrender the waybill to him since by doing so, the carrier is in effect complying with the delivery instructions given by the shipper.<sup>25</sup> Most standard forms of sea waybills have express provisions to this effect.

However, the duty of the carrier to comply only with the instructions of the shipper restricts the usefulness of the sea waybill as a trading document and accordingly, the Comité Maritime International (CMI) sought to redress these difficulties in 1990 in the form of the *CMI Rules for Sea Waybills* which are not compulsorily applicable but which can be incorporated into sea waybills by agreement (See for example, the BIMCO Genwaybill). These Rules provide that the shipper has the option to transfer to the consignee named in the sea waybill the right to nominate the party to whom delivery is to be made. However, this option is exercisable no later than the time that

<sup>24</sup> See paras. 2.15-2.20 of *Bills of Lading* by Aikens Lord and Bools, 2006, Informa.

<sup>25</sup> See Chapter 3.2.9.2.3 for the difference between sea waybills and bills of lading in this regard.

the goods are received by the carrier. The receiver of cargo will often have paid the shipper for the shipment of a full cargo in apparent good order and condition, but may find when the cargo is delivered to him that loss or damage has occurred during the transit by sea. In such circumstances, the receiver faces a potential difficulty since the waybill evidences a contract between the carrier and the shipper and therefore, there is no contract of carriage between the carrier and the receiver. Under the laws of some countries such as the UK a solution has been found by providing the receiver with a statutory right to sue the carrier, but if such a solution is not possible, the receiver may have to rely on the goodwill of the shipper to bring a claim against the carrier on his behalf. This problem was also recognised by the CMI and the *CMI Rules for Sea Waybills* provides that the shipper enters into the sea waybill contract 'not only on his own behalf but also as agent for and on behalf of the consignee' thereby purporting to enable the consignee to bring an action against the carrier in his own name if necessary. However, it is uncertain to what extent this provision is enforceable in all jurisdictions.

The Hague and Hague-Visby Rules themselves do not apply compulsorily to sea waybills but some countries such as the UK have extended the applicability of the Rules to sea waybills under the local statute which gives force to the Rules under the local law. Furthermore, most standard forms of sea waybills provide expressly by means of a Paramount Clause that the Rules are to apply to the sea waybill by agreement as though the sea waybill were a bill of lading.

The Hamburg Rules do apply compulsorily to sea waybills since such a document is a "contract of carriage by sea" for the purposes of the Rules in that it is a "contract whereby the carrier undertakes against payment of freight to carry goods from one port to another" but is not a charterparty.

### 3.2.8 Delivery Orders<sup>26</sup>

A delivery order is a mechanism which enables an owner of goods to 'split' the total quantity under a bill of lading, e.g. 1,000 tons, into smaller units, e.g. 10 delivery orders for 100 tons each. This normally occurs when a bill of lading holder has bought the total quantity of cargo in one lot under one bill of lading but subsequently sells the cargo in smaller lots to different buyers. In such circumstances, the bill of lading holder cannot transfer the bill of lading for the total quantity to any one of the new buyers and will, therefore, require alternative documents from the carrier equal to the tonnage sold to each new buyer. Therefore, the holder of the bill of lading will normally surrender that bill to the carrier before or at the end of the voyage and request the carrier to produce substitute delivery

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<sup>26</sup> See paras 2.21-2.34 of *Bills of Lading* by Aikens Lord and Bools, 2006, Informa.



orders for each buyer, and to then deliver the cargo to the different buyers under the individual delivery orders. The rules relating to the surrender of bills of lading are considered below.

Each delivery order is usually made subject to the terms of the bill of lading which has been surrendered to the carrier. Therefore, theoretically, the liability of the carrier to each holder of the delivery orders is no different to the liability that the carrier had to the seller under the bill of lading. However, the situation is not always that simple. For example, if a cargo of 1,000 tons had originally been shipped under one bill of lading, the carrier would have no liability to the holder of the bill if a total of 1,000 tons was in fact delivered. However, if that bill of lading were to be replaced by ten delivery orders for 100 tons each, then even if the carrier were still to deliver a total of 1,000 tons, the carrier may nevertheless be liable to the holder of the final delivery order if he has in fact delivered 102 tons not 100 tons under one of the other delivery orders. In such circumstances, only 98 tons would be available for delivery to the holder of the final delivery order who can then be expected to bring a claim for short delivery.

This form of delivery order should be distinguished from another form of document which is sometimes also called a 'delivery order' but which is in fact nothing more than the order which is given by the carrier to a port authority or terminal to deliver cargo to a party that has demonstrated its entitlement to receive the cargo by presentation of the original bill of lading to the carrier or the carrier's agent.

### 3.2.9 The Relevance of Compulsory International Conventions<sup>27</sup>

There are three international conventions which are currently in force and which establish the minimum degree of liability that is to be borne by carriers. However, these conventions are intended to apply only to contractual claims and not to claims in tort. Whilst Article 4 bis 1 of the Hague-Visby Rules provides that "*the defences and limits of liability provided for in these Rules shall apply in any action against the carrier in respect of loss or damage to goods covered by a contract of carriage whether the action be founded in contract or in tort*", the English Court of Appeal has held in the case of *The Captain Gregos*<sup>28</sup> that the Rules can only apply when there is a contract of carriage between the claimant and the carrier, which means, in effect, that if there is a contract between the cargo claimant and the carrier, a claim against the carrier must be brought in contract and that the reference to claims in tort is of little if any relevance.

<sup>27</sup> For a more detailed commentary see Chapter 19 of the *Gard Handbook on P&I Insurance*, Chapter 10 of *Bills of Lading* by Aikens Lord and Bools, Informa 2006. and Chapter 85 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007.

<sup>28</sup> [1990] 1 Lloyd's Rep. 310.

The conventions provide that if a carrier tries to secure more protection than that which is allowed by the conventions then any clause in the contract of carriage which purports to have that effect will be *"null and void and of no effect"*.

The international conventions which are currently in force are the following:

- The Hague Rules;
- The Hague-Visby Rules; and
- The Hamburg Rules.

These Rules are not uniformly applied by all countries. Some countries are parties to the Hague Rules, some to the Hague-Visby Rules and a small number to the Hamburg Rules, whilst some countries are not parties to any of these conventions. Furthermore, even when countries have adopted a particular convention, they may have done so in a piecemeal and non-uniform manner. Therefore, the degree of protection that is available to a carrier is variable and it is always necessary to consider which, if any, of the Rules apply and in what manner.

In general terms, the liability that the carrier bears under the Hague and Hague-Visby Rules differs from the liability that the carrier bears under the Hamburg Rules in the following manner:

- Under the Hague and Hague-Visby Rules the carrier is not liable unless the cargo claimant proves that the carrier is in breach of specified duties, in which case the carrier can rely on specified rights of protection;
- Under the Hamburg Rules the carrier is deemed to be liable for loss/damage to cargo which occurs whilst the goods are in his charge unless he proves that he has taken *"all measures that could reasonably be required"* to care for them.

Nevertheless, there are also some important differences between the Hague Rules and the Hague-Visby Rules particularly in relation to the availability and quantum of package limitation rights.<sup>29</sup>

### **3.2.9.1 The Extent of the Regulation**

It is important to establish whether the Rules are to apply in any particular situation since if they do not apply, the relationship between the carrier and the cargo interest is subject to freedom of contract principles, whereas if the Rules do apply, some provisions of the contract may be deemed null and void. For example, Article III Rule 8 of the Hague and Hague-Visby Rules provides as follows:

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<sup>29</sup> See Chapter 3.2.9.4.

*“Any clause, covenant or agreement in a contract of carriage relieving the carrier or the ship from liability for loss or damage to or in connection with the goods arising from the negligence, fault or failure in the duties and obligations provided in this Article or lessening such liability otherwise than as provided in these Rules, shall be null and void and of no effect.”*

There is also a similar provision in Article 23 of the Hamburg Rules.

#### **3.2.9.1.1 The Hague and Hague-Visby Rules**

The Hague and Hague-Visby Rules do not apply compulsorily in all circumstances. For example, they do not apply compulsorily to:

- Contracts other than ‘to order’ or straight bills of lading;
- The responsibility of the carrier before loading and after discharging;
- Carriage from a country which is not a party to the Rules or to bills of lading which have been issued in a country which is not a party to the Rules;
- The carriage of live animals;
- The carriage of deck cargo which has been recorded on the bill of lading.

It is also debatable in some countries whether the Rules apply to claims for delay where there is no physical loss or damage.

However, parties will frequently extend the application of the Rules in such circumstances by agreement through the medium of a Paramount Clause. For example, the Rules are commonly applied by agreement to charterparties.

Nevertheless, the Rules do not apply at all to the following issues:

- Who is the carrier?
- Who can sue for cargo loss or damage?
- What is the relevant jurisdiction and law?
- The effect of a bill of lading as a document of title.

Since such issues are not regulated by the Rules, they are regulated by the law of the country that governs the relevant contract of carriage.

### 3.2.9.1.2 *The Hamburg Rules*

By contrast the compulsory ambit of the Hamburg Rule is much wider. The Hamburg Rules apply compulsorily to:

- All contracts (other than charterparties) under which freight is payable;
- The responsibility of the carrier from the time that the goods are delivered into his custody at the loading port until he delivers them into the custody of the receiver at the port of discharge;
- Carriage from or to a country which is a party to the Rules;
- The carriage of live animals and deck cargo;
- Claims for delay.

The Hamburg Rules also have compulsory provisions that regulate the jurisdiction where claims may be brought.

Furthermore, the Hamburg Rules place compulsory responsibility on both the carrier (who is defined as the party who enters into the contract of carriage with the shipper) and the actual carrier (if this is a different party to the carrier as defined). Such parties have joint and several liability for cargo claims.

### 3.2.9.2 *The Carrier's Obligations*

#### 3.2.9.2.1 *The Hague and Hague-Visby Rules*

The carrier has the following major duties under the Hague and Hague-Visby Rules:

Under Article III Rule 1:

- "1. The carrier shall be bound before and at the beginning of the voyage to exercise due diligence to:*
- a) Make the ship seaworthy.*
  - b) Properly man, equip and supply the ship.*
  - c) Make the holds, refrigerating and cool chambers, and all other parts of the ship in which goods are carried, fit and safe for their reception, carriage and preservation."*

The following factors are relevant in relation to this provision:

- The reference to *"the carrier"* includes all the carrier's servants, agents and independent contractors. They must all exercise due diligence;
- The reference to *"before and at the beginning of the voyage"* means that the carrier must prove that he has engaged in the practise of due diligence at all times that the ship has been in the carrier's control up to and including the commencement of the voyage;
- The exercise of due diligence means that there must be no negligence.

Under Article III Rule 2:

*"Subject to the provisions of Article IV, the carrier shall properly and carefully load, handle, stow, carry, keep, care for, and discharge the goods carried."*

The following factors are relevant in relation to this provision:

- The reference to *"the carrier"* includes all the carrier's servants, agents and independent contractors. They must all *"properly and carefully load etc."*;
- The carrier's duty under this provision is a continuing one throughout the time that he has the cargo in his care.

Under the common law (but possibly not under the law of all countries) the carrier and the cargo interests are allowed to decide *inter se* which of them is to perform the various cargo operations specified in the article and the carrier has the responsibility to perform *"properly and carefully"* only those operations that he has agreed to perform. For example, if the parties have agreed that the *cost and risk* of cargo operations is to be borne by the cargo owners on 'Free in and out' (FIOS) terms, the carrier may have the duty merely to *"properly and carefully ... carry, keep, care for, ... the goods carried"* since responsibility for the loading, handling, stowing and discharging of the goods has been transferred to the cargo interests. However, the mere transfer of *the cost* of such operations to the cargo owner is probably not sufficient to transfer the risk and clear terms will usually be necessary to absolve the carrier from his wider duties under Article III Rule 2.

#### 3.2.9.2.2 *The Hamburg Rules*

The carrier's liability under the Hamburg Rules is very different from the liability that he has under the Hague or Hague-Visby Rules. The carriage of live animals and deck cargo is subject to special rules but otherwise, the responsibility of the carrier and/or actual carrier is encapsulated in Article 5.1 which provides as follows:

*"The carrier is liable for loss resulting from loss of or damage to the goods, as well as from delay in delivery, if the occurrence which caused the loss, damage or delay took place whilst the goods were in his charge as defined in Article 4 unless the carrier proves that he, his servants or agents took all measures that could reasonably be required to avoid the occurrence and its consequences."*

Therefore, once the cargo claimant proves that the cargo has been lost, damaged or delayed whilst it was in the carrier's charge, the carrier is deemed to be liable and there is no need for the cargo claimant to prove how the cargo was lost, damaged or delayed or that it was due to the negligence of the carrier or his servants or agents.

### 3.2.9.2.3 The Delivery of the Cargo<sup>30</sup>

The carrier has a duty to ensure that the cargo is delivered at the end of the voyage to the party that is entitled to take delivery. If the Hamburg Rules apply such duty is probably regulated by those Rules since the Rules govern the carriage from the time that the carrier has taken over the goods from the shipper until *“the time that he has delivered the goods by handing over the goods to the consignee.”*

However, the Hague or Hague-Visby Rules make no express mention of the duty to deliver the goods and apply only *“from the time when the goods are loaded on to the time they are discharged from the ship”* (i.e. from tackle to tackle). The distinction is important since cargo may be ‘discharged’ when it is placed on the quay but may not be ‘delivered’ until it is subsequently handed over into the custody of the consignee. In the case of some trades (e.g. the tanker trade) there is no material distinction since the cargo is often both discharged and delivered at the moment that it passes from the ship through the manifold to the shore line. However, in the case of the container trade, the container may be discharged from the ship into the container receiving yard in the port area but may not be delivered for some days until the consignee comes to collect it.

In any event, even if the Rules do not apply, there is a long-standing rule of the common law which is now applied in most countries around the world and which provides that a carrier should not deliver cargo which has been shipped under a ‘to order’ or straight bill of lading unless and until the original bills of lading have been surrendered to him. The reason for the rule is that whilst the carrier has the duty to deliver the cargo to the party that is entitled to take delivery of the cargo, the carrier may have no idea who that is since the bill of lading may have been traded and passed from holder to holder a number of times during the voyage unbeknown to the carrier. Even if the bill of lading is a straight bill of lading, the carrier may not know whether delivery should be made to the shipper or to the named consignee as he will not know whether payment for the goods has been made in exchange for such bills. Therefore, since the bill of lading operates as a document of title, the carrier is entitled to deliver the cargo to the party who produces the original document of title to him. If the carrier delivers the cargo without requiring the surrender of the original bills of lading he ‘does so at his peril’ since, if he has in fact delivered to the wrong party:

- He will be liable to the true owner for the full value of the cargo that has been misdelivered; and
- He will not normally be entitled to rely on the protection of any of the exclusion clauses in the bill of lading; and

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<sup>30</sup> For a more detailed commentary see Chapter 21.3.7.1 of the *Gard Handbook on P&I Insurance and Chapter 5 of Bills of Lading*, by Aikens Lord and Bools, Informa 2006.

- He may prejudice his right to limit his liability; and
- He will normally have lost his P&I cover for liabilities arising as a result of the misdelivery.

Notwithstanding such rule, it is often the case that original bills of lading are not available at the time of delivery and, in order to prevent delay to the ship, carriers will often consider that they have no alternative for commercial reasons but to deliver cargoes without surrender of the original bills of lading against the offer of a letter of indemnity (LOI) from charterers or the party requiring delivery. In recognition of this reality, the International Group P&I Clubs have co-operated to produce a form of LOI which their members may consider using in such circumstances. However, it must be clearly understood that the clubs have done so purely as a service to their members. There is no obligation to use such forms; indeed, it must be emphasised that even if these forms are used, the member will still normally have lost his P&I cover for liabilities arising as a result of the misdelivery.

The obligation to deliver cargo against the surrender of the original bills of lading arises simply because it is a document of title and creates for the carrier the difficulty described above. Therefore, if the goods are carried under a sea waybill, there is no need for the carrier to demand surrender of the original waybill before tendering delivery of the cargo since the sea waybill is not a document of title. Therefore, the carrier is entitled to deliver in accordance with instructions received from the shipper without requiring proof of the shipper's entitlement to give such instructions. However, since a straight bill of lading may be transferred once from the shipper to the named consignee, the carrier cannot safely deliver to the named consignee without surrender by the consignee of the original bills of lading since, without surrender of such document, the carrier has no other means of knowing whether delivery should be made to the shipper or to the named consignee.

Difficulties can arise since bills of lading have traditionally been produced in sets of three originals each one of which is in effect a document of title. Therefore, the carrier runs a possible risk if he delivers the cargo against the surrender of less than the full set of original bills since a party other than the one to whom the cargo has been delivered could produce another original bill at a later date and demand delivery of the cargo. However, courts have tended to take the view that any party who pays for cargo other than against receipt of the full set of original bills runs a risk and that the carrier is entitled to deliver the cargo to whoever produces one original bill (in which case the other originals are considered to be 'accomplished', i.e. to cease to have the ability to operate as documents of title.) Most forms of bill of lading provide expressly that delivery can be made against production of one original bill of lading and this protects the carrier unless he is put on notice at the time that delivery is requested that another party is holding one or more of the

other original bills. Nevertheless, because bills of lading frauds have become more common in recent years, carriers are expected to be wary in such circumstances and to ask the party demanding delivery to explain why less than the full set of bills are being surrendered and run the risk if they do not do so that a court may conclude that delivery has not been made to the legitimate receiver.

### **3.2.9.3 The Carrier's Rights**

#### **3.2.9.3.1 The Hague and Hague-Visby Rules**

Under the Hague and Hague-Visby Rules the carrier is entitled to rely on any one out of a long list of possible defences. Most of the defences are *force majeure* in nature, e.g. Act of God, perils of the sea, inherent vice etc. However, there are two controversial defences which provide the carrier with a defence even when the loss or damage has been caused by the carrier's own negligence. These are in Article IV Rule 2 which reads as follows:

*"Neither the carrier nor the ship shall be responsible for loss or damage arising or resulting from –*

- a) Act, neglect or default of the master, mariner, pilot, or the servants of the carrier in the navigation or the management of the ship.*
- b) Fire, unless caused by the actual fault or privity of the carrier."*

Therefore, if the cargo has been damaged as a result of a collision which has been caused by the negligence of the master in the navigation of the ship, the carrier is not liable. However, the defence is not as comprehensive as might first appear to be the case since the carrier is not entitled to rely on any of the defences in Article IV Rule 2 unless and until he has proved that there is no causative breach of his overriding duty to exercise due diligence under Article III Rule 1.

#### **3.2.9.3.2 The Hamburg Rules**

There is no long list of possible defences under the Hamburg Rules. The carrier has a defence only if he is able to prove pursuant to Article 5.1 that:

*"... he, his servants or agents took all measures that could reasonably be required to avoid the occurrence and its consequences."*



### 3.2.9.4 Package Limitation

The carrier's first line of defence to any cargo claim is to prove that he is entitled to rely on a relevant exception clause. If he is able to prove such a right the claim will proceed no further. However, if the carrier has no right to rely on a relevant exception clause he may still be entitled to limit his liability for the claim to a sum which is less than the actual loss. There are two different kinds of limitation:

- Package limitation, i.e. the limitation of individual cargo claims in accordance with the number of packages or units or weight that has been lost or damaged; and
- Global limitation, i.e. the limitation of all qualifying claims (including cargo claims) arising out of any one incident in accordance with either the tonnage or value of the ship against which the claims are brought.

The carrier is entitled to rely on both types of limitation if needs be.<sup>31</sup> The carrier will normally apply the relevant package limitation to each individual claim and then, if the total of such claims (after application of the package limits) and all other qualifying claims of different types exceed the limits specified under the relevant tonnage limitation convention, the individual cargo claims may be further reduced pursuant to the provisions of the relevant tonnage limitation convention on a pro rata basis.<sup>32</sup> However, unless there are many other claims arising out of a major incident (e.g. damage to another ship and/or cargo, personal injury, damage to harbour works etc.), or the cargo claim is of a very high value, package limitation will normally be the carrier's sole limitation remedy in the event of cargo claims.

The Hague, Hague-Visby and Hamburg Rules all specify that whilst the carrier is entitled to increase the limitation threshold, they are not entitled to reduce it below the figures specified in the Rules.

**NB!** There is no right to package limitation if the value of the goods is recorded on the bill of lading (an *ad valorem* bill of lading). Consequently, there is no standard P&I cover for liabilities arising under such bills, and should a carrier agree to provide such a bill of lading, he will normally charge an enhanced freight.<sup>33</sup>

31 For a more detailed commentary on the issues that arise in relation to limitation of liability see Chapter 21 (Limitation of Liability), Chapters 27-30 of the *Gard Handbook on P&I Insurance* and Chapter 6 of the *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, 4th edition, 2005, Informa.

32 An example of such a calculation can be found in the case study in Chapter 28.5 of the *Gard Handbook on P&I Insurance*.

33 See Chapter 3.7 and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 vi).

### 3.2.9.4.1 The Hague Rules

Article IV provides that:

*"5. Neither the carrier nor the ship shall in any event be or become liable for any loss or damage to or in connection with goods in an amount exceeding £100 per package or unit or the equivalent of that sum in other currencies ..."*

Those countries that are still parties to the Hague Rules have replaced the reference to '£100' with a sum quantified in their own currency. However, to the extent that the unamended Hague Rules may be applicable in any particular situation, the reference to '£100' is in fact a reference to the gold value of £100 which is very substantially higher.

The words of the Hague Rules give rise to certain difficulties. For example, the right to package limitation is applicable only where the cargo can be fairly described as 'packages' or 'units' (which has been construed as a physical unit such as a truck.) Therefore, if the cargo is a bulk cargo, there may be no right to limitation. Similarly, it is debatable in the context of containerised cargo whether the relevant 'package' or 'unit' is the container itself (i.e. one unit) or the 'packages' or 'units' stuffed in the container (i.e. many units). The English court takes the view that provided that the cargo that has been stuffed inside the container can truly be said to be packages or units then the relevant package or unit is the cargo package or unit rather than the container.<sup>34</sup> However, the US courts have tended to be guided by the manner in which the bill of lading describes the cargo.<sup>35</sup> Therefore, a bill of lading recording the shipment of 'one container said to contain 99 bales of leather' was treated as recording the shipment of 99 bales whereas a bill of lading evidencing the shipment of 'one container said to contain machinery' was treated as a bill of lading recording the shipment of a single package although, in fact, it contained 350 individual cartons.

The Hague-Visby Rules seeks to cure these ambiguities.

Whilst limitation has traditionally been considered to be a privilege which can be lost if the carrier is guilty of reprehensible conduct, the words '*in any event*' have been construed in some jurisdictions as indicating that it is extremely difficult for the carrier to lose the right of limitation under the Hague Rules.

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<sup>34</sup> *The River Gurara*, [1998] 1 Lloyd's Rep. 225.

<sup>35</sup> See *Standard Electrica v Hamburg Sudamerikanische*, [1967] 2 Lloyd's Rep. 193 (US Court of Appeal, 2nd Cir.)

#### 3.2.9.4.2 The Hague-Visby Rules

The Hague-Visby Rules differs from the Hague Rules in the following manner:

- The package limitation is increased significantly and there is an alternative limitation based on the weight of the cargo which is intended to ensure that limitation is available in the case of bulk cargoes;
- The relevant limitation in the case of containerised cargo is based on *“the number of packages or units enumerated in the bill of lading as packed in such”* container;
- The right to limitation may be lost if *“the damage resulted from an act or omission of the carrier done with intent to cause damage, or recklessly and with knowledge that damage would probably result”*.<sup>36</sup>

#### 3.2.9.4.3 The Hamburg Rules

The Hamburg Rules mirror the Hague-Visby Rules to a large extent but differ in the following manner:

- The limitation sums are increased by approximately 25 per cent;
- There is a special limitation for delay claims which is quantified in accordance with the freight that is payable.

#### 3.2.9.5 Time Limits

It is the public policy of practically all countries to provide that claims must be brought within a specified period of time failing which the claims will thereafter be unenforceable. The relevant time limit will vary depending on the particular country. However, most cargo claims will be subject to the time limit provisions of the Hague, Hague-Visby or Hamburg Rules.

##### 3.2.9.5.1 The Hague and Hague-Visby Rules

The Hague and Hague-Visby Rules provide that claims must be brought against the carrier within one year of the delivery of the cargo or, in cases where the goods are never delivered, within one year of the date when they should have been delivered. Claims are not brought for these purposes unless and until court or arbitration proceedings have been commenced. Therefore, the mere notification of a claim does not suspend the time limit. Consequently, it is common for cargo claimants to request the carrier to grant a time extension, i.e. for additional time within which to commence legal proceedings. Carriers are not obliged to grant such requests, but may wish to do so if they believe that the claim may be settled without the need to incur the costs of legal proceedings

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<sup>36</sup> This is also the test that is applied in most other limitation conventions such as the 1976 Limitation Convention, the Hamburg Rules etc.

It must be emphasised that the time limit specified in the Rules is a 'one-way' time limit. It applies merely to claims *against* the carrier and not to claims by the carrier. The Rules do not regulate the time limit for claims that may be brought by the carrier and consequently, the time limit for such claims depends on the law that governs the contract. For example, if the bill of lading is subject to English law, a cargo claim against the carrier will be subject to the one year time limit specified in the Rules whereas a claim by the carrier against the cargo interests (e.g. for freight) will be subject to a time limit of six years.

#### 3.2.9.5.2 *The Hamburg Rules*

The provisions of the Hamburg Rules differ from those of the Hague and Hague-Visby Rules in the following respects:

- The relevant time limit is two years, not one year; and
- The time limit applies to claims both against and by the carrier, i.e. it is a 'two-way' time limit.

#### 3.2.9.6 Multimodal and Through Transport<sup>37</sup>

The traditional form of shipment in which the whole of the transportation is performed merely from port to port by one carrier is no longer the norm. The development of the container has had a dramatic impact on traditional shipping systems and it is now possible for cargo to be carried in the one container from an inland location in one country to another inland location in another country by various means of transport without any disturbance to the contents of the container.

Although these terms are often used interchangeably, a distinction should strictly be drawn between multimodal transport and through transport. Multimodal transport is where the carrier assumes responsibility for the whole of the carriage from door to door but the goods are delivered by a combination of different transport modes (e.g. by road/rail/sea etc.). Through transport is where goods are carried solely by sea but the carriage involves transshipment at one or more points during the transit and the carrier (although he may collect freight for the whole of the carriage from door to door) assumes responsibility as carrier only for the first leg of the transit (usually carriage on his own vessel) and merely acts as agent for the cargo owner in arranging onward carriage on another ship as from the transshipment point. Therefore, in the case of multimodal transport, a claim may be brought against the carrier should loss or damage occur at any point during the carriage door to door whereas in the case of through transport, a claim for loss or damage can be

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<sup>37</sup> For a more detailed commentary see Chapter 11 of *Bills of Lading*, by Aikens Lord and Bools, Informa 2006.

brought against the carrier only if the loss or damage occurs whilst the goods are being carried on his own vessel, and claims for loss or damage that occurs after transshipment can normally be brought only against the transshipment vessel.

It is a fundamental characteristic of multimodal transport that whilst one contractual carrier may assume contractual responsibility for the whole of the carriage of the cargo from one inland location to another inland location by land, sea or air, responsibility for various sectors of the overall transportation will often be delegated to other parties. Therefore, in a substantial number of such cases, the contractual carrier is a non vessel owning carrier (NVOCC) who will then delegate the sea carriage to the shipowner.

Such form of transport is subject to the following difficulties:

- There is currently no international convention in force which regulates the whole of the carriage whether by land, sea or air;
- Different sectors of the overall transport are regulated by separate international conventions (unimodal conventions) which have different terms (e.g. the Hague or Hague-Visby or Hamburg Rules for sea carriage, the Warsaw/Montreal Conventions for air carriage, CMR for land carriage and CIM/COTIF for rail carriage);
- Some sectors of the overall transport are not regulated by any international conventions but by national laws or local carriage terms which can differ substantially;
- The fact that the container remains sealed for the whole of the carriage often makes it difficult to establish where the loss or damage occurred and therefore, which international convention, local laws or carriage terms are to apply;
- Sub-contractors are vulnerable to claims in tort.

In order to counter such difficulties most multimodal bills of lading adopt the 'network system' which operates as follows:

- If it can be established that the loss or damage occurred during carriage by any particular transport mode, and that such carriage is regulated by a compulsory unimodal international regime, then that regime will apply;
- However, if it cannot be established that the loss or damage occurred during carriage by any particular transport mode, the liability will be determined in accordance with specific terms of the bill of lading which are to apply in such circumstances.

Finally, most bills of lading protect the interests of sub-contractors by the inclusion of special clauses.<sup>38</sup>

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<sup>38</sup> See Chapter 3.3.1.

### 3.2.9.7 The Rotterdam Rules<sup>39</sup>

The current system of regulation for the international carriage of goods suffers from the following deficiencies:

- There is no consistency in the form of regulation that is implemented by different countries for the carriage of goods by sea since different countries apply three different conventions in an inconsistent manner;
- The different legs of multimodal transport are regulated either by separate unimodal conventions or by no conventions with the consequence that liability differs depending on whether loss or damage occurred during the sea, land, rail or air leg of the carriage.

Consequently, efforts have been made to replace the current system with one convention which is intended to apply a uniform form of regulation for all modes of international carriage of goods provided that at least one leg of the overall transport is by sea. The result of these efforts is the UN Convention on Contracts for the carriage of Goods Wholly or Partly by Sea (The Rotterdam Rules). This convention is not yet in force but will, if adopted, introduce substantial changes. The new convention has 96 Articles and it is not possible to comment on each and every change. However, the most important changes are as follows:

- The Hague, Hague-Visby and Hamburg Rules will be repealed and replaced by the Rotterdam Rules;
- A carrier of goods by sea must exercise due diligence to keep the ship seaworthy throughout the voyage;
- The defence of negligent navigation will no longer be available;
- The Rules will apply uniformly to all legs of multimodal carriage unless, in the case of carriage other than by sea, that leg is subject to one of the compulsory international unimodal conventions;
- The contractual carrier is responsible for the acts and omissions of all of his sub-contractors;
- A sub-contractor who performs services either in the port of loading or during the voyage or at the port of discharge (i.e. a maritime performing party) will be jointly and severally liable to cargo claimants together with the contractual carrier. However, the Rules do not make sub-contractors who do not perform services at such stages of the transit (e.g. an inland road carrier), directly liable to cargo claimants (although such carriers might still have personal liability under the local law of the country where the transit took place);

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<sup>39</sup> For a more detailed commentary on the Rotterdam Rules see *A New Convention for the Carriage of Goods by Sea: The Rotterdam Rules*, 2009, Lawtext.

- The use of electronic contracts of carriage will be recognised and regulated;
- The package limits of liability are increased; and
- The time limit for claims is increased to two years and the time limit applies not only to claims against carriers but also to claims by carriers.

It is possible to avoid many of the provisions of the Rotterdam Rules if the relevant contract of carriage falls within the definition of a 'volume contract', i.e. *"a contract of carriage that provides for the carriage of a specified quantity of goods in a series of shipments during an agreed period of time."*

The Rotterdam Rules also introduce detailed compulsory jurisdictional regulations which will have the effect of limiting the effectiveness of traditional contractual jurisdictional clauses. However, this is one part of the Rotterdam Rules that countries who wish to adopt the Rules can exclude should they so wish.

### 3.3 Liability in Tort<sup>40</sup>

The fact that there may be no contractual link between the owner of the cargo and the person who causes damage or loss to them does not mean that the person who causes damage or loss has no liability for the damage or loss. It is a fundamental principle of the law system of most countries that each person has a duty to take care not to cause damage or loss to the property of another person.<sup>41</sup> Accordingly, if the owner of the cargo can prove that the damage or loss has been caused by the negligence of someone who is not the contractual carrier then he may be entitled to bring a claim against that party in tort. Furthermore, since that party is not a party to the contract of carriage between the owner of the goods and the carrier that party may not be able to rely on any exception clause in that contract even if that clause was intended to benefit him.<sup>42</sup>

Liability in tort normally arises in two situations:

- Where the contractual carrier is not the shipowner (e.g. a charterer or freight forwarder) and the carriage is delegated to a shipowner who causes loss or damage to the cargo during the carriage; or
- Where loss or damage to the cargo is caused by a sub-contractor of the carrier (e.g. a stevedore).

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<sup>40</sup> For a more detailed commentary see Chapter 9 of *Bills of Lading*, by Aikens Lord and Bools, Informa 2006.

<sup>41</sup> For more detailed commentary see Chapter 14 of the *Gard Handbook on P&I Insurance*.

<sup>42</sup> However, a carrier may be protected in some circumstances pursuant to the doctrine of bailment on terms. See Chapter 3.3.1 below.

Claims in tort may prove an attractive remedy to a cargo claimant where the carrier under the bill of lading is the charterer or NVOCC and it is proved that the loss or damage has been caused by the shipowner during the carriage. In such circumstances, the cargo claimant may prefer not to sue the carrier but to sue the shipowner and to arrest the ship for security for the claim. Such a strategy may prove to be even more attractive if there are doubts about the financial health of the contractual carrier.

However, a claim in tort can be brought only by the party who was entitled to possession of the cargo at the time when the negligence occurred. Therefore, a claim in tort may not be possible in all circumstances. For example, if cargo is shipped on Monday by A, is damaged on Wednesday, and sold by A to B on Thursday, B cannot bring a claim in tort against the shipowner if he finds on taking delivery of the cargo on Saturday that the cargo is damaged. A, as the party entitled to possession on Wednesday, would be entitled to bring such a claim. However, A may well have been paid by B in full on Thursday and will, therefore, have no interest in bringing such a claim. Consequently, B's only remedy will be the contractual claim against the carrier under the bill of lading.

### **3.3.1 The Protection of Third Parties**

The traditional form of port-to-port shipment involved merely two parties – the carrier and the cargo owner – and the whole of the transportation was performed by one carrier. However, modern systems are far more complex and involve a substantial degree of sub-delegation. For example, shipowners no longer load or discharge cargoes themselves but engage specialist stevedores to do the work for them. Furthermore, it is a fundamental characteristic of multimodal transport that whilst a carrier assumes contractual responsibility for the carriage of the cargo from one inland location to another inland location by land, sea or air, responsibility for various sectors of the overall transportation will be delegated to other parties. Therefore, it may well be that the cargo is lost or damaged whilst it is in the custody of the sub-contractor and such a sub-contractor may be vulnerable to a claim in tort from the cargo owner.

There is a general recognition in the industry that such third parties need protection. However, no international convention that is currently in force provides such protection. The domestic law of some countries does provide such protection (e.g. the Contracts (Rights of Third Parties) Act 1999 of the UK). However, such laws are relevant only if the dispute is subject to the law of that country. Consequently, the industry has developed its own form of protection by the development of standard clauses for inclusion in bills of lading. The classic clauses are the following:



- The Himalaya Clause which specifies that the contractual carrier enters into the bill of lading not only for his own account but also as agent for sub-contractors, thereby creating a contractual relationship between the cargo owner and the sub-contractor and enabling the sub-contractor to rely on various defences in the bill of lading;<sup>43</sup>
- The Circular Indemnity Clause in which the cargo owner promises not to bring a claim against anyone other than the contractual carrier and to indemnify the carrier if that promise is broken.<sup>44</sup>

Finally, there has in recent years been a development whereby a third party may be able to rely either on the terms of contracts between the contractual carrier and the cargo owner or on his own standard terms of business for protection pursuant to the doctrine of bailment.<sup>45</sup> Bailment is a common law doctrine whereby a person who voluntarily takes possession of the property of another (the bailee) has the responsibility to take care of the property regardless of whether there is a contract between them, and to return it to its owner (the bailor) on request in the same good order and condition. However, the bailee is entitled, before taking possession of the property, to notify the bailor that he will do so subject to terms that may protect him against liability. Therefore, if the bailor subsequently delivers the property into the possession of the bailee, he is deemed to have accepted that the bailment will be subject to such terms and that the bailee can rely on the protection of such terms should the property be lost or damaged whilst in his possession.

Therefore, a bailment is created when goods are voluntarily accepted by a sub-contractor pursuant to a contract between the carrier and the goods owner. However, if the contract between the carrier and the goods owner gives notice that the goods may in fact be carried by a third party on different terms, the goods owner may be deemed to have accepted such terms if he subsequently allows his goods to be carried pursuant to such arrangements. In such circumstances, the cargo owner will have been put on notice that a third party who will be involved in the carriage will be relying on such terms for protection and has accepted that eventuality.<sup>46</sup> However, bailment is an extremely complicated concept and requires parties to take legal advice for further clarification.

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43 For a detailed commentary on the Revised Himalaya Clauses that has been drafted by the P&I clubs that are members of the International Group see *Gard Circular No. 11 of 2010* (September 2010) which can be found at: <http://www.gard.no/ikbViewer/Content/8475980/Member%20Circular%2011%202010%20Himalaya%20clause.pdf>.

44 For a fictional example based on the principles outlined in *The Elbe Maru*, [1978], 1 Lloyd's Rep. 206, see the Case Study in Chapter 23.11 (Remedies).

45 For more detailed commentary see paras 9.38 to 9.80 of *Bills of lading*, by Aikens Lord and Bools, Informa 2006.

46 See *The KH Enterprise*, [1994] Lloyd's Rep. 603.

### 3.4 Indemnity Claims under Charterparties<sup>47</sup>

If claims are brought under bills of lading which are issued pursuant to a charterparty then the carriers under the bills of lading (whether they be the shipowners or the charterers) may wish, if they are held liable to the cargo claimant, to claim an indemnity from the other party to the charterparty. The merits of such an indemnity claim will depend on the terms of the charter and the cause of the cargo damage/loss. However, in the majority of cases, if the liability that the carrier has under the bills of lading is greater than the liability that he would have if the same claim had been brought under the charterparty, the carrier is entitled to an indemnity from his contracting partner under the charterparty for the 'extra' liability that he has incurred under the bill of lading.

If the cargo claim arises because of the unseaworthy nature of the carrying ship then in the majority of cases, the shipowner, if he is the carrier under the bills of lading, will have no right to claim an indemnity from the charterers, whilst the charterers, if they are the carriers under the bills of lading, will have the right to claim an indemnity from the shipowners.

However, if the cargo claim arises because of the failure to care for the cargo the matter is more complicated. A failure to care for the cargo during the transit can normally be attributed to the negligence of the crew (and therefore, to the negligence of the shipowner) in which case, the situation is similar to that just explained in relation to unseaworthiness. However, if the cargo claim relates to loss or damage caused during the loading or stowage or discharging of the cargo the responsibilities of the shipowners and charterers *inter se* depends on the terms which have been agreed for these cargo operations. For example, if the parties have agreed FIOS terms, the responsibility for such operations will be assumed by the charterers. Therefore, if the shipowner is liable as carrier under the bills of lading for such claims, the shipowner may be entitled to claim an indemnity from the charterers whilst the charterers, if they are the carriers under the bills of lading, will have no right to claim an indemnity from the shipowners.

The rights of shipowners and charterers to claim indemnities *inter se* under dry cargo time charters for loss or damage caused by cargo handling is notoriously complicated. Consequently, the industry has developed a special system to regulate such claims under the New York Produce Exchange 1946 and 93 forms of time

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47 For a more detailed commentary see Chapters 19-21 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008, and paras 3.129-3.138 of *Bills of Lading*, by Aikens Lord and Bools, Informa 2006.

charter. The system, called the Inter-Club New York Produce Exchange Agreement (ICA), is a 'rough and ready' allocation of responsibility between shipowners and time charterers for various types of claims.<sup>48</sup>

Originally, the ICA was simply an agreement between P&I clubs to recommend to their members that indemnity claims would be settled on the terms of the Agreement. However, it has now become common for the ICA to be included in dry cargo time charters as a term which is directly binding on the parties themselves.<sup>49</sup>

The ICA has been repeatedly amended over the years and the current version is that of 1996 as further amended in September 2011. The agreement is detailed and provides in a 'rough and ready' manner that, unless there are 'material amendments' to the printed provisions of the charter, cargo claims are to be apportioned as follows:

- a** Claims caused by the unseaworthiness of the vessel and/or by error or fault in the navigation or management of the vessel are to be borne 100 per cent by shipowners unless the shipowners prove that the unseaworthiness was caused by the loading, stowage, lashing, discharge or other handling of the cargo, in which case the claim shall be apportioned under sub-clause (b).
- b** Claims caused by the loading, stowage, lashing, discharge, storage or other handling of cargo are to be borne 100 per cent by charterers unless the words 'and responsibility' are added to Clause 8 of the NYPE forms of charters or there is a similar amendment making the master responsible for cargo handling, in which case the apportionment is to be borne 50 per cent by charterers and 50 per cent by shipowners unless the charterers prove that the failure to properly load, stow, lash, discharge or handle the cargo was caused by the unseaworthiness of the vessel, in which case, liability is borne 100 per cent by shipowners.
- c** Subject to (a) and (b) above, claims for shortage or overcarriage are to be borne 50 per cent by charterers and 50 per cent by shipowners unless there is clear and irrefutable evidence that the claim arose as a result of pilferage or the act or neglect of one or the other (including their servants or sub-contractors), in which case that party shall then bear 100 per cent of the claim.
- d** All other cargo claims whatsoever (including claims for delay to cargo) are to be borne 50 per cent by charterers and 50 per cent by shipowners unless there is clear and irrefutable evidence that the claim arose as a result 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 per cent of the claim.

<sup>48</sup> For more detailed commentary see Chapter 20 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

<sup>49</sup> See, for example, Clause 27 of the NYPE 93 form of charter.

The September 2011 amendments to the ICA 1996 also introduced a new provision which enables a party that has been obliged to provide security for a cargo claim that has been brought by a third party claimant to demand security in an acceptable form from his contracting partner under the charterparty provided that the requesting party is prepared to reciprocate by providing security in an acceptable form and for an equivalent amount to that other party.

### **3.5 The Importance of Evidence**<sup>50</sup>

It is normally difficult to pursue a claim without supporting evidence since without evidence the cause of the loss or damage cannot be established. The mere fact that cargo has been lost or damaged during transit does not automatically mean that the cargo owner is entitled to make a recovery from someone else. In some instances the loss may lie where it falls, i.e. the cargo claimant may have to bear his own loss. Therefore, if the cargo claimant wishes to establish the liability of some other party, it is necessary firstly to establish the cause of the loss or damage and secondly, to prove that he is entitled to be indemnified by someone else for loss or damage so caused.

A claimant will normally wish to establish the cause of the loss or damage for the purposes of the following contracts:

- The contract of sale;
- The contract of carriage; and/or
- The contract of insurance.

The terms upon which these contracts entitle the claimant to a recovery differ. Therefore, evidence is necessary to establish which contract (if any) will entitle the claimant to indemnification. For example:

- if the cargo has been damaged by inherent vice, there will normally be no right to recover under the contract of carriage or the contract of cargo insurance, but there may be a right of recovery under the contract of sale;
- if the cargo has been damaged by the unseaworthiness of the ship, there will normally be no right to recover under the contract of sale, but there will be a right of recovery under the contract of insurance and/or the contract of carriage;
- if the cargo has been damaged by a collision, there will normally be no right to recover under the contract of sale or the contract of carriage, but there will be a right of recovery under the contract of insurance;
- if the cargo has not been damaged at all but is found to be of inferior quality, there will normally be no right to recover under the contract of carriage or the contract of insurance, but there may be a right of recovery under the contract of sale.

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<sup>50</sup> For a more detailed commentary on the importance of evidence and of the steps that need to be taken to obtain and preserve such evidence see Chapter 27 (Claims Management) and section 3.2 (Cargo damage or loss) of the *Gard Guidance to Masters*.

The need for evidence is important both for the claimant and for the respondent. It is important for the claimant in order to prove that the loss or damage has been caused by an event for which the respondent is responsible. It is equally important for the respondent either to disprove such an allegation and/or because he may wish to rely on the terms of the contract or the various international conventions to protect him against liability. Therefore, evidence is all important and care must be taken to monitor and record the carriage from the moment that the cargo leaves its original location until it is delivered to its final location. A failure to do so may seriously affect the merits of a claim or a defence to a claim.

There will usually be three sources of evidence:

- Carrier source evidence;
- Cargo source evidence;
- Survey evidence.

### 3.5.1 Carrier Source Evidence

The evidence that may be obtained from carriers relates to both the cargo and the ship.

#### 3.5.1.1 Evidence of Cargo<sup>51</sup>

A carrier will normally check both the quantity and apparent order and condition of the cargo at the time that it is received by the carrier. Such information is normally recorded in documents such as the mate's receipt or the cargo manifest. When loading is complete, the information so recorded is transferred onto the formal documents that are used in order to record the carriage, i.e. the bill of lading, sea waybill etc. These documents constitute a formal receipt that is intended to be for the benefit not only of the shipper, but also for the benefit of subsequent transferees of the documents who were not present in person to witness the actual shipment of the goods and who will, consequently, be relying on the truth of the receipt provided by the carrier.

A bill of lading or sea waybill will normally record the following data:

- The apparent order and condition of the goods;
- The quantity or weight of the goods;
- The date and place of shipment.

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<sup>51</sup> For a more detailed commentary see Chapters 4 and 10 of *Bills of Lading* by Aikens Lord and Bools, Informa 2006.

### 3.5.1.1.2 *The apparent Order and Condition of the Goods*

It is important to understand that the bill of lading or sea waybill records:

- The condition not the quality of the goods; and
- Only that condition which is apparent, i.e. visible.

The quality of the goods is a description of the inherent or natural state of the goods when produced. However, the condition of the goods is a description of whether or not the goods have been damaged after production. The distinction may sometimes be difficult to establish but is nevertheless important since the quality of the goods is not relevant as between the carrier and the cargo owner under the contract of carriage, or as between the cargo owner and the cargo insurer, but is relevant as between the seller and buyer of the cargo under the contract of sale.

Since the bill of lading or sea waybill is no evidence of the quality of the goods, contracts for the sale of goods will normally provide that payment is to be made not only against a bill of lading or sea waybill but also against provision of a certificate of quality proving that the goods are of the right quality.<sup>52</sup>

The bill of lading or sea waybill merely records the apparent (i.e. visible) condition of the goods at the time of shipment. Therefore, if the goods are presented for carriage in a packed condition, the document will not record the condition of the goods within the packaging but merely the visible condition of the exterior packaging. Therefore, in trades such as the container trade, the bill of lading or sea waybill does not constitute meaningful evidence of the condition of the goods.

Furthermore, the ship's crew are not expected to be scientists or experts in any particular trade and therefore, their obligation is merely to take note of any visible features and to exercise their judgement as reasonable seafarers as to whether or not the goods are damaged. If the exercise of such judgement leads to the conclusion that the goods are damaged then the carrier has the duty to include a clause to that effect on the face of the bill in order to give notice to any subsequent transferee of the bill that the goods were already damaged prior to shipment and thereby protect the carrier's interests in the event of any future claim that such damage was caused by the carrier during the carriage. If the carrier does not do so then he may have no defence to a claim brought by a subsequent transferee of the bill and will have no right of recourse against the shipper since

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<sup>52</sup> See Chapter 3.5.2 below.

the Hague, Hague-Visby and Hamburg Rules give no right of indemnity in such circumstances. Furthermore, the carrier may have no P&I cover for liabilities incurred in such circumstances.<sup>53</sup>

Nevertheless, the carrier must exercise caution when clausing the bill in this way since a bill of lading which includes such a clause is not a 'clean bill of lading' and may therefore frustrate the ability of the shipper to obtain payment for the goods under the contract of sale or accompanying letter of credit. For example, Article 27 of the ICC Uniform Customs and Practice for Documentary Credits (UCP 600) which govern the acceptability of documents including bills of lading for the purposes of letters of credit defines a 'clean transport document' as follows:

*"A bank will only accept a clean transport document. A clean transport document is one bearing no clause or notation declaring a defective condition of the goods or their packaging. The word 'clean' need not appear on a transport document, even if a credit has a requirement for that document to be 'clean on board'."*

#### **3.5.1.1.3 The Quantity or Weight of the Goods<sup>54</sup>**

In some instances, usually involving the shipment of bulk cargo, it is not possible to establish categorically exactly how much cargo has in fact been shipped. In such circumstances, Article III Rule 3 of the Hague and Hague-Visby Rules entitle (but do not oblige) the carrier to sign bills of lading for the quantity or weight that has *"been furnished in writing by the shipper."* The shipper is deemed to have guaranteed the accuracy of the quantity or weight furnished by him and Article III Rule 5 of the Hague and Hague-Visby Rules obliges the shipper to indemnify the carrier in such circumstances. However, if the carrier, although doubting the accuracy of the figures provided by the shipper, nevertheless agrees to issue the bill in accordance with those figures, he may have to settle a claim brought by a transferee of the bill before seeking an indemnity from the shipper. Indeed, if the carrier agrees to issue the bill in accordance with figures provided by the shipper which the carrier *knows* to be inaccurate, he will probably lose his P&I cover for the claim that may be brought by the transferee of the bill.<sup>55</sup>

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<sup>53</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 x (Cargo Liability)).

<sup>54</sup> This Chapter should be read together with Chapter 3.5.1.1.4 in order to obtain the full picture.

<sup>55</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 x (Cargo Liability)).

Therefore, if the carrier believes that the figures provided by the shipper may be inaccurate, the following alternatives are normally available to him:

- 1 He may issue the bill in accordance with the shippers' figures and claim an indemnity from the shippers if he is subsequently obliged to settle a shortage claim brought by the transferee of the bill. It is also sensible in such circumstances to issue a note of protest when releasing the bill of lading or sea waybill notifying the shipper that the carrier is not convinced by the shipper's figures. However, the issue of a protest is unlikely to prevent the carrier from incurring liability to a receiver. Furthermore, if the carrier *knew* that the figures were inaccurate, he may not only lose his P&I cover but also any right to claim an indemnity from the shippers or from the charterers (if they have presented the bills to the carriers for signing.)
- 2 He may clause the bill by recording the ship's figures next to the shipper's figures thereby notifying a transferee of the bill that the carrier does not accept the shipper's figures. This is the safest course of action for the carrier, but also the most difficult since shippers will be reluctant to accept claused bills of lading in case they are rejected by the buyer under the contract of sale or by a bank under the letter of credit.
- 3 He may refuse to sign the bill pursuant to Article III Rule 3 of the Hague and Hague-Visby Rules if "*he has reasonable grounds for suspecting (that the bill does) not accurately ... represent the goods actually received*" or if "*he has had no reasonable means of checking.*" However, since the cargo has been loaded, a bill of lading will have to be issued at some point in time and therefore, this remedy is normally helpful merely to enable the carrier and/or shippers to have some additional time to double-check the figures before issuing the bill.
- 4 He may seek to rely on a general printed protective clause such as 'weight unknown' or 'quantity unknown' which is normally found in most bill of lading forms. This is considered further in the following section.

However, if the carriage is subject to The Hamburg Rules it does not seem that the carrier can make use of alternatives 3 and 4 above.

#### **3.5.1.1.4 The Evidential Value of the Documents**

If it is proved that goods have been shipped in apparent good order and condition but have been delivered in a damaged condition, or that less cargo has been delivered than the quantity or weight recorded on the bills of lading or sea waybill, there is a presumption that the goods have been damaged or lost as a result of a ship board incident. The onus is then on the carrier to prove the cause of the loss or damage and to prove that he is entitled to a defence in such circumstances. Therefore, the bills of lading and sea waybills have an important evidential value.



Whilst these documents remain in the hands of the shipper, the bill of lading or sea waybill is not conclusive evidence of the accuracy of the order, condition, quantity or weight of the goods. Therefore, in the event that a claim is brought by the shipper, the carrier is entitled to refer to other sources of evidence such as the mate's receipts to prove that such data is inaccurate. However, once a bill of lading has been transferred by the shipper to another holder, the bill of lading is considered to be conclusive evidence of the accuracy of such data and the carrier is not entitled to refer to other sources of evidence to disprove the accuracy of that data. For these reasons, it is important that the data in it is as accurate as it reasonably can be.

For example, if the bill of lading states that the quantity shipped is greater than the actual quantity shipped, then even if the ship delivers all the cargo that was actually shipped, it is still possible for a receiver to claim from the carrier the value of the cargo which was apparently short-delivered but which was not in fact ever loaded on board the ship (i.e. a 'paper shortage'). However, if the carrier is liable to the receiver for a 'paper shortage' the carrier will usually be entitled to claim an indemnity from the shippers (or charterers if they have presented the bills) since the shippers/charterers are deemed to have guaranteed the accuracy of the quantity or weight furnished by them. The merits of such an indemnity claim may be strengthened if the carrier has issued a notice of protest at the time of the release of the bill of lading.

However, where the bill of lading or sea waybill includes the words 'weight unknown' or 'quantity unknown' it has been accepted in some common law countries that the bill of lading is in fact no evidence of the quantity or weight shipped, in which case, the claimant must refer to other sources of evidence (e.g. the mate's receipt or shore tallies) to evidence the quantity or weight shipped. However, not all countries follow the same rule and in many countries the inclusion of such words does not undermine the evidential worth of the bill of lading or sea waybill.

### 3.5.1.2 Evidence of Ship<sup>56</sup>

In the majority of cases the investigation of the cause of loss or damage will include an investigation of the physical condition of the ship or other vehicle in which the goods have been carried and of the conduct of the crew or other servants of the carrier. Such investigation will necessitate inspection of records kept by the carrier. In many cases the onus is on the carrier to establish the cause of the loss or damage and to prove that he is entitled to a defence in such circumstances. Consequently, evidence relating to the ship and the conduct of the crew will be vital.<sup>57</sup>

<sup>56</sup> For a more detailed commentary see the *Gard Guidance to Masters* Chapters 2.2, 3.2 and Annex 1.

<sup>57</sup> See also Chapters 3.2.2 and 3.2.3 of the *Gard Guidance to Masters*.

It should be noted in this respect that the following documents are required to be kept on board ships by a variety of international conventions:

- Deck and engine logbooks;
- Oil record books;
- Pump-room log book;
- Tank cleaning record book;
- Loading plans;
- Stability calculations;
- Fire equipment records;
- SMS check lists.

In particular the ISM Code calls for the implementation of a safety management system (SMS) and for paper records to be kept on ship and ashore in order to audit and review compliance with the requirements of the Code, and also for the appointment of a 'designated person' who has access to the highest management of the company and who has the authority to rectify any deficiencies. For example, Articles 9 and 10 of the ISM Code provide that:

- all non-conformities are to be reported to the designated person; and that
- records of these non-conformities and of all corrective action be kept; and that
- these records and procedures be audited.

If such records are not kept this is in itself likely to be seen to be evidence of a failure by the company to exercise due diligence.

Similarly, employers need to keep personnel records relating to the qualifications and periodic assessments of the crew and other servants or agents.

Whilst road and rail carriers may not be subject to similar formal requirements, they do nevertheless need to keep such records to prove that they have exercised the necessary degree of due diligence.

### 3.5.2 Cargo Source Evidence

Most international sales of cargo will require the seller to produce a number of documents relating to the quantity, quality and provenance of the cargo. Such documents are normally produced by independent cargo inspectors and include *inter alia*:

- Certificates of Quality;
- Certificates of Origin;
- Certificates of Quantity or Weight.

It is also common to take samples of bulk cargo before, during and after loading and for sampling certificates to be provided evidencing the sampling and the sealing of the samples. This is particularly important in the liquid bulk trade since it is not uncommon for it to be alleged that vegetable, chemical and petroleum products are 'off-specification' at the time of discharge in which case it will be necessary to identify the cause of the problem. For example, the flash point specification of a gasoil cargo may be affected by events either in the shore terminal or on the ship. Therefore, samples should be taken by the crew at the ship's manifold both at the time of loading and at the time of discharge since it could well be difficult otherwise to challenge any pre-loading samples that may have been taken by the cargo owners showing the cargo to be 'on-spec.'

Samples should always be properly taken, sealed and retained by the vessel and should not be disposed of until it is clear that they are no longer required. In this connection it should be appreciated that cargo claims may take a year or even longer to materialise.

### 3.5.3 Survey Evidence

The documents and records to which reference is made in Chapters 3.5.2 and 3.5.3 relate to the condition, quantity etc., of the goods on shipment. However, in the event that loss or damage is caused by a subsequent event, evidence is also needed to prove the nature, cause and extent of the loss or damage. It may therefore be necessary to appoint surveyors, naval architects, cargo quality inspectors, accountants or other experts to comment on these matters since it must be assumed that each and every fact or assertion may need to be proved if the claim or defence is to succeed.

### 3.5.4 The Disclosure of Evidence

The laws of most countries require parties to any litigation to make available all documents and records that may be relevant to the dispute. The degree to which disclosure must be made varies between countries and therefore, guidance must be sought in each case from legal advisers in the country where the claim is being litigated.

Although parties are normally reluctant to disclose evidence which is detrimental to their case the laws of many countries require such documents to be disclosed together with any documents which support the claim. For example, the Rules of the Supreme Court (RSC) of the UK require a litigant to disclose *inter alia*:

- “(a) the documents on which he relies; and
- (b) the documents which –
  - (i) adversely affect his own case;
  - (ii) adversely affect another party’s case; or
  - (iii) support another party’s case.”

However, an exception may be made in the case of survey reports and other documents which have been commissioned by or on behalf of the legal advisers of the party in question and which are intended to assist those legal advisers to prosecute or defend the claim. Such documents may be subject to legal privilege and need not be disclosed. Therefore, survey reports which have been commissioned by or on behalf of lawyers after a claim has been made will usually fall within this category, but all other documents, survey reports, samples and records which are made in the course of normal carriage and trading, and not for the purpose of prosecuting or defending a claim, must be disclosed.

The laws of most countries enable the court or arbitration tribunal dealing with the claim to make orders demanding the production of samples and witnesses if this is necessary to consider the merits of the claim. If necessary, a witness can be compelled to attend by subpoena and any failure to attend constitutes a contempt of court which is punishable by a fine or even imprisonment in serious cases.

### 3.6 Law and Jurisdiction<sup>58</sup>

If the claim is compulsorily subject to the Hamburg Rules then those Rules provide the claimant with the option of bringing the claim in one of five different countries including the country where the cargo has been discharged. The claimant has an unfettered choice between the five locations even if the bill of lading purports to impose an exclusive jurisdiction clause. Therefore, such a choice provides the claimant with a valuable litigation advantage and this advantage is maintained under the Rotterdam Rules, if and when these Rules come into force, provided that the law and jurisdiction provisions of the Rules are ratified by the relevant country.

The Hague and the Hague-Visby Rules have no provisions relating to jurisdiction, but those Rules are applied by a substantial number of seaboard countries around the world. Nevertheless, the governing law and jurisdiction provisions of the contract of carriage are very important since these conventions are not implemented in a uniform manner in all countries. Therefore, the governing law and jurisdiction can have a major influence on the merits of the cargo claim.

It must also be appreciated that even though a contract of carriage may have an express law and jurisdiction clause, the law of many countries may allow the courts of those countries to retain jurisdiction even in the face of a contradictory jurisdiction clause. Furthermore, the laws of most seaboard countries allow the arrest of ships that are within the territorial limits of those countries for the purposes of obtaining security. Therefore, a ship may be arrested in country A for security in respect of a claim which is to be litigated in country B. If security is provided the courts of country A may then stay further proceedings in that country to allow the merits of the claim to be adjudicated in country B.

### 3.7 Insurance<sup>59</sup>

A cargo claimant is likely in the first instance to make a claim under the relevant cargo insurance. In the majority of cases, the cargo insurance is likely to provide cover for physical loss of and/or damage to the cargo (but not for losses caused solely by the delay of the cargo) and for cargo's proportion of salvage or general average, in which case the cargo insurers will be subrogated to whatever rights the assured has to bring a claim in contract or in tort against the carrier or the party that has caused the loss or damage. Therefore, in the majority of cases, the claim against

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<sup>58</sup> For more detailed commentary on jurisdictional issues see Chapter 19 (Law and Jurisdiction).

<sup>59</sup> For more detailed commentary on the relevant insurance issues see Chapter 25 (The Fundamental Principles of Marine Insurance), Chapter 26 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34).

the carrier or the party that has caused the loss or damage will be brought by cargo insurers. Depending on the country where the claim is brought such claim may be brought either in the insurers' own name or in the name of the assured.

Normally, the liability of the carrier or the party that has caused the loss or damage will be covered by the standard P&I cover provided on a mutual basis by the International Group P&I clubs or by other market insurers on a fixed premium basis. However, in both cases, cover is subject to many detailed exclusions. For example, the clubs do not provide standard P&I cover for liabilities arising as a result of the delivery of the cargo without surrender of the original bills of lading and cover for claims arising under *ad valorem* bills of lading is limited to a sum of USD 2,500 per unit, package or piece. Furthermore, since it is perceived that the carrier may incur more liability under the Hamburg Rules or Rotterdam Rules than under the Hague or Hague-Visby Rules, the member clubs of the International Group of P&I Clubs provide cover for liabilities arising under the Hamburg Rules or Rotterdam Rules where such Rules apply compulsorily but not where the Rules are voluntarily adopted by the carrier. Therefore, it is important that shipowners have a firm grasp of the extent of cover that is available in such circumstances. In the event of an actual or suspected claim, the shipowners should notify their liability insurers promptly and should work closely with them to defend the claim. Any failure to do so may prejudice the shipowners' right to be indemnified by their insurers for any sums that they may be obliged to pay to the cargo claimant in due course.

It must be appreciated that a cargo claimant is not normally entitled to bring a claim directly against a liability insurer. The cover provided by the member clubs of the International Group of P&I Clubs is on a 'pay to be paid' basis, i.e. the shipowner must pay the claim first and then seek indemnification from the club. It must also be appreciated that, even if cover is available, the club is not obliged to offer security to prevent the arrest of a ship or to release a ship from arrest. If the club were to exercise its discretion to provide such security it would do so purely as a service to its member and subject to terms to be agreed.

### 3.8 Case Study

A vessel loaded a full cargo of sugar beet pellets in Poland for Norway. Some hours after arriving in Norway the duty officer noticed a burning smell emanating from a ventilator to one of the holds. Although there was no smoke the local fire brigade was called in. After opening the hatch it was discovered that a powerful hold light had been inadvertently switched on which, due to its proximity to the cargo had resulted in the cargo smouldering. The fire was extinguished but the cargo receivers claimed that the whole cargo was smoke-damaged and refused to take delivery. The vessel was then discharged in Rotterdam at significant expense to the carriers. Additionally, a cargo claim for USD 130,000 was filed by cargo underwriters who had settled the claim that had been brought under the cargo policy by the receivers. The master of the vessel stated that the subject hold light had been accidentally switched on by a crew member who had been requested to only switch on the deck lights. The case was finally settled for USD 30,000.

Four problems normally arise in a case such as this:

- 1 Do the claimants have the right to sue the carrier?
  - 2 Was the damage caused by the stated event?
  - 3 Are the carriers liable in the circumstances?
  - 4 Do the carriers have insurance cover for the cargo claim and for the extra costs of disposing of the cargo?
- 
- 1 It is likely that the cargo underwriters are entitled to bring the claim since, once they have settled the claim under the cargo policy (which will normally provide cover for fortuitous damage such as this), they are subrogated to the rights of the assured including the right of the assured to bring a claim against the carrier under the bill of lading. Depending on the jurisdiction where the claim is brought, the cargo insurers may either sue in their own name or in the name of the assured.
  - 2 It is very important to establish the precise cause of the damage. Therefore, the carriers need to ensure that they have established a satisfactory system on the vessel to identify and record incidents and deficiencies and to report any problems promptly to shore management. Shore management also need to ensure that they notify their liability insurers (normally their P&I club) promptly of the incident since a failure to do so may not only hamper the carrier's defence but may also prejudice his club cover since the club may wish to instruct surveyors and lawyers at an early stage to gather evidence and protect the carrier's interest. Whilst the cause of the cargo damage is reasonably clear in this case study, that is not always so; fire can be caused by many different events including the spontaneous combustion of the cargo itself. Therefore, it may be necessary to appoint a fire expert to attend on board to make a forensic examination.

Unless the cause of the incident can be identified it is normally impossible for the carrier to avoid liability since there is normally a presumption that if the cargo has been loaded in good condition, any damage that is discovered on discharge has been caused by default on the part of the carrier. However, if the cause of the incident has been ascertained, that may enable the carrier to rely on whatever defences that are available under the contract.

- 3** Most cargo claims are brought under contracts that are subject either compulsorily or by agreement to the Hague or Hague-Visby Rules. Article IV Rule 2 (a) of the Rules provides that the carrier is not liable for *“loss or damage arising or resulting from ... act, neglect or default of the master, mariner ... or the servants of the carrier in the ... management of the ship.”* If the cargo has indeed, been damaged by the act of the crew member in inadvertently switching on the hold light, then, on the face of it, that should provide the carrier with a defence since the negligence was directed to the ship’s equipment which is not designed for the care of the cargo rather than to equipment which is designed to care for and protect the cargo. (In the latter event, the carrier would be liable for breach of his duties under Article III Rule 2 of the Rules.)

However, it is important to establish that the relevant crew member is properly qualified, competent and properly trained since, if not, the cargo claimant may be able to argue that the carrier has not satisfied his obligation under Article III Rule 1 of the Rules to *“exercise due diligence to ... properly man ... the ship”* and that this was causative of the damage, thereby depriving the carrier of a defence. Similarly, if it is established that the light was switched on before the end of loading and left on thereafter, this may again lead to the conclusion that the carrier has not exercised due diligence *“before and at the beginning of the voyage ... to make the ship seaworthy”* which will again deprive the carrier of his defence.

- 4** If the carrier is found liable, or if the settlement that is reached with the cargo claimants has been approved by the carrier’s P&I club on the basis that it is a sensible compromise of a potential legal liability, the carrier is likely to be able to recover the amount paid to the cargo claimants under his P&I cover. Similarly, the carrier is likely to recover the additional costs of disposing of the cargo that has been rejected by the cargo receivers under his P&I cover.

For more examples of relevant case studies, see Chapter 21 of the *Gard Handbook on P&I Insurance*, 5th edition.



## Chapter 4

# Charterparty Claims<sup>1</sup>

### 4.1 Introduction

Ships are generally used by parties other than shipowners in order to perform commercial contracts that they have entered into with third parties. Typically, a seller or buyer of goods may need the use of a vessel in order to satisfy the terms of the international contract of sale. Such contracts will necessarily be negotiated some time before the goods are actually loaded on to the ship and may be supplemented in due course by other documents which record the fact that the goods have subsequently been shipped. Therefore, there are generally two different types of relevant contracts:

- 1 contracts for the use of the whole (or, at least, a substantial part) of the ship, i.e. charterparties; and
- 2 contracts evidencing the shipment of cargo and recording the terms under which the cargo is to be carried, i.e. bills of lading or sea waybills.

In the case of bulk cargoes it will generally be necessary to have both types of contracts as the size of the cargo will necessitate the use of the whole or, at least, a substantial part, of the ship. However, since the charterparty does not evidence the actual shipment of the cargo it will also be necessary to issue a bill of lading or sea waybill when the cargo is subsequently shipped. On the other hand, if the cargo is a small consignment, then there may be no need for a charterparty and the goods can be carried simply under a bill of lading or sea waybill.

A fundamental difference between the two types of contract is that a charterparty is not normally transferable whereas the most common form of contract evidencing the shipment of the cargo (i.e. a bill of lading) is transferable. Therefore, the charterparty does not normally play any major role in relation to the trading of the cargo whereas

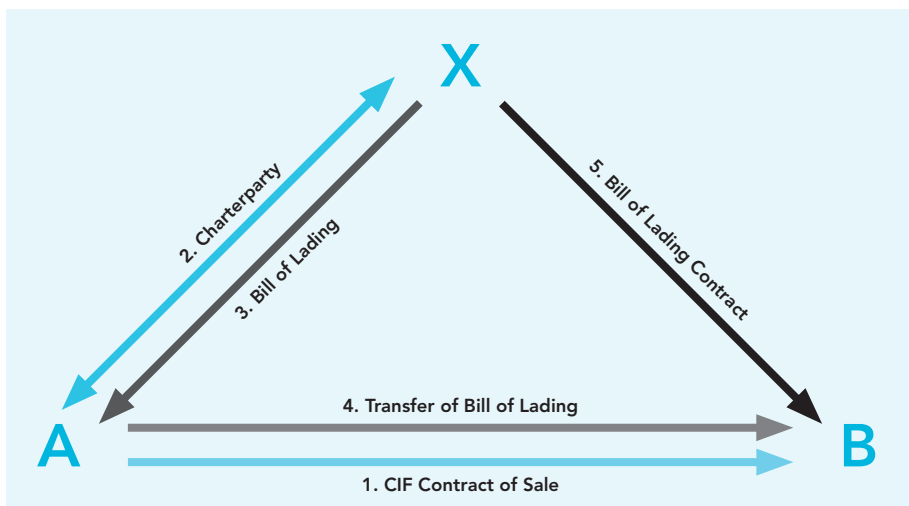
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<sup>1</sup> See also Chapter 18 of the *Gard Handbook on P&I Insurance*, 5th edition. Further commentary on cargo claims arising under charterparties can be found in Chapter 3 (Cargo Claims).

a bill of lading has a major role to play in that regard since, by transferring the contract from seller to buyer, the right to take possession of the cargo from the ship is thereby transferred from seller to buyer. Indeed, the bill of lading contract may be transferred a number of times during the course of the voyage depending upon how often the cargo has been sold. However, the charterparty will continue to govern the relationship between the shipowner and the charterer notwithstanding the transfer of the bill of lading.

### Example

A sells 5,000 tons of cement to B on CIF terms (contract 1). This means that as between the seller and the buyer it is the duty of the seller to arrange and provide the transportation of the cargo from A to B. Given the size of the cargo, A will need to charter a vessel since this will give him the right to utilise the carrying capacity of the vessel as he may require. Therefore, a charterparty is concluded between A as charterer and X as shipowner (contract 2). In due course the cargo is loaded on to the vessel and a bill of lading is issued evidencing the shipment. Since A is the shipper of the cargo the bill of lading will initially evidence a contract between X as carrier and A as shipper (contract 3). However, in order to satisfy the terms of the sale contract, A will subsequently transfer the bill of lading to B (contract 4) at which point all rights that A originally had under the bill of lading are transferred to B and the bill of lading now evidences a contract between X and B (contract 5). However, notwithstanding the transfer of the bill of lading, the charterparty contract between A and X still remains in full force and A and X continue to be subject to the rights and obligations contained in the charterparty contract. It therefore follows that X may in due course be a party to two quite separate contracts on different terms with two quite different parties, i.e. the charterparty contract with A and the bill of lading contract with B.



Another important difference between charterparties and contracts evidencing the shipment of cargo such as bills of lading is that, whereas the terms of bills of lading are heavily regulated by international conventions such as the Hague, Hague-Visby or Hamburg Rules,<sup>2</sup> charterparties are not subject to any such regulation. In other words, in the case of charterparties, the principle of freedom of contract applies.

**NB!** Where issues arise in relation to the carriage of goods, particularly when the goods are lost or damaged, it is normally necessary to consider the rights of the parties under both the charterparty and the bill of lading or other contract of carriage as the two contracts are closely inter-linked. However, in this chapter, consideration is given purely to issues which arise under the charterparty.<sup>3</sup>

## 4.2 Types of Charterparties<sup>4</sup>

There are two basic types of charterparty:

- 1 A bareboat (or demise) charter, i.e. a contract which give the charterer full control of the ship for an agreed period in exchange for the payment of hire. The contract is similar to a time charter (see below) but with the important difference that it obliges the charterer to provide his own crew and to incur responsibility as 'owner' for liabilities arising during the operation of the ship; and
- 2 other forms of charter, i.e. contracts which oblige the owner of the ship to provide the crew and to remain responsible as 'owner' for liabilities arising during the operation of the ship.

A useful analogy is the distinction that can be drawn between the hire of a car from a hire car company when the hirer is given the use of the vehicle but has to drive it himself and the hire of a taxi when the hirer is given the use of the vehicle and the driver. A bareboat charter is the equivalent of the contract with the hire car company whereas other charters are the equivalent of the contract with the owner of the taxi.

### 4.2.1 Bareboat Charterparties<sup>5</sup>

It is normally the bareboat charterer who is responsible for the maintenance and insurance of the ship during the charter period and for operating costs such as crewing, bunkering, port costs etc.

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2 The Rotterdam Rules are not in force at the time of going to print but may come into force in due course.

3 A consideration of the issue that arise under bills of lading, sea waybills etc. can be found in Chapter 3 (Cargo Claims).

4 See Chapter 18.2 of the *Gard Handbook on P&I Insurance*, 5th edition, 2002 and paras 2.31-2.34 of *Bills of Lading* by Aikens, Lord and Bools. Informa 2006.

5 For more detailed commentary see *Bareboat Charters* by Mark Davis, Informa, 2nd edition 2005.

Since the master and crew members are employees not of the shipowner but of the bareboat charterer it is the bareboat charterer who is responsible for the acts, neglect or omissions of the crew. Therefore, in general terms, it is the bareboat charterer rather than the shipowner who will be liable for claims arising out of the operation of the vessel. For example, it is the bareboat charterer rather than the shipowner who is responsible for collisions and other tortious acts committed by the crew. Similarly, bills of lading signed by the master will normally make the bareboat charterer and not the shipowner liable as carrier under those contracts.

Bareboat charters are created not so much with a view to the carriage of goods but more as part of a complicated financing arrangement, often with the intention that the charterer should become the owner of the ship in due course. Thus, a contract for the purchase of a ship by instalments will often incorporate a bareboat charter into the contract. A variant of this would be for investors to lend the funds required to buy the ship, the bank then acquiring the ownership of the ship, but bareboat chartering it to the borrower for the period of the loan. In this way the bank can obtain the necessary security but is able at the same time to avoid not only the operating costs but also the liabilities which it would otherwise have to bear in relation to the operation of the ship under a mortgage. Bareboat charters are also concluded between two associated companies for tax or employment reasons.

#### **4.2.2 Charterparties other than Bareboat Charterparties**

Such charters normally fall into one of two basic categories:

- 1** Time charters, i.e. contracts for the use of the ship and her crew for a specified period of time within agreed trading limits as directed by the time charterer in consideration for the payment of hire; and
- 2** Voyage charters, i.e. contracts for the use of the ship and her crew to carry an agreed cargo on an agreed voyage regardless of time in consideration for the payment of freight (and, possibly, other remuneration such as demurrage if the loading/discharging is delayed beyond the time agreed for such operations.)

However, it is becoming increasingly common to see charters which combine some of the aspects of both time and voyage charters. The following are examples:

- trip charters, i.e. contracts obliging the charterer to pay *hire* for the time taken by the ship to complete a specified voyage, e.g. a 'round Atlantic' voyage; or
- consecutive voyage charters, e.g. four consecutive voyages between A and B within a specified period; or

- slot charters or ‘space sharing agreements’, i.e. agreements which enable liner operators to utilise empty space on their ships by allowing other operators to use some of the (empty) carrying capacity in their vessels in exchange for the right to use an equivalent amount of space on the ships of such other operators. This form of arrangement is common in the container trade and remuneration is a complicated equation often calculated with regard to the net profit earned over a period by all the operators who are part of the arrangement.

### 4.2.3 Basic Differences between Time<sup>6</sup> and Voyage<sup>7</sup> Charterparties

Although it is important to appreciate that the terms of a particular charterparty may make fundamental changes to the customary rights and obligations of shipowners and charterers, time and voyage charterparties normally have the following differences:

- Under a voyage charter the shipowner is normally obliged, in consideration for the payment of the freight by the charterer, to pay for all the operating costs of the ship. However, under a time charter the cost allocation is more balanced – whereas the shipowner pays for the crew and the cost of insuring the ship, the charterer normally pays for bunkers, port and stevedoring costs, agencies, pilotages and ‘all other usual expenses’.
- Since a voyage charter is a contract for a particular voyage most of the relevant factors (e.g. the freight, cargo, loading and discharging ports etc.) will have already been agreed during the pre-fixture negotiations and become terms of the contract. Consequently, there is limited need for the voyage charterer to play an active part in the subsequent operation of the vessel when performing the charter. However, a time charter is a contract which gives the charterer the ability to control the commercial operation of the vessel during the duration of the charter. Therefore, the parties will not normally have agreed in advance where the vessel is to trade and which cargoes she will carry during the charter period. Consequently, the time charterer will normally play an active role in the operation of the vessel during the charter period as it will be necessary for the charterer to give orders and directions to the ship and crew as to how and where the vessel is to trade.
- The nature of a time charter is that the shipowner receives remuneration (hire) in return for making the ship available to the time charterer for an agreed period of time. Therefore, so long as the ship is made available, the shipowner is entitled to receive the hire even if no cargo is in fact carried. Consequently, the commercial risk of finding the necessary cargoes in order to make the venture profitable is

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<sup>6</sup> For more detailed commentary see *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

<sup>7</sup> For more detailed commentary see *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007.

borne by the time charterer not the shipowner. However, in the case of a voyage charter, the shipowner receives remuneration (freight) for the carriage of goods on an agreed voyage. Therefore, unless cargo is carried, the shipowner receives no remuneration. Consequently, in the case of a voyage charter, the commercial risk of finding the cargoes to carry in order to gain remuneration is borne by the shipowner and not the charterer.

- Under a time charter, hire is paid continuously, in full and in advance provided that the ship is made available for use by the shipowners. Therefore, if the contractually agreed performance of the ship is delayed or prevented by events which cannot be attributed to the shipowners' fault or to an agreed off-hire clause (e.g. heavy weather, port strikes etc.), hire continues to be payable. Consequently, the risk of delay in time charters usually falls on the time charterer. However, in the case of a voyage charter, the freight that the shipowner receives is not calculated according to time but is a fixed agreed amount for carrying goods from an agreed loadport to an agreed discharge port. Therefore, if the voyage takes longer than originally estimated by events which cannot be attributed to the charterers' fault the shipowner does not receive additional freight but is nevertheless obliged to bear any extra voyage costs which may be incurred as a result of the delay. Consequently, the risk of delay in voyage charters falls predominantly on the shipowner.

### **4.3 The Terms of the Charterparty**

It is not possible to comment in detail on the importance that is attached to different terms under different systems of law. However, it is important to appreciate that, depending on the governing law, the breach of different terms can provide the innocent party with different remedies.<sup>8</sup> Therefore, legal advice should always be sought before any attempt is made to terminate a contract.

There are very many printed forms of time and voyage charters which reflect the intended trade of the vessel. Some forms (such as the *Baltimex* and *Gencon* forms) are intended for general non-specific trading whilst other forms (such as the *Asbatankvoy*, *CoalOrevoy*, *Sugarcharter*, *BPTIME 3* and *ShellLNGTime* forms) are intended for the carriage of specific cargoes. The meaning of particular terms is often affected by such factors. For example, the question of what constitutes a seaworthy ship for the purposes of 'ordinary cargo service' will often be different to what constitutes a seaworthy ship for the purposes of the carriage of refrigerated products.

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<sup>8</sup> For more detailed commentary see Chapter 23 (Remedies).

Furthermore, whilst these printed forms are frequently used, parties will often supplement these forms with a large number of 'special' clauses which in many instances include a trader's standard terms. Since such 'special' clauses are usually considered to represent the parties' true intentions whilst the printed terms are merely terms of a contract which the parties have chosen to use as a general framework, the law of most countries will afford more weight to the 'special' clauses than to the printed terms of the standard contract. Therefore, if there is a conflict between the printed terms and the 'special' clauses, the latter will normally prevail.

Furthermore, it must not be assumed that the only relevant terms are those which are expressly stated in the contract. Even when the charter is silent on a particular issue, the law may imply a term if it is necessary to do so to give business efficacy to the contract. Common examples include the following:

- The ship must be seaworthy;
- The ship must proceed with reasonable dispatch;
- The charterer will not ship dangerous cargo;
- The charterer will not nominate unsafe ports or places.

Subject to the fact that rights and obligations may be varied by the particular terms of the charterparty, the various rights and duties that are normally imposed on parties to charterparties (whether time or voyage) can be summarised as follows.

- a** The shipowners have the duty:
- to provide a seaworthy ship which complies with the charterparty description;
  - to properly and carefully load, handle, stow, carry, keep, care for, discharge and deliver the cargo;
  - to comply with charterers' legitimate employment instructions;
  - to prosecute voyages with reasonable dispatch.
- b** The charterers have the duty:
- to pay remuneration to the shipowner;
  - to give legitimate employment instructions;
  - to ensure that dangerous goods are not loaded without giving notice;
  - to ensure that the vessel is directed by them only to safe ports;
  - to perform their duties without delay.

The law recognises that performance cannot always be perfect. Therefore, unless the contract provides otherwise, if a breach is 'so trivial as to be negligible' according to the opinions and expectations of reasonable men engaged in that type of trade, there will not be considered to be an actionable breach at law. Furthermore, parties often provide expressly that strict reliance on a particular term will be softened by addition of the word 'about', e.g. "the vessel will load 'about' 2,600 tons".

The question of what degree of flexibility is given by use of the word 'about' is a question of fact in each case but it is doubtful that an allowance of more than five per cent more or less would be contemplated.

In recent years, parties have also started to modify terms of description by adding the phrase 'without guarantee', e.g. 'a time charter trip of three months without guarantee'. The use of such a phrase has been held to substantially dilute the effect of the estimate, and the party making the estimate is liable only if it can be proved that the estimate was not given in good faith, i.e. it does not seem to be necessary for that party to prove in addition that the estimate was given on reasonable grounds.

## 4.4 The Shipowner's Duties

### 4.4.1 The Shipowner's Duty to provide a Seaworthy Ship<sup>9</sup>

The charterparty will normally describe the ship in some detail and will go on to provide that the ship is to be seaworthy' or 'tight, staunch, and strong and in every way fitted for the voyage' or words to similar effect. Such words constitute an express promise of the vessel's seaworthiness. However, even if the charter does not include such words, it is in any event normally an implied term that the ship will be seaworthy for the contemplated employment.

#### 4.4.1.1 What is Seaworthiness?

'Seaworthiness' means that the ship, her equipment and crew must be fit to withstand the perils which can foreseeably be encountered on the contemplated voyage. The classic test is the following:

*"The ship must have that degree of fitness which an ordinary careful owner would require his vessel to have at the commencement of her voyage having regard to all the probable circumstances of it. Would a prudent owner have required that it (the defect) should be made good before sending his ship to sea, had he known of it?"*<sup>10</sup>

If the answer is 'Yes' then the vessel is unseaworthy.

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<sup>9</sup> For a more detailed commentary see Chapters 21.24 to 21.25 of the *Gard Handbook on P&I Insurance*, Chapters 11.18 to 11.41 and 85.91 to 85.107 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2005, Chapters 8.7 to 8.74 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008 and paras 10.82 to 10.133 of *Bills of Lading* by Aikens, Lord and Bools, Informa 2006.

<sup>10</sup> See *Mc Fadden v Blue Star Line*, [1905] 1 KB 697 at 706.



The standard of seaworthiness required depends upon the nature and age of the ship, the kind of voyage envisaged, the nature of the cargo and a host of other factors. The most obvious instances of unseaworthiness are where the vessel has some physical defect or inadequate or insufficient equipment. However, unseaworthiness is a broader concept and includes the following:

- The absence of updated charts for the voyage;
- An incompetent crew;
- A crew which is insufficiently instructed or insufficient in numbers;
- Insufficient bunkers for the voyage;
- The absence of the legal documents that may be required for the satisfactory prosecution of the contemplated voyage, e.g. SMS and ISPS compliance certificates.

The vessel may also be unseaworthy if her holds or tanks are not reasonably fit and safe for the reception, carriage and preservation of the contemplated cargo on the contemplated voyage.

At common law, the carrier is under a strict duty to provide a seaworthy ship and is in breach if the ship is not seaworthy even if the defect is a latent defect which it is not possible to discover. However, in the majority of cases, the charterparty will incorporate either the Hague or Hague-Visby Rules by agreement. Such Rules specify that such strict liability is replaced by a duty on the part of the carrier to “exercise due diligence” before and at the beginning of the voyage to make the ship seaworthy. Although such wording suggests a lesser degree of responsibility the duty to exercise due diligence is strictly construed and any negligence on the part of any of the servants, agents and even independent contractors acting for the carrier is likely to constitute a breach of that duty.

#### **4.4.1.2 When is Seaworthiness Relevant?**

Whilst the issue of seaworthiness is generally relevant in order to determine the cause of any particular incident, the issue may also arise in a secondary context if the ship has suffered a breakdown during the charter. The issue which then arises is whether the shipowner has a continuing duty to repair the vessel in order to perform the charterparty.

When there is no express seaworthiness obligation in the charter the implied duty placed on the carrier obliges him to provide a vessel which is merely seaworthy at the commencement of the voyage. However, if the contract contains an express clause obliging the carrier to provide a seaworthy ship then the relevant time will depend upon the construction of that particular clause. It may be:

- the date of the charter; or
- the time of delivery into service under the charter; or
- the commencement of loading; or
- throughout the charter.

If the duty is to provide a ship that is seaworthy at the date of the charter or at the date of delivery into the charter or at the commencement of loading, then this will not normally impose any further duty on the shipowner to repair the vessel if she subsequently becomes unseaworthy as a result of an incident which occurs during the voyage. However, if the duty is to maintain the ship in a seaworthy condition throughout the charter then the shipowner has the duty to take whatever steps that are reasonably necessary to repair the ship within a reasonable time. Indeed, some charterparties contain a guarantee that the vessel will continue to be maintained in the same condition as on delivery and will remain fully in class and able to carry all permissible cargoes.

#### **4.4.2 The Shipowner's Duty to properly and carefully load, handle, stow, carry, keep, care for, discharge and deliver the Cargo**

A detailed commentary on these issues can be found in Chapter 3 (Cargo Claims).

#### **4.4.3 The Shipowner's Duty to prosecute Voyages with reasonable Dispatch**

The shipowner's duty to prosecute voyages with reasonable dispatch is important both for time and voyage charterers. It is important for time charterers since they are obliged to pay hire continuously and therefore, the longer that it takes to perform voyages the more hire the time charterers have to pay. Similarly, it is normally important to voyage charterers since the underlying cargo sale contract may require prompt carriage and delivery and may impose penalties if carriage is delayed. Therefore, the warranted speed of the ship is a factor that influences the financial worth of the vessel to the charterers and the amount of remuneration that they are prepared to pay the shipowners.

#### 4.4.3.1 Time Charterparties

In the case of time charters, the shipowner generally has the duty throughout the charter period to perform the commercial services required by the time charterers promptly and to “*prosecute his voyages with the utmost dispatch*”. Therefore, if the shipowner or the master fails without good and sufficient reason to comply with legitimate employment instructions given by the time charterer, the charterers may have the following remedies:

- They may place the vessel off-hire;<sup>11</sup> and/or
- They may claim damages for losses incurred by them as a result of such delay.

##### 4.4.3.1.1 Claims for Damages for failure to prosecute Voyages with dispatch<sup>12</sup>

Even if the vessel is not off-hire, the time charterer may nevertheless be entitled to bring a claim for damages against the shipowner for the value of the hire which has been paid in advance but which has not been earned and for any other losses which he has incurred as a result of the failure of the vessel to “*prosecute ... voyages with the utmost dispatch*.” For example, in one case charterers directed a master to proceed from the Pacific North West of North America to northern China. The charterers wished the master to take the quickest route which was the Great Circle route. However, the master proceeded by the more southerly – and longer – Rhumb Line route since he believed (unreasonably) that the Great Circle route was more dangerous. It was held that the master had not prosecuted his voyages with the utmost dispatch.

The precise wording of charters may differ in this respect. Some charters use the phrase ‘utmost dispatch’, some the phrase ‘due dispatch’ and some the phrase ‘reasonable dispatch’. However, the words normally have the same meaning – the ship is not obliged to proceed at top speed in all circumstances but as quickly as sea, weather, political etc., conditions safely allow.

If the vessel does not proceed with the utmost dispatch, the time charterers are entitled to claim damages for the losses that they have incurred as a result. Such losses will normally include the additional hire or bunkers that the charterers have been obliged to pay because of the delay.

In most cases, if the time charterers are not satisfied with the performance of the vessel then claims are submitted on a number of grounds including off-hire, failure to proceed with due dispatch and breach of description.

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<sup>11</sup> Commentary on off-hire may be found in Chapter 4.5.1.1.2 below.

<sup>12</sup> See Chapter 18 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

#### 4.4.3.1.2 Claims for Damages for breach of Description<sup>13</sup>

Most time charters have provisions which describe the speed and fuel consumption of the vessel. For example:

*"Vessel when fully loaded capable of steaming about 14.5 knots in good weather and smooth water on a consumption of about 38 tons of oil fuel."*

Therefore, if the performance of the vessel appears to fall short of such description, claims for damages may be brought by the charterers for losses suffered by them as a result. The calculation of the damages which the charterer is entitled to claim as a result of a breach by the owners of the vessel's performance obligations is notoriously complicated. The basic approach is to make a comparison between the performance (both in terms of speed and consumption of bunkers) which the vessel should have achieved in the weather conditions which she encountered and the performance which she actually achieved and the extra cost is then deducted from the hire calculation. However, some charters provide that the comparison is to be made at the end of each voyage whereas others require a calculation at the end of the charter or at the end of specific periods (e.g. every six months).

#### 4.4.3.2 Voyage Charterparties

In the case of voyage charters, the shipowner normally has the duty to proceed with reasonable dispatch in relation to two separate stages of the charter, i.e. in relation to the:

- Approach voyage to the loading port; and
- The laden voyage to the discharge port.

##### 4.4.3.2.1 The approach Voyage to the loading Port<sup>14</sup>

It is rare for a vessel to be 'ready to load' at the loading port at the time that a voyage charter is fixed. More usually the vessel will need to undertake a preliminary voyage in order to reach the load port. However, the charterers may, nevertheless, face some deadline for loading the cargo under the terms of a sale contract. It is, therefore, usual for voyage charters to include a cancelling clause which provides that if the vessel is not ready to load at the agreed location by an agreed time and date, then the charterer shall have the option of cancelling the charterparty. Such clauses are strictly construed. If the ship is not ready to load by the cancelling time and date, then the charterers are entitled to cancel the charter irrespective of the cause of the delayed arrival and irrespective of whether the delay is outside the control of the shipowner, e.g. delay caused by heavy weather en route to the load port.

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<sup>13</sup> See Chapter 3 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

<sup>14</sup> See Chapter 4 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2005.

However, the charterers may also have incurred losses as a result of the delayed arrival (e.g. extra cargo storage charges) and may wish to claim such losses from the shipowners. Whilst the fact that the ship has not arrived before the agreed cancelling time and date may entitle the charterers to cancel the charter, that does not of itself entitle them to claim damages from the shipowner since the reason for the delay may not be attributable to default on the part of the shipowners. Therefore, in order to substantiate a claim for damages the charterers must establish that the delayed arrival has been caused by a breach by the shipowners of one of the following terms of the charter:

- The duty to provide an 'estimated ready to load' date in good faith and on reasonable grounds during the fixture negotiations; and/or
- The duty to proceed to the load port with due dispatch.

#### 4.4.3.2.2 *The laden Voyage to the discharge Port*<sup>15</sup>

If the carrier intentionally proceeds to the discharge port other than by the usual and customary route or without reasonable dispatch then he may be committing a deviation. Traditionally, deviation has had a dramatic impact on the rights and defences that are available to a carrier of goods. In a nutshell, the carrier may lose the right to rely on any exception clauses in the contract and may consequently lose the benefit of his P&I cover for any liabilities that arise as a result of the deviation.<sup>16</sup>

## 4.5 The Charterer's Duties

### 4.5.1 The Charterer's Duty to pay Remuneration to the Shipowner

Cash flow is vital to enable a shipowner to maintain good service under a charterparty. Accordingly, the laws of most countries protect the rights of shipowners to receive remuneration in full without deduction unless the terms of the charter or public policy dictate otherwise. Such principles apply to both time and voyage charters.

#### 4.5.1.1 The Duty to Pay Hire under Time Charterparties<sup>17</sup>

Time charters invariably provide that hire is payable:

- Continuously;
- In full; and
- In advance.

<sup>15</sup> See Chapter 12 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2005 and paras 10.264 to 10.284 of *Bills of Lading* by Aikens, Lord and Bools, Informa 2006.

<sup>16</sup> Further commentary can be found in the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 xi (Cargo Liability)).

<sup>17</sup> See Chapter 16 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

In some cases the charter will provide expressly that deductions can be made from hire. The most common examples are the following two:

#### **4.5.1.1.1 Cash Advances to the Master**

Most time charters provide that if the charterers have made cash advancements to the master or paid on behalf of the shipowners for disbursements which are strictly for shipowners' account, such payments "*shall be deducted from the hire*".<sup>18</sup> Some charters provide expressly that deduction is allowed only if the charterers have provided invoices and other satisfactory evidence of the payment.

#### **4.5.1.1.2 Off-Hire<sup>19</sup>**

Since the shipowner is entitled to receive hire in advance throughout the charter period, the time charterer will normally pay in advance for services which will be provided by the ship in due course. If the contemplated service is not in fact provided by the ship in due course, the charterer will not have received the benefit of the hire that has been paid in full in advance. Therefore, the aim of off-hire is to enable the time charterer to deduct from subsequent hire payments the amount of hire that has been paid, but not earned, in the preceding period. For example, if hire is paid monthly in advance on the first day of the month, then on 1 December the charterers will be obliged to pay 31 days of hire. However, if the vessel breaks down for 15 days in December, the charterers have in effect paid in advance for 15 days on which they have received no service. Consequently, when the next hire installment falls due on 1 January, the off-hire clause may entitle the charterers to deduct from the 31 days hire that should normally have been paid on that day the 15 days of hire that they had in fact over-paid on 1 December.

It is a basic principle that hire is to be paid in full in advance and therefore, if the charterers wish to deduct hire under an off-hire clause there is a heavy onus on them to prove that they are entitled to do so. If they make such a deduction when they are not entitled to do so they run the risks that are described in Chapter 4.6.1 below.

Many off-hire clauses provide that the ship may be placed off-hire by events which are not within the control of the shipowners, e.g. grounding, fire, crew illness etc. Therefore, so long as the particular event falls within the ambit of the off-hire clause, it is not necessary for the charterers to prove that the particular event which has caused delay has been caused by a breach of contract on the part of the shipowners.

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<sup>18</sup> For example, see lines 65-66 of the NYPE 1946 form.

<sup>19</sup> For more detailed commentary see Chapter 25 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

The wording of off-hire clauses can vary dramatically from charter to charter, but a charterer would normally be entitled to place the vessel off-hire if all of the following conditions are satisfied:

- The ship has not provided the service required by the charterers;
- That failure has been caused by an event which falls clearly within the ambit of the off-hire clause;
- That failure cannot be attributed to the act or omission of the charterers themselves;
- Time has been lost as a result of such failure.

#### 4.5.1.1.3 *Equitable Set-off*

Since it is the public policy of most countries to maximise the cash income of shipowners for the reasons explained above, the scope for time charterers to make deductions from hire in circumstances where the charter does not expressly allow such right, is extremely limited. Under the common law, a time charterer cannot set-off (i.e. deduct) all cross-claims from hire but merely those cross-claims "*which go directly to impeach the plaintiff's demands*" and "*are so closely connected with his demands that it would be manifestly unjust to allow him to enforce them without taking into account the cross-claim.*"<sup>20</sup> The precise meaning of these phrases is notoriously unclear but perhaps the easiest way to understand them is to say that a cross-claim may be deducted only if it is essentially 'of the same nature' as the shipowner's claim. Therefore, a cargo claim cannot be deducted from hire since a claim for hire and a claim for cargo damage are fundamentally different in nature. However, a claim for deficient speed performance might, depending on the particular circumstances, be deductible since the claim is in essence a claim for overpaid hire and is therefore, of the same nature as the shipowner's claim for hire.

#### 4.5.1.1.4 *The Shipowner's Remedies for Non-Payment of Hire*

If the time charterers wish to stop paying hire, or to pay less than the full hire, the onus is on them to prove that they have the right to do so. If they fail to do so they run the following risks:

- Under older forms of time charter (e.g. the NYPE 1946 form) shipowners have the right to withdraw the vessel from the charterers' service and thereby terminate the charterparty irrespective of whether the failure to pay was deliberate or accidental or the result of an oversight.
- Under more modern forms of time charter (e.g. NYPE93, BPTIME 3 etc.), the shipowners may not withdraw the vessel from the charterers' service and thereby terminate the charter unless and until they have firstly given the charterers notice to rectify the failure to pay (an anti-technicality clause notice) and the charterers fail to rectify within the notice period (the grace period).

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<sup>20</sup> Per Lord Denning in *The Nanfri*, [1978] 2 Lloyd's Rep. 132 at page 140.

- Under more modern forms of time charter (e.g. NYPE93, BPTIME 3 etc.), the shipowner is also given the additional right (without prejudice to the right to withdraw the vessel), to suspend the performance of the services that the shipowner must normally provide under the time charter whilst hire remains unpaid. Such suspension of services does not terminate the charter and hire continues to accrue due whilst services are suspended. Such rights are also usually dependent on the giving of an anti-technicality clause notice before services can be suspended.
- The shipowner may exercise a lien on any sub-freights that are payable to the time charterer under a sub-charter.

However, a shipowner should ensure that he takes legal advice before adopting any of these remedies since the remedies are extremely technical in nature and courts will normally require proof that the shipowner has complied strictly with all of the necessary formalities. A failure by the shipowner to comply with such formalities may mean that the shipowner is in danger of having repudiated the charter and incurring substantial liability to the charterers.

#### **4.5.1.2 Voyage Charterparties**

##### **4.5.1.2.1 *The Duty to Pay Freight*<sup>21</sup>**

The charterers have the duty to pay freight to the shipowner for carrying the cargo from the load port to the discharge port. It is up to the parties to decide the basis upon which freight is to be charged. The basis of calculation is usually determined by the nature of the cargo and can be calculated in accordance with quantity, weight or volume but may also be determined with reference to published scales or even as a lump sum. The parties will also decide whether the calculation applies to the received or delivered weight. The latter decision is important in the case of cargoes such as crude oil or gases which lose weight naturally during the course of the voyage.

The following are common examples:

- Freight on delivered quantity, e.g. '£3 per ton, net weight delivered.'
- Freight on received quantity, e.g. '£3 per ton computed on received quantity.'
- Lump sum freight, e.g. 'freight to be £11,250 lump sum.'
- Published scales of freight, e.g. 'Worldscale' or 'Intascale'.

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<sup>21</sup> See Chapter 13 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2005.



If the freight is calculated in accordance with the quantity or weight of the cargo that is to be shipped but the charterer does not provide the vessel with the total quantity of agreed cargo, the owner will lose the ability to earn freight on the quantity short-shipped. He will, therefore, be entitled to claim such loss (called 'deadfreight') either as damages or sometimes as a result of an express clause in the charter.

#### 4.5.1.2.1.1 *When is Freight Earned?*

Unless the charter provides otherwise, no freight is earned unless and until the goods are delivered at the port of discharge. Therefore, if the vessel performs 95 per cent of the voyage but then is unable to complete the rest of the contemplated voyage, the shipowner is not entitled to any freight since there is no entitlement to pro rata freight.

Consequently, the risk of earning freight lies on the owner until he successfully completes the voyage and should the vessel require salvage services during the course of the voyage, that proportion of any salvage award that is payable in respect of unearned freight must be paid by the owner.

However, since the carrier will frequently require funds to enable him to defray the expenses which he must pay in order to perform the voyage the traditional rule is often modified (particularly in the case of dry cargo charters) and it is now common to see clauses which provide, for example, that:

*"freight deemed earned on shipment, ship or cargo lost or not lost, 90 per cent payable within three days of signing and releasing bills of lading and the balance on true and complete delivery of the cargo."*

In such circumstances, the shipowner becomes entitled to the freight once he has loaded the cargo and the risk of freight is passed from the owner to the charterer. This has the following results:

- if the ship and/or cargo is lost before the freight is paid through no fault of the shipowner, the charterer is still obliged to pay the freight on the agreed date;
- if the freight has been paid and the ship and/or cargo is subsequently lost through no fault of the shipowner, the charterer is not entitled to recover the freight;
- should the vessel require salvage services during the course of the voyage, that proportion of any salvage award which is payable in respect of unearned freight must be paid by the owner.

#### 4.5.1.2.1.2 *The Rule Against Set-off (i.e. Deductions from Freight)*

For the public policy reasons explained above in Chapter 4.5.1, it is not normally permissible to deduct or to set off claims for damages for breach of contract against the owner's claim for freight unless there is a clear clause allowing such deductions or set-off in the contract. The freight must be paid in full and the charterer must bring his cross-claim in separate proceedings. Consequently, such cross claims will be subject to whatever exception, limitation or time limit clauses that are applicable under the charter and the result may be that the shipowner receives his full freight whilst the charterer's claim fails.

Because of such restrictions, it has become common in the case of tanker charters to include clauses which expressly allow charterers to deduct from freight the value of any cargo which remains unpumpable or in liquid form on the vessel on completion of discharge:

*"If there is a difference of more than 0.5 per cent between bill of lading figures and delivered cargo as ascertained by Customs Authorities at discharge port, charterers have the right to deduct from freight the CIF value of the short delivered cargo. Owners have the right to appoint an independent surveyor in order to check the cargo figures in conjunction with Customs Authorities."*

However, it must be emphasized that the terms of these clauses can vary substantially and that if the meaning of the clause is uncertain, courts and arbitrators normally construe them in favour of shipowners consistent with the basic rule at common law.

#### 4.5.1.2.2 *The Duty to Pay Demurrage*<sup>22</sup>

A voyage charter normally involves four distinct stages:

- The approach voyage;
- The loading;
- The laden voyage;
- The discharging.

Whilst the shipowner is the party who is best able to be in control of the two voyage stages, it is the voyage charterers who are best placed to control the loading and the discharging stages since it is they who have to make the cargo available for shipment and to take delivery of the cargo. This poses a problem for the shipowner since he will have calculated the freight which makes the voyage commercially viable after having estimated the time required for performing the four stages and the consequent voyage costs based on that time estimate. Therefore, anything which

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<sup>22</sup> This issue is considered in more detail in Chapter 4.5.6.1.1.

interrupts the loading or discharging operations or causes them to take longer than was originally foreseen will cost the shipowner money and may well result in an overall loss on the voyage. Consequently, the shipowner is normally entitled to additional remuneration in the form of agreed damages (demurrage) for any additional time taken by the charterers to load and/or discharge the cargo over and above the time granted to them for that purpose in the contract (the laytime).

#### 4.5.1.3 Liens<sup>23</sup>

Most voyage charters will provide expressly that the shipowner is to have a lien on cargo for freight and demurrage. However, even if the charter is silent in that regard, there is normally an implied right at common law to exercise a lien for freight (but not for demurrage) that is payable on delivery of the cargo.<sup>24</sup>

#### 4.5.2 The Charterer's Duty to Give Legitimate Employment Instructions<sup>25</sup>

In general, a time charterer has greater powers to exercise commercial control than a voyage charterer since the fundamental basis of a time charter is that the charterer has the ship to use (subject to the terms of the charter) as and where he pleases during the term of the charter, whilst in the case of the voyage charter, the charterer cannot use the vessel to perform any employment which is outside the ambit of the agreed voyage. However, the more modern forms of voyage charters (particularly tanker charters) do allow the charterers more flexibility than has traditionally been allowed in that they entitle the charterers to amend or vary voyage orders usually in exchange for providing the shipowner with an indemnity against any losses and/or liabilities that the shipowner may incur as a result of complying with such revised orders.

Most time charters have clauses in which the right of the time charterer to give employment instructions is expressly outlined. The charterer is entitled to give, and the owner is obliged to comply with, employment instructions given by the charterer, in consideration for which, the charterer agrees to indemnify the owner, sometimes expressly and sometimes impliedly, for most (but not all) losses and liabilities incurred by the owners as a direct result of so doing. The wide extent of the charterers' rights in that regard have been described as follows:

<sup>23</sup> For more detailed commentary see Chapter 24.3 (Security Enforcement Measures) and Chapter 17 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2005.

<sup>24</sup> There is a similar implied right under the common law to exercise a lien on the cargo for general average (see Chapter 10) and salvage (see Chapter 14).

<sup>25</sup> See Chapters 19 and 21 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

*“Clause 8 of the present charterparty, providing that the master (although appointed by the owners) shall be under the orders and directions of the charterers, gives the charterer his key right under the contract: to decide where the vessel shall go and what she shall carry, how (in short) she shall be used, always subject to the terms of the charterparty. The language used is general and the power correspondingly wide.”*

However, the owner is not obliged to comply with every order given by the charterer and the owner is not always protected by an indemnity if he complies with an employment instruction.

#### **4.5.2.1 Restrictions on the Charterers’ Right to Give Employment Instructions**

The charterer is not entitled to give and the shipowner has a *duty* to refuse to comply with orders which:

- Subject the vessel or her crew to danger; or
- Oblige the vessel or crew to commit illegal acts; or
- Oblige the vessel or crew to commit fraudulent acts.

In such circumstances, the shipowner must refuse to comply with the order and if he fails to do so, he cannot claim an indemnity from the charterers for any liability, loss or damage that he suffers as a result of complying with the order since the cause of such liability etc., is not the charterer’s order but the shipowner’s own fault in doing something that he had a duty not to do.

Furthermore, the charterer is not entitled to give and the shipowner has a *right* to refuse to comply with orders which require the shipowner to do something which (although not illegal or fraudulent) falls outside that ambit of the services which he has agreed to perform under the charter, e.g. to proceed outside the agreed trading limits or to load an excluded cargo or to issue bills of lading otherwise than in the form agreed in the charter.

In such circumstances the shipowner can either:

- agree to comply with the order and rely upon an implied right to indemnification at common law; or
- refuse to comply with the order; or
- agree to perform only if the charterers agree to additional terms which are not included in the time charter. Typically, a shipowner can be expected to demand additional remuneration, and/or indemnification for additional expenses incurred and/or a more secure indemnity (possibly in the form of a bank guarantee) for any liabilities which he incurs to third parties as a result of complying with the order.

Finally, the shipowners are not obliged to comply with the charterers' employment orders immediately in all circumstances. It may not always be completely clear at the time when an employment order is given whether the order is indeed a legitimate order and, consequently, the shipowners are normally given a reasonable time within which to make enquiries to ascertain the facts, to evaluate the legitimacy of the order given and the potential ramifications for owners before they are obliged to comply with the order. It follows that the ship remains on hire during such periods of enquiry.

#### **4.5.2.2 Restrictions on the Shipowner's Right to be indemnified by the Charterers**

If shipowners comply with the charterers' employment instruction they will normally be entitled to an indemnity either as a result of an express provision in the charterparty (an express indemnity) or as a result of the implication of law (an implied indemnity). However, even when the owner is entitled in *principle* to an indemnity it does not follow that he will secure an indemnity in all circumstances or in respect of all losses. It must be proved that the charterers' order was the direct cause of the liability, loss or damage incurred by the shipowner. Therefore, there may be no right to an indemnity if the liability, loss or damage is not caused by the employment order but by some other intervening event such as the negligent manner in which the crew have carried out the charterers' employment order. Similarly, the shipowner would not normally be entitled to claim an indemnity for costs and expenses which would have been incurred in any event even if the vessel was not engaged in performing the services ordered by charterers.

#### **4.5.3 The Charterer's Duty to ensure that Dangerous Goods are not loaded without Giving Notice**

Detailed commentary on this issue can be found in Chapter 7 (Dangerous Goods Claims).

#### **4.5.4 The Charterer's Duty to ensure that the Vessel is directed by them only to Safe Ports**

Detailed commentary on this issue can be found in Chapter 13 (Safe Ports Claims).

## 4.5.6 The Charterer's Duty to perform their Duties without Delay

### 4.5.6.1 Voyage Charters

It has already been pointed out in Chapter 4.2.3 above that, under a voyage charter, the risk of delay falls predominantly on the shipowner.

#### 4.5.6.1.1 *The Duty to Load and/or Discharge within the agreed Laytime*<sup>26</sup>

The freight which the charterer pays entitles him to use the vessel not only for the carriage of the cargo but also for the time which is taken to load and discharge the cargo. In calculating the freight, the owner makes an estimation of the time which the loading and discharge is likely to take and the charterer is allowed to use this time (called 'laytime') as he wishes without further payment. However, once this time has been used, the freight becomes less valuable to the owner as the delay causes him to incur greater expense. Accordingly, the charter usually provides that once the laytime has expired, the charterer becomes liable to pay liquidated (i.e. agreed) damages for the delay. Such payment is usually calculated on a daily basis and is called 'demurrage'.

The voyage charter usually has detailed provisions relating to laytime and demurrage and it is often a complex issue to calculate the running of laytime and demurrage. The key questions are normally the following:

- How is laytime calculated?
- When does time start to run?
- What suspends the running of time?
- When does time finally stop running?

The time spent before laytime has been used up is normally referred to as the running of the laytime clock. However, once the agreed laytime has been used up the vessel will immediately go on to demurrage and thereafter reference is normally made to the running of the demurrage clock. For the purposes of this discussion, reference to the running of 'time' is intended to refer to either laytime or demurrage (whichever clock is then running) except where specific reference is made to either laytime or demurrage.

The moment when time commences to run at the load port or discharge port is an important moment since that is the time when the risk of delay is passed from the shipowner to the charterer and the moment when laytime finally stops running is also an important moment since that is the time when the risk of delay is passed

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<sup>26</sup> See Chapters 15 and 16 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2005, and for further detailed commentary, see *Laytime and Demurrage* By John Schofield, Informa, 6th edition 2011 and *Commencement of Laytime* by Donald Davies, Informa, 4th edition, 2006.

back from the charterer to the shipowner. For example, if a ship is delayed getting into port the risk of delay falls on the shipowner but if the ship is delayed after it has completed the voyage the risk of delay falls on the charterer. Similarly, if the vessel cannot leave port after the loading or discharging has been completed, the risk of that delay normally falls on the shipowner.

Normally, time does not start to run until all the following conditions have been satisfied:

- The vessel must have reached the agreed destination (whether port, berth, anchorage etc.); *and*
- She must be ready in all material respects to load or discharge; *and*
- A valid Notice of Readiness (NOR) confirming (1) and (2) must have been given to the persons nominated in the charterparty to receive it.

Once time has started to run it runs continuously and will be suspended only if the delay has been caused by either:

- Default on the part of the shipowner; or by
- An incident which clearly falls within a clause of the charter specifying that time is to be suspended in such circumstances. In this connection, a clause specifying that 'laytime' is to be suspended is not sufficient to suspend the running of the demurrage clock if the vessel is already on demurrage at the time of the incident. To suspend the running of the demurrage clock the clause must refer expressly to demurrage and not merely to laytime.

Demurrage is intended to be agreed compensation for a breach by the charterers of their duty to complete cargo operations within the laytime. Therefore, unless the charterparty provides otherwise, it is not normally possible for shipowners to recover other losses in addition to demurrage if the cause of those losses is a breach by the charterers of their duty to complete cargo operations within the laytime.

Normally, time finally stops running not when the vessel leaves the port of loading or discharging but when loading or discharging has been completed. However, it has become common in some industries to extend the running of time. For example, it is common in the tanker trade for time to continue to run until hoses are disconnected or until certain specified documents (e.g. bills of lading) have been delivered on board.

#### 4.5.6.2 Time Charters<sup>27</sup>

The duration of the charter period is important to both owners and charterers for the following reasons:

- It is important to shipowners since firstly, they wish to know what their overall income will be for the charter period and since secondly they need to know when the vessel is likely to be redelivered to them in order to plan future employment;
- It is important to time charterers since they cannot properly plan sub-fixtures unless they know that they have the use of the vessel for a specified period.

Therefore, any event that subsequently affects the duration of the period may have important repercussions for both parties. If the vessel is redelivered before the agreed redelivery date (i.e. underlap) and charterers refuse to pay hire for the underlap period the shipowners will have lost the income that was contemplated for the underlap period. Similarly, if the charterers have entered into a sub-charter with a third party to perform a voyage which is likely to result in redelivery of the vessel under the head time charter after the agreed redelivery date (i.e. overlap), they may find themselves unable to carry that cargo whilst shipowners, should they allow the vessel to be used for such a purpose, may find themselves unable to deliver the vessel before the cancelling date specified in her next fixture.

##### 4.5.6.2.1 Underlap

Since the charterers have promised to pay hire for the agreed charter duration a failure by them to do so otherwise than as a result of redelivery forced by shipowners' default is a breach of contract. In such circumstances, shipowners are normally entitled to damages equivalent to the hire which they should have received for the underlap period at the charter rate together with sums which charterers were obliged to pay under the charter (e.g. bunkers etc.), less any savings made as a result of early redelivery.

##### 4.5.6.2.2 Overlap

In the absence of any contrary terms, the contract defines the period for which the time charterers are entitled to exploit the vessel commercially and the shipowner is entitled to re-assume control of his vessel on the expiry of that period. If the vessel is not redelivered at the agreed location by the end of the charter period the time charterer is in breach of contract and is obliged to recompense the shipowner in damages for the overlap period. Normally, the damages that are recoverable by shipowners will reflect the opportunity lost by the shipowners as a result of the delayed redelivery and will be the difference between the charterparty rate of hire and the market rate of hire for the vessel (if higher) for the overlap period.

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<sup>27</sup> See Chapter 4 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.



Alternatively, and again in the absence of any contrary terms, if it appears at the time that the charterers order the vessel to proceed on her last voyage under the charter that the voyage, if performed, is likely to result in redelivery after the agreed redelivery date, the shipowners are entitled to refuse to comply with the order. In such circumstances, the charterers are likely to experience difficulty since they may be committed to sub voyage charterers to complete the contemplated voyage but are not able to secure the use of the vessel in order to perform that voyage. The shipowners have the right to refuse the charterer's order in such circumstances even though it had originally been perfectly feasible to perform the sub voyage in time and circumstances have subsequently changed through no fault of their own, e.g. because another ship has run aground and blocked traffic in and out of the contemplated loading port for the cargo.

These principles underline the basic principle that in the context of a time charter:

*"... the risk of delay is primarily on the Charterer."*

#### **4.5.6.2.3 Protective Clauses**

There is nothing in principle to prevent time charterers from introducing provisions which are designed either to balance the risk of delay or to transfer the risk of delay to the shipowners. Historically, a balance has been achieved by ensuring that the charter duration is made subject to a tolerance. For example, if the charter duration is described as *"3 months 15 days more or less charterers' option,"* so long as the vessel is redelivered at any time within 15 days before or 15 days after the three months, there is no overlap and no underlap and no breach of contract on the part of the charterers. Even the addition of the word 'about' (e.g. 'about three months') entitles the charterers to some tolerance albeit that the extent of the tolerance has not been expressly stated.

In the tanker industry it has become common for the time charter forms developed by the oil majors to introduce clauses ('last voyage clauses') which are designed to provide the charterers with whatever extra time that may be needed to ensure that they have the use of the ship to complete any sub-fixtures which remain to be performed at the expiry of the originally agreed redelivery date. The effect of such clauses is to transfer the risk of delay from the charterers to the shipowners. For example, if the shipowner has negotiated his next fixture on the basis that the vessel will be redelivered under the current charter on or about the agreed redelivery date, he runs the risk that the current time charterers may exercise their rights under the last voyage clause with the result that the vessel may not be delivered to her 'next' charterers by the cancellation date in that charter. Should the 'next' charterers exercise the option to cancel that charter the shipowner has no remedy against the current time charterers.

Finally, it has become common, particularly in the case of time charter trips, to qualify the charter duration with the words 'without guarantee', e.g. *"one round Atlantic voyage 3 months without guarantee."* It appears that so long as the time charterers have estimated the likely duration in good faith then they are not in breach of contract even if that estimate appears to reasonable men to be completely inaccurate. The effect of such words is again to transfer the risk of delay from the charterers to the shipowners.

#### **4.6 Law and Jurisdiction**<sup>28</sup>

Charterparties will normally include a law and jurisdiction clause which will establish the agreed system of law that is to be applied for dispute resolution and the country and/or city where claims are to be pursued. In the majority of cases, such clauses will provide for arbitration in one of the major arbitration centres around the world. The choice of law and jurisdiction will often have a major impact on the merits of a claim or defence and on the ability to enforce an award or judgment in another country. Therefore, this is not a choice that should be taken lightly. Traditionally, parties have tended to choose English law as the governing law since English law has over the centuries developed well-established and balanced rules for regulating charterparty disputes.

#### **4.7 Insurance**<sup>29</sup>

A distinction needs to be drawn between:

- The claims which are made under charterparties; and
- The costs incurred in litigating such claims.

All kinds of claims may be made under charterparties and such claims may or may not be the subject of insurance. For example, claims for loss of or damage to cargo are usually covered by P&I insurance whereas claims for liabilities arising as a result of the delivery of cargo without surrender to the carrier of the original bills of lading are not.<sup>30</sup> In each case it is necessary to consider the nature of the claim and the cover afforded by the various types of insurance that are available. However, it must be appreciated that in many instances, insurance cover may not be available.

The costs that may be incurred in pursuing or defending charterparty claims may be high. Such claims include not only legal fees but the costs of surveyors, consultants, technical experts etc. Should the claim that is being litigated be the subject of insurance then the costs incurred in pursuing or defending such claims are usually covered by the same insurance. However, even if the claim is not subject to

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<sup>28</sup> A more detailed commentary on this issue can be found in Chapter 19 (Law and Jurisdiction).

<sup>29</sup> A more detailed commentary on this issue can be found in Chapter 25 (The Fundamental Principles of Marine Insurance), Chapter 26 (The Structure of Marine Insurance) and in the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV Rule 6: Defence Cover).

<sup>30</sup> For more detailed commentary see Chapter 20.2.1.3 (Letters of Indemnity).

insurance, it is possible to insure the litigation and other related costs that may be incurred in pursuing or defending such claims. The International Group of P&I Clubs offer such insurance under a separate class of insurance which is normally referred to as Defence Cover or FD&D cover.<sup>31</sup> Similar insurance is also offered by market insurers on a fixed premium basis.

## 4.8 Claims Management

More charterparty claims are heard by arbitrators and courts than any other type of claim and such claims can be both costly and time consuming. Therefore, it is important that shipowners and charterers should familiarise themselves with the various forms of charterparty that are commonly used and with the advantages and disadvantages that accompanies each form. In the event of a dispute, parties should consult their defence insurers at an early stage since the lawyers that are employed by such insurers can give valuable guidance which can ensure that the member's rights are preserved and that the right litigation strategy is followed.

For those parties who are members of BIMCO much useful guidance on the most common types of charterparty dispute can be found in the BIMCO booklet entitled *Check Before Fixing* which is regularly updated.

## 4.9 Case Studies

### Case Study 1<sup>32</sup>

The TRITON LARK<sup>33</sup> was time chartered on the New York Produce Exchange (NYPE) form and was ordered by time charterers to proceed from Hamburg to China via the Suez Canal. However, because of the fear of piracy off the Horn of Africa, the owners insisted on proceeding via the Cape of Good Hope despite the fact that this would substantially increase the cost and delay. The charterers subsequently claimed from the shipowners the additional hire and expenses incurred by them as a result of the longer voyage. The court held that whilst the employment orders that the time charterers were normally entitled to give included the right to dictate the route that the vessel should follow, that right was subject to any restrictions that were placed by the terms of the particular charter and also by the common law. The charter included the CONWARTIME 1993 clause which entitled the vessel to refuse orders "to ... any ... place ... where it appears that the Vessel, her cargo, crew or other persons on board the Vessel, in the reasonable judgement of the master and/or the owners, may be, or are likely to be, exposed to war risks." The court held that this clause entitled the shipowners to follow the route that they considered safe if "in the

31 For more detailed commentary see Chapter 26.3.1.6 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV Rule 65 (Defence Cover)).

32 Examples of further case studies can be found in the BIMCO publication *Check Before Fixing*.

33 [2012] 1 Lloyds Rep. 151 and 457.

reasonable judgment of (the Shipowners), there was a real likelihood that the Gulf of Aden would, on account of acts of piracy, be dangerous to TRITON LARK"; and also stated that "the owners must make a judgment ... in good faith" and "the judgment reached must be objectively reasonable." Consequently, the ship remained on hire throughout the voyage via the Cape of Good Hope and charterers remained responsible for the extra costs incurred by such voyage (e.g. additional bunkers, crew costs etc.).

**(NB!** It is likely that the result would be the same if the time charter had included the BIMCO Revised Piracy Clause for Time Charters).

### Case Study 2

The SEAFLOWER<sup>34</sup> charterparty included the following Oil Majors Approval Clause:

*"Vessel is presently MOBIL (expiring 27/1/98) CONOCO (expiring 3/2/98) BP (expiring 28/1/98) and SHELL (expiring 14/1/98) acceptable. Owners guarantee to obtain within 60 days (sixty) days EXXON approval in addition to present approvals."*

The vessel was delivered to charterers on the 5 November 1997 and performed three sub-voyage charters for BP between that date and the end of December. On 30 December the charterers fixed the vessel 'on subjects' to load a cargo of Exxon products and called on the shipowners to obtain Exxon approval by the 5 January (i.e. by the end of the 60 days). The shipowners responded by saying:

*"... Owners wish to confirm that preparation works for all Majors approval concerning the charter (including Exxon) are in progress and proper schedule of vetting inspections will take place within Jan/Feb 1998."*

The charterers cancelled the charterparty on the basis that the failure of the shipowners to obtain within the 60 days the Exxon approval that they had guaranteed to obtain was a very serious breach (a breach of condition). It is critical for charterers to ensure that the vessel that they have chartered is able to meet certain terminal standards otherwise the vessel will not be allowed to load cargo at that terminal. Oil major approval is one example of the manner in which charterers try to control this issue and other commodity trades also require similar approvals.

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34 (2001) 1 Lloyd's Rep. 341

## Chapter 5

# Claims for the Loss of, or for Damage to, the Ship

### 5.1 Introduction

Ships are designed, insofar as it is possible, to withstand the forces of nature. Furthermore, the ship's machinery, propulsion and equipment are designed in such a way that that it can move safely at the appropriate speed between ports in order to achieve its commercial purpose. Therefore, most ships are able to trade throughout their working lives without sustaining any substantial damage and, gratifyingly, the number of ships that become a total loss is small and has decreased even further in recent years relative to the increased size of the world merchant fleet.<sup>1</sup>

However, some ships are lost each year with tragic consequences that involve loss of life, damage to the environment and/or the loss of property value. Insurance cannot provide a full and complete remedy in such circumstances, but it does provide financial support to the assured for his own losses and for the liabilities that he has to other parties. It can also, in some circumstances, provide victims with a direct remedy.

Claims for the loss of a ship are not usually complicated provided that it is clear that a total loss has occurred. However, it may not always be easy to assess whether a seriously damaged ship is in fact a total loss or whether it is still economically feasible to salvage and repair it. In most cases, ships incur physical damage that is not sufficient to amount to a total loss but which, nevertheless, requires repairs to enable the ship to resume normal trading activities. The severity, complexity and consequences of such damage can differ substantially from case to case. In many cases, the incident will merely result in minor damage that does not require any

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<sup>1</sup> See the report entitled *Safety and Shipping 1912-2012: From Titanic to Costa Concordia* published by Allianz Global Corporate & Specialty in conjunction with Cardiff University which can be accessed at: <http://www.agcs.allianz.com/insights/white-papers-and-case-studies/safety-and-shipping-report/downloads/>.

insurance claim to be made. However, at the other end of the scale, there may be a serious incident resulting in a substantial insurance claim for salvage, towage, repair, third party liabilities and loss of income.

It is not possible within the framework of this publication to discuss in detail all relevant aspects of the claims that can be made for loss of, or damage to, ships, and the following commentary is intended to focus on certain key aspects that are normally relevant when dealing with such incidents and claims. It is also important to emphasise that the following commentary should be read in conjunction with the commentary that can be found in Chapter 26 (The Structure of Marine Insurance). Finally, it must be appreciated that, in the final analysis, the right to recover will be determined by the precise terms of the particular policy, and that policy terms can differ substantially from each other.

## 5.2 Proof of Damage to, or Loss of, the Ship

Most policies provide that the assured may claim compensation in the event that the ship has been lost or damaged as a result of a fortuitous event. Under English Institute Time Clauses Hulls (ITCH) terms, the onus of proof is on the assured to prove that the damage has been caused by one of the specifically named insured perils and not for example, by wear and tear. However, the position differs somewhat under the Nordic Marine Insurance Plan (NMIP), which is an 'all risks' insurance rather than a 'named peril' insurance. Therefore, the burden of proof is discharged under the NMIP if the assured shows that loss or damage of the kind that is insured under the policy has been caused during the period of insurance, as well as the extent of the loss.<sup>2</sup> If so, the assured has a *prima facie* right of compensation unless the insurer can prove that the loss was in fact caused by an excepted peril. For example, if the assured has shown that the vessel has suffered some physical damage during the policy period, the assured is entitled to compensation under the NMIP unless the H&M insurer can prove that the damage was caused by an excluded peril, whereas under ITCH terms, the assured is not entitled to compensation unless he can prove that the loss was in fact caused by one of the named perils.

## 5.3 Actual Total Loss

An 'actual total loss' is defined in the UK Marine Insurance Act 1906 (MIA) as follows:

*"Where the subject-matter insured is destroyed, or so damaged as to cease to be a thing of the kind insured, or where the assured is irretrievably deprived thereof, there is an actual total loss."*<sup>3</sup>

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2 See Clause 2 – 12 of the Nordic Marine Insurance Plan.

3 Marine Insurance Act, Section 57(1).

Therefore, a ship would normally be considered to be an actual total loss should it, for example, be totally destroyed,<sup>4</sup> or sunk in water that is so deep that it is technically not feasible to recover it, or, in one particular case, when a bulk carrier was carried on a tidal wave far ashore into the mangrove jungle with the result that it was not possible to salvage and refloat it.

A ship may also be considered to be an actual total loss (or a presumed total loss) if it has disappeared, or has been abandoned by its crew, and a specified period of time has passed. For example, the MIA<sup>5</sup> provides that:

*“Where the ship concerned in the adventure is missing, and after the lapse of a reasonable time no news of her has been received, an actual total loss may be presumed.”*

However, the Nordic Marine Insurance Plan (NMIP)<sup>6</sup> has a more elaborate provision:

*“If the ship is reported missing, the assured may claim for a total loss when three months have elapsed from the date on which the ship was, at the latest, expected to arrive at a port. If the ship is reported missing under circumstances that give reason to assume that it is icebound and will subsequently be recovered, the time-limit is twelve months.*

*If the ship has been abandoned by the crew at sea without its subsequent fate being known, the assured may claim for a total loss when three months have elapsed from the day when the ship was abandoned. If it was abandoned because it was icebound, the time-limit is twelve months. If the ship has been seen after being abandoned, the time-limit runs from the day on which it was last seen.*

*If, before expiry of the time-limit mentioned in paragraphs 1 and 2, it is clear that the assured will not recover the ship, he may at once claim for a total loss.*

*If the time-limit has expired and the assured has submitted a claim for a total loss, the insurer may not reject the claim because the ship is subsequently recovered.”*

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4 On 6 December 1917, the city of Halifax, Nova Scotia, Canada, was devastated by the detonation of the SS *Mont-Blanc*, a French cargo ship that was fully loaded with wartime explosives, after colliding with the Norwegian SS *Imo*. About 2,000 people were killed by debris, fires, and collapsed buildings, and it is estimated that around 9,000 were injured.

5 Marine Insurance Act, Section 58.

6 Nordic Marine Insurance Plan, 1996 – Version 2010: § 11-7.

### 5.3.1 Compensation for Total Loss

In such cases, the assured is entitled to be paid the value of the ship. However, it is a peculiarity of marine insurance that the assured and the insurer are entitled to agree the extent of the indemnity at the time that the contract of insurance has been concluded, i.e. to agree a valued policy. If the extent of the indemnity has been agreed in this manner, the indemnity is, in the absence of fraud, conclusive and binding between the parties although it may be less, or even more, than the actual pecuniary loss. In contrast, an unvalued policy has no specified value stated in the policy and the payment, if a loss occurs, will be the actual market value of the ship. However, most H&M policies (and associated Increased Value insurances)<sup>7</sup> are valued policies.<sup>8</sup>

The relevant value is payable in full even if the ship may already have sustained unrepaired damage at the time of the actual total loss<sup>9</sup> and the assured is entitled to be compensated on this basis as soon as agreement has been reached with the insurers that such an event has occurred. However, in some circumstances, the insurers may wish to try to salvage the ship in order to avoid condemnation. The NMIP gives the insurer an absolute right to do so and places a duty on the assured to do his utmost to enable the insurer to carry out the salvage operation.<sup>10</sup>

### 5.4 Constructive Total Loss<sup>11</sup>

A constructive total loss (CTL) occurs when the ship has sustained such damage and/or is located in such a difficult place that the cost of salvaging, moving and repairing it would exceed its subsequent value. For example, Section 60 (1) of the MIA provides that:

*“Subject to any express provision in the policy, there is a constructive total loss where [the ship] is reasonably abandoned ... because it could not be preserved from actual total loss without an expenditure which would exceed its value when the expenditure had been incurred.”*

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7 See Chapter 26.3.1.2 (The Structure of Marine Insurance).

8 See, for example, Clause 2 -3 of the Nordic Marine Insurance Plan.

9 The principle is sometimes referred to as ‘Total loss absorbs partial damage.’ See, for example, Section 77(2) of the UK Marine Insurance Act.

10 See the Nordic Marine Insurance Plan, § 11-2.

11 The NMIP does not use the phrase CTL but refers to the ‘condemnation’ of the ship. However, both terms have effectively the same meaning and the use of the phrase CTL will be used hereafter for the sake of ease.



Section 60 (2) (b)(ii) the goes on to provide that:

*"In particular, there is a constructive total loss where:*

- (b) the cost of recovering the ship or goods, as the case may be, would exceed their value when recovered; or*
- (ii) In the case of damage to a ship, where she is so damaged by a peril insured against that the cost of repairing the damage would exceed the value of the ship when repaired."<sup>12</sup>*

However, the NMIP provides that a ship can be considered to be a CTL<sup>13</sup> in more liberal circumstances:

*"The conditions for condemnation are met when casualty damage is so extensive that the cost of repairing the ship will amount to at least 80% of the insurable value, or of the value of the ship after repairs if the latter is higher than the insurable value."<sup>14</sup>*

Therefore, the assured is entitled to treat the ship as a CTL if the cost of repairs exceeds the ship's value or an agreed percentage of that value depending on the precise terms of the particular insurance. However, it is necessary in both cases to clarify two issues:

- What items are included in the cost of repairs; and
- What constitutes the ship's value.

#### **5.4.1 What Items are included in the Cost of Repairs?**

It is again important to remember that different policies will have different rules in this regard. For example, the MIA provides that the relevant repairs are only those that are necessary to repair the damage that has been caused by the relevant casualty. However, the approach that is adopted by the NMIP is more liberal in that Clause 11-3 provides that:

*"Casualty damage shall be deemed to include only such damage as has been reported to the insurer concerned and surveyed by him in the course of the last three years prior to the casualty that gives rise to the request for condemnation."*

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<sup>12</sup> Although section 27 (4) of the Marine Insurance Act provides that the 'value of the ship' for these purposes is to be the actual value rather than any agreed value, the terms of most standard policies provide that it is the agreed insured value that is to be relevant.

<sup>13</sup> See footnote 11.

<sup>14</sup> NMIC 1996 – Version 2010: § 11-3.

Furthermore, whereas the MIA provides that “ ... account is to be taken of the expense of future salvage operations ... ”<sup>15</sup> when assessing the cost of repairs, the NMIP provides that:

*“Costs of repairs are deemed to include all costs of removal and repairs which, at the time when the request for condemnation is submitted, must be anticipated if the ship is to be repaired **except, however, salvage awards or compensation for depreciation in value under § 12-1, paragraph 4.**”*

#### 5.4.2 What constitutes the Ship's Value?

Once the cost of repairs has been calculated that cost must then be measured against what the ship's value would be after repairs assuming that she were to be repaired. Although section 27 (4) of the MIA provides that the 'value of the ship' for these purposes is to be the actual market value rather than any agreed value, the terms of most standard policies provide that it is the agreed insured value<sup>16</sup> that is to be relevant.<sup>17</sup> However, the NMIP provides that the relevant value is to be the higher of the insured value or the actual market value and that the assessment is to be made at the time that the claim for a CTL is made.

### 5.5 Compromised Total Loss

A compromised total loss is an imprecise concept in the sense that it is not defined in any statute or standard H&M insurance terms and can best be described as a form of settlement for unrepaired damage to the ship which may be funded either solely by H&M, or jointly by H&M and IV insurers, but not necessarily in equal proportion. In situations where the criteria that is necessary to establish a total loss has not been satisfied, the insurers and the assured may, nonetheless, reach agreement that the loss shall be compensated by way of a cash settlement in lieu of the cost of actual removal and/or repairs. Therefore, this approach has been adopted in borderline CTL cases where the H&M insurers are in genuine doubt whether there is truly a CTL, but are prepared to treat it as such if the assured accepts some deduction in the total loss compensation that is to be paid. It has also been adopted in ship damage cases where the H&M insurers agree to assume ownership of the ship against payment of a cash settlement to the assured. Therefore, such a form of settlement can range between full compensation that is similar to a total loss, and a payment that is merely a proportion thereof.

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15 MIA section 60 (2) (ii). The principle is also reflected in Clause 19.2 of Institute Time Clauses Hulls 1/10/83.

16 This is the insured value under the H&M policy and any increased value in the accompanying IV policy is not relevant for these purposes.

17 See, for example, Clause 19 of the Institute Time Clauses Hulls 1/10/83 and 1/11/95.

## 5.6 Subrogation and Abandonment<sup>18</sup>

If the assured is compensated by the insurers on the basis that the ship is an actual total loss or a CTL the insurers are subrogated to whatever rights the assured may have in relation to the ship and any remedies that the assured may have to claim against any other parties that have caused the ship to become an actual or constructive total loss. However, the assured may also wish to abandon his interest in the ship to the insurers who are entitled (but not obliged) to accept such abandonment. In many such instances, the insurer may prefer to settle the claim on the basis of an actual total loss or CTL but not accept the abandonment since, if he were to do so, the ship would thereafter become the insurer's property and he would become obliged to remove the wreck if so required by the relevant authorities.<sup>19</sup>

## 5.7 The Cost of Repairing a Damaged Ship

The assured is entitled to claim the 'reasonable cost'<sup>20</sup> of repairing the damage that has been caused to the ship by an insured peril even if the damage is not sufficient to amount to an actual or constructive total loss. The assured is entitled to claim the cost of the repairs that are necessary in order to bring the ship back into the condition that it was in before the damage was caused provided that the cost of repairs exceeds the applicable deductible.<sup>21</sup> Therefore, if the ship has already been damaged but not repaired prior to the incident in question, the cost of repairing that prior damage does not form part of the claim that can be made in respect of the subsequent incident. Similarly, although it may be inevitable in some instances that damaged parts may have to be replaced by new parts, the assured is not otherwise entitled to claim the cost of repairs that result in an upgrading of the ship. Therefore, if parts can be realistically re-used as part of the repairs, the insurer is entitled to require that this be done.

In order to ensure that repairs are carried out in a cost-effective manner the insurer is normally entitled to require the assured to obtain repair work tenders from competing shipyards chosen by the insurer. For example, Clause 12-11 of the NMIP states that:

*"The insurer may demand that tenders be obtained from the repair yards of his choice. If the assured does not obtain such tenders, the insurer may do so."*<sup>22</sup>

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18 For more detailed commentary see Chapters 25.5 and 25.6 (The Fundamental Principles of Marine Insurance).

19 For further commentary see Chapter 16 (Wreck Removal Claims).

20 See Section 69 of the MIA.

21 In some instances different deductibles may apply to different types of claims. For example, there may be a separate deductible for machinery damage or for hull damage that has been caused by contact with ice.

22 See also Clause 10.3 of the Institute Time Clauses Hulls 1/10/83.

Some policies provide that the insurer will also have the right to decide where the vessel shall undergo repair<sup>23</sup> whereas others give the assured the right to select which repair yard to use based on the tenders received. However, in either case, the assured may not receive full compensation for the subsequent repair costs if the ship is not repaired at the yard that has provided the lowest tender.<sup>24</sup>

The ship may not be able to move safely (or at all) to a yard or place of repair under its own power and the assured may, therefore, be obliged to incur additional costs in towing the ship to, and docking it at, the chosen repair yard. However, cover is normally available under standard H&M insurance for such costs, as well as for any other costs that are reasonably and necessarily incurred in order to prepare the ship for repair such as, for example, costs incurred in removing oil or other contaminants from areas that require repair, pilotage, anchoring and docking costs, port dues, and survey costs.

Since an insurance policy is a contract of indemnity<sup>25</sup> the assured must normally have repaired the ship and produced proof of payment in the form of repair invoices before he is entitled to receive payment from the insurers. However, in some cases, the assured may be entitled to receive advance payments from the insurer in order to fund the repair costs if it is considered that cover is available under the H&M insurance. For example, Clause 5-7 of the NMIP provides that:

*“If the assured, before the adjustment can be issued, proves that he has incurred, or will in the near future incur, major expenses or losses which are covered by the insurance, he is entitled to an appropriate payment on account. If the payment on account concerns expenses which the assured has not yet paid, the insurer has the right to pay the amount directly to the third party concerned.”*

*The rules contained in the preceding paragraph do not apply if the insurer has reasonable doubts as regards his liability. A payment on account by the insurer in no way affects the question of his liability to the assured.”*

### 5.7.1 Temporary Repairs

In some instances, the assured may wish to carry out temporary repairs to the ship pending full and final repair (‘permanent repairs’) of the damage at a later date. There may be a number of reasons for this. For example, it may be necessary to carry out temporary repairs in order to obtain the approval of the classification society for the completion of the voyage and the discharge of all the cargo before

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23 See Clause 10.2 of the Institute Time Clauses Hulls 1/10/83.

24 See Clause 12-12 of the NMIP.

25 See section 1 of the MIA.

the ship can proceed to a yard for final repairs. Alternatively, it may be necessary to carry out such repairs at the casualty site in order to ensure that the ship can be safely moved to a yard where it can be repaired. Finally, if the damage is not serious, the assured may prefer to carry out whatever temporary repairs that may be necessary in order to obtain the approval of the classification society for the ship to continue trading until her next scheduled docking when permanent repairs can then be carried out.

The cost of temporary repairs is usually covered under standard H&M insurance terms if the assured is able to demonstrate that such repairs are necessary since permanent repairs cannot be carried out at or near the place where the ship is located,<sup>26</sup> or because performing the temporary repairs is likely to save removal and repair costs overall. For example, Clause 12-7 second paragraph of the Nordic Marine Insurance Plan states as follows:

*“If temporary repairs of the damaged object are carried out in other cases [than where permanent repairs cannot be carried out], the insurer is liable for costs up to the amount he saves through the postponement of the permanent repairs, or up to 20 per cent p.a. of the assessed insurable hull value for the time the assured saves, if the latter amount is higher.”*

Since the burden of proof lies on the assured to prove that the cost of temporary repairs is covered, it is clearly sensible to involve the H&M insurer in the decision-making as soon as possible.

### **5.8 Unrepaired Damage**

In some cases, the assured may decide not to repair the damage if, for example, the ship may be trading at the time under a lucrative time charterparty and the damage may be of such a nature that the ship can continue to trade safely with the approval of the classification society without repairing the damage. In such circumstances, the shipowner may prefer to postpone the repair until the charterparty has ended or until the ship is due to undergo her next periodic dry-dock survey. Nevertheless, as an alternative to claiming repair costs as and when they are incurred, H&M policies will usually entitle the assured to receive an amount equivalent to the reasonable depreciation in value that has been caused by the damage but not exceeding the reasonable cost of repairs had they been carried out. However, a claim for unrepaired damage cannot normally be made until after the expiry of the policy under which the damage can be claimed.<sup>27</sup>

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<sup>26</sup> See Clause 12-7, first paragraph of the NMIP.

<sup>27</sup> See NMIP 12-2, 1st paragraph and Clause 18 of Institute Time Clauses Hulls 1/10/83.



## Chapter 6

# Collision Claims<sup>1</sup>

### 6.1 Introduction

Despite the advances in marine technology, advanced electronic, satellite and other navigational aids, as well as new training methods for those operating vessels, maritime accidents generally – and marine collisions specifically – continue to feature prominently in annual maritime casualty statistics.

When two large steel structures come into contact, even at low speeds, the incident may result in significant loss and damage involving people, the environment and valuable property, and the following claims are likely to arise:

- i Collision damage to the hulls of the colliding vessels;
- ii Damage to the cargo carried on one or both vessels;
- iii Personal injury claims;<sup>2</sup>
- iv Salvage claims;<sup>3</sup>
- v Pollution claims;<sup>4</sup>
- vi General average claims;<sup>5</sup>
- vii Delay claims.

There may also be consequential claims for loss of income and in a worst case scenario, the collision may cause one or both ships to sink resulting in claims for wreck removal.<sup>6</sup>

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1 For more detailed commentary see Chapter 9 of the *Gard Handbook on P&I Insurance*, 5th edition and *Marsden – Collisions at Sea* by Gault, Hazelwood and Tettenborn, Sweet & Maxwell, 13th edition 2003.

2 For more detailed commentary see Chapter 11 (People Claims).

3 For more detailed commentary see Chapter 14 (Salvage Claims).

4 For more detailed commentary see Chapter 12 (Pollution Claims).

5 For more detailed commentary see Chapter 10 (General Average Claims).

6 For more detailed commentary see Chapter 16 (Wreck Removal Claims).

The severity and complexity of marine collisions may create several challenges that involve casualty response, early strategic claims decisions and proper investigation and evaluation. The claims that arise as a result of marine collisions may also involve different insurers, so that it is important to understand and fully appreciate the scope of the individual insurance covers and the manner in which they interface.

It is not possible within the framework of this Guidance to discuss all relevant aspects of marine collision claims in detail. Therefore, the following is intended to focus on certain key aspects that are aimed to facilitate the proper handling of such incidents and claims.

### 6.1.1 What is a 'Collision'?

A collision is defined in the Oxford English Dictionary as *"the violent encounter of a moving body with another"*. However, for the purposes of maritime law, there is a collision when there is contact between two ships regardless of whether they are moving or at anchor. Therefore, it is necessary to draw a distinction between contacts between a ship and another ship whether moving or stationary (i.e. a 'collision') and contacts between a ship and a floating object that is not a ship (such as a floating oil rig, loading/discharge tank or mooring buoy), or between a ship and an object that is not afloat, (such as a bridge, wharf, crane or offshore structure sitting on the seabed) (i.e. an allusion). A collision between ships is usually governed by different rules of law than those that regulate contact between a ship and a 'fixed or floating object' that is not a ship (an FFO). Similarly, a distinction is drawn in marine insurance between a collision between 'ships' (whether both are moving or one is stationary) and a contact between a ship and a 'fixed or floating object' (FFO). Therefore, the liability that arises as a result of a collision between ships and as a result of contact between a ship and an FFO may be (but does not have to be) insured with different insurers.

It is not necessary for the purposes of a collision that there be contact with the hull of another vessel so long as there is contact with some part of another vessel. Therefore, there can be a collision if ship A comes into contact with the anchor chain of ship B or with the fishing net of another vessel. Indeed, the English court has held that a collision can occur even without actual contact if there is sufficient proximity between the vessels to cause damage to one or both vessels, as may occur, for example, if the wash of a ship proceeding at excessive speed causes ranging damage to another ship which is already berthed.<sup>7</sup>

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<sup>7</sup> *The Royal Sovereign*, [1950] 84 Lloyd's Rep. 549 and *The Royal Eagle*, [1950] 84 Lloyd's Rep. 543.



Perhaps surprisingly, it is not always easy to decide whether something is a 'ship' or an 'FFO.' For example, a floating offshore oil storage and off-taking unit is equipped with machinery and propulsion and may therefore be operating at one moment in time as a ship transporting cargo, but is otherwise used for the storage and for the off-taking of oil and remain stationary offshore for long periods of time.<sup>8</sup>

This Chapter deals solely with issues that arise as a result of collision between ships whereas Chapter 9 deals with issues relating to contacts between ships and FFOs.

## 6.2 Fault

Most countries have laws which impose a duty of care on persons and corporations and require them to take reasonable care not to injure the person or property of other people or corporations.<sup>9</sup> Breach of such duty usually gives rise to liability in tort<sup>10</sup> and it is this principle that has traditionally formed the basis of collision liability. Therefore, the mere fact that two ships collide is not in itself sufficient to establish liability; it must be proved that the collision was caused by the fault (i.e. negligence) of one or both ships.<sup>11</sup>

To establish fault it is necessary to establish blameworthiness for a navigational error and that such error caused or contributed to the collision. The owners of ships are answerable for the faults of their own servants and agents including those of pilots, irrespective of whether the ship is under voluntary or compulsory pilotage.

To establish blameworthiness it is necessary to establish negligence or "*a failure to exercise that degree of skill and care which is ordinarily to be found in a competent seaman*" under the prevailing circumstances.<sup>12</sup> The key question is: could the collision have been prevented by the exercise of ordinary care, caution and skill? The standard of care is the same for all vessels, regardless of type, trade or size and has been defined legally as follows: "*the standard of skill and care to be applied by the court is that of the ordinary mariner and not the extraordinary one, and seamen under criticism should be judged by reference to the situation as it reasonably appeared to them at the time, and not by hindsight.*"<sup>13</sup>

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8 This aspect is also important in relation to the international conventions that regulate compensation for marine pollution, such as the CLC. The IOPC Fund has established a working group and commissioned a legal analysis in this regard. See their website: [www.iopcfund.org](http://www.iopcfund.org) for further details.

9 For more detailed commentary see Chapter 14 of the *Gard Handbook on P&I Insurance*.

10 This is referred to as 'delict' or 'culpa' in civil law jurisdictions.

11 For a searching review of this history see for example David R Owen, *The Origins and Development of Marine Collision Law* 51 *Tul. L. Rev.* 759 (1977). In the US, a different rule of 'divided damages' applied for about 120 years until 1975 when it was changed in the landmark US Supreme Court decision: *United States v Reliable Transfer Co.*, 421 U.S. 397, S. Ct. 1708, 44 L. Ed. 2d, 251, 1975 AMC 541.

12 Viscount Maughan in *The Llanover*, [1944] 78 *Lloyd's Rep.* 461.

13 Brandon, J in *The Boleslaw Chrobry*, [1974] 2 *Lloyd's Rep.* 308, at 316.

The standard of care against which fault is measured is based on three broad principles:

- i General concepts of prudent seamanship and reasonable care;
- ii Statutory and regulatory rules on the movement and management of ships;
- iii Traditionally accepted customs and usages.

The burden of proof rests upon the party that asserts a cause of action against the other party and when both ships have suffered damage, each party has the burden of proving a cause of action against the other.

Liability for collision can be imposed even if there is no breach of any statute or convention. However, the most frequent basis for collision liability is the violation of internationally recognised regulations or a local regulation such as a local harbour bye-law.

### 6.2.1 COLREGS

When assessing fault, courts have traditionally been guided by a widely accepted set of international rules for the conduct of vessels at sea that has been in existence since the end of the 19th century. A major revision of such rules was undertaken by the International Maritime Organization (IMO)<sup>14</sup> in 1972, which produced the International Regulations for Preventing Collisions at Sea, 1972, more widely known as 'the COLREGS.' These Rules are applicable "to all vessels upon the high seas and in all waters connected therewith"<sup>15</sup> and have been accepted by almost all countries.

The COLREGS are divided into five parts and have four attached annexes.<sup>16</sup> Part A, Rules 1-3, deals with General Principles; Part B, Rules 4-19, contains the Steering and Sailing Rules, of special relevance in collision matters; Part C, Rules 20-31, governs the lights and shapes that ships must show for identification purposes; Part D, Rules 32-37, sets out the required sound and light signals; and, Part E, Rule 38, contains information about exempted vessels.

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<sup>14</sup> See Chapter 22.2 (Maritime Regulation and Compliance).

<sup>15</sup> States are permitted to make specific rules for harbours, rivers, lakes, roadsteads and inland waterways connected to the high seas, but such rules should comply as closely as possible with the main rules. In many states the COLREGS also apply to inland waters. However, it should be noted that this is not so in the case of North American inland waters. For more detailed commentary see the *Gard Handbook on P&I Insurance*, 5th edition Chapter 9, p. 171-172.

<sup>16</sup> COLREGS Annex I deals with the positioning and technical details of lights and shapes; Annex II deals with additional signals for fishing vessels fishing in close proximity; Annex III provides technical details of sound signal appliances; and, Annex IV lists the various distress signals.

It should be noted that, although the COLREGS were not designed or intended for establishing liability, fault or damages, the breach of these Rules, nevertheless, leads in most cases to the finding of fault or negligence that has been discussed in Chapter 6.2 above. It is particularly important to note that Rule 2 of the COLREGS provides that, whilst a breach of the Rules may demonstrate negligence, adherence to the Rules does not in itself mean lack of negligence or lead to exoneration from liability.

Mariners are expected to have very specific knowledge of the COLREGS and any breach of these Rules will always provide *prima facie* evidence of negligence. This is especially so in cases where a breach of the Steering and Sailing Rules appears to have occurred. Important examples are:

- i Look-out (Rule 5): Many collisions occur because of a lack of a proper look-out. This has become especially problematic in the case of modern vessels and smaller crews. Nevertheless, the law does not make allowances for this and has interpreted a proper lookout to include: (a) Visual look-out; (b) Aural look-out; and (c) Intelligent interpretation of data received from electronic navigational aids on board, at sea and ashore.

The number of persons that are necessary to constitute a proper look-out will depend on a number of factors, such as the size of the vessel, the degree of visibility, and the density and speed of traffic.

Monitoring or observing a radar screen, without proper plotting, does not constitute a proper look-out. Indeed, there have been a number of so-called 'radar-assisted collisions' that have occurred as a result of the fact that undue reliance has been placed on radar information to the exclusion of other information.

- ii Safe speed (Rule 6): Many collisions occur because vessels operate at speeds that are considered unsafe under the prevailing circumstances. Unsafe speed usually means excessive speed, but not always so since there may be circumstances when an increase in speed may be a safe manoeuvre.

There is no one rule to define what is or is not a safe speed. The term 'safe' is relative; the vessel must proceed at a speed that is considered safe for each particular circumstance, i.e. clear visibility on the open ocean; clear visibility in restricted waters or in dense traffic; in restricted visibility; with restricted draught etc. It is sometimes asserted that being able to stop a vessel in half the range of visibility may be a safe speed, but this cannot be relied on as a rule of law.

- iii Risk of collision (Rule 7): Many collisions occur because vessels have failed to appreciate or determine that a risk of collision has developed. Careful observation is transformed into inference and prediction as to what may occur. Vessels are required to be constantly aware of the risk of collision and to determine, in the presence of other vessels, if such a risk exists. This determination must be made through all means available; i.e. look-out, electronic plotting, bearings etc.
- iv Action to avoid collision (Rule 8): In many cases collisions occur due to the fact that inadequate or incorrect action has been taken to avoid collision. Rule 8 requires avoiding action to be taken early, to be positive and consistent with good seamanship. In many cases a timely and substantial course alteration alone may be sufficient.
- v Traffic separation schemes (Rule 10): Although Traffic Separation Schemes (TSS) and Vessel Traffic Management Systems (VTMS) are specifically designed to separate vessels in order to avoid collisions, many collisions still occur within or close to such systems, either because vessels do not obey the COLREGS, which still apply fully within such systems, or because they simply navigate improperly within such systems based on fixed assumptions in the face of changing data.
- vi Overtaking (Rule 13): This is a surprisingly frequent cause of collision. It is clear that overtaking vessels must keep out of the way of vessels being overtaken. If doubt exists, the faster vessel should assume that she is overtaking.
- vii Head-on situation (Rule 14): A case of two vessels colliding head-on has the potential for the most serious damage. It occurs too frequently, even when relatively minor avoiding action could have prevented the collision. The expression in the Rule of "*vessels meeting end-on or nearly end-on*", has been interpreted to mean opposing courses that are within some six degrees of each other. The Rule indicates that it is the direction of the vessel's head and not the vessel's course that must be used to determine if an end-on situation exists.
- viii Crossing situation (Rule 15): Vessels crossing at sea are also often involved in collision situations. This is despite the very clear Rule that requires the vessel that has the other on her starboard side, to 'give way', i.e. to keep clear. This can be achieved by (a) altering course to starboard so as to pass astern of the other vessel; (b) reducing the speed sufficiently to allow the other vessel to cross ahead; or (c) making a full-turn alteration to port. In some cases, doubt may arise as to whether there is a crossing or overtaking situation, which will depend on the degrees of the respective vessels' courses to each other.

- ix** Action by 'stand-on' vessel (Rule 17): This Rule sets out proper navigation rules for different stages of 'an emerging collision situation': (a) At long range and before risk of collision exists, both vessels are free to take any avoidance action; (b) When risk of collision first emerges, the give-way vessel is required to take early and substantial action to achieve a safe passing distance, whilst the stand-on vessel must keep her course and speed; (c) When it becomes apparent that the give-way vessel does not take appropriate action in accordance with the Rules, the stand-on vessel is required to give sound signal as per Rule 34(d) and is permitted to take action to avoid collision by her action alone, but must not alter course to port to avoid another vessel on her port side. Meanwhile, the give-way vessel is not relieved of her obligation to keep out of the way; and, (d) When collision cannot be avoided by the give-way vessel alone, the stand-on vessel is required to take such action as is most appropriate to avoid collision.
- x** Responsibilities between vessels (Rule 18): Many collisions occur because vessels do not understand the responsibilities that they have to each other, especially when hampered vessels are involved.
- xi** Conduct of vessels in restricted visibility (Rule 19): This has always been, and continues to be, the most serious cause of collision and is usually caused by excessive speed and/or improper look-out in restricted visibility. The Rule applies only to vessels "*not in sight of one another*" and applies not only when navigating in restricted visibility but also when doing so in the vicinity of such conditions. Observing another vessel by radar is not considered to be "*in sight of ...*" for the purposes of the Rules. Excessive speed in restricted visibility, regardless of circumstances, is never acceptable.

Whilst COLREGS does not contain rules regulating radio (VHF) communication between ships on a collision course, case law has numerous examples of so-called 'VHF aided collisions', which refers to the danger of inadequate communication between ships on a collision course in the time leading up to the collision.

The vessel that creates a situation of danger is generally assigned a higher proportion of fault than a vessel that fails to extricate itself from the dangerous situation that has been so created and the apportionment of fault is a qualitative rather than a quantitative exercise, i.e. it is not a matter of adding up the faults on both sides.

### 6.3 Liability

Traditionally, the law of many countries stipulated that when loss or damage was caused by the joint action of two or more negligent parties, the innocent party was entitled to claim his entire loss from one or all of the negligent parties leaving the negligent parties to claim contribution from each other thereafter. However, the disparity between the laws of different countries made it difficult to predict the outcome of collisions that involved multiple interests from multiple countries. Therefore, the issue was considered by the Comité Maritime International (CMI)<sup>17</sup> in depth at the beginning of the 20th century resulting in The International Convention for the Unification of certain Rules of Law with Respect to Collision, 1910 (The 1910 Collision Convention) which has been widely adopted throughout the world and which still remains in force as the basis of regulation of collision liability. The USA is not a signatory to the 1910 Collision Convention, but follows the same principles with some exceptions.<sup>18</sup>

#### 6.3.1 The liability of Colliding Ships to each Other and to Personnel, Cargoes and Other Property that is Carried on one or more Colliding Ships under the 1910 Collision Convention

Article 4 of the 1910 Collision Convention provides that when cargo or other property belonging to third parties is lost or damaged as a result of a collision, each ship is liable only for that proportion of the loss or damage that can be attributed to its fault. However, if the collision results in death or personal injury, each ship that is at fault is jointly and severally liable in full for such claims without prejudice to the right of a party that has paid more than its proportion of blame to recover contribution from the other party or parties at fault for any sums that it may have paid in excess of that proportion.

Therefore, in a collision between ship A and ship B, if ship A is 70 per cent to blame and ship B is 30 per cent to blame, ship A will bear 70 per cent of the property claims that may be brought by the ship B interests and ship B will bear 30 per cent of the property claims that may be brought by the ship A interests. Such liabilities will then be set-off against each other and payment of the residual sum will be made by the one ship to the other.<sup>19</sup> However, if the collision resulted in death or personal injury on ship A, ship A and ship B are jointly and severally liable for 100 per cent of such claims. If ship A pays such claims in full then ship A is entitled to claim 30 per cent of such payment from ship B whereas if ship B pays such claims in full it is entitled to claim 70 per cent of such payment from ship A.

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17 See Chapter 22.2 (Maritime Regulation and Compliance).

18 See Chapter 22.4.1 (Maritime Regulation and Compliance).

19 For a specific example see the Case Study in Chapter 6.10 below.

In very exceptional circumstances<sup>20</sup> it may not be possible to establish the degree of fault (sometimes referred to as 'inscrutable fault'), or a collision may occur where nobody could be said to have been at fault, e.g. if the collision is caused by an inevitable accident.<sup>21</sup> In both cases, the Convention provides that the loss shall 'lie where it falls', i.e. each side shall bear its own damages and neither shall have a claim against the other.

### 6.3.1.1 Liability in Respect of Cargo

Article 4 of the 1910 Collision Convention provides that each ship is liable to each other for that proportion of cargo claims that can be attributed to its proportion of fault for the collision.<sup>22</sup> However, it is necessary to distinguish between claims that may be brought by cargo interests against its carrying ship and claims that may be brought against the non-carrying ship.

In a collision between ship A and ship B where ship A is 70 per cent to blame and ship B is 30 per cent to blame, the cargo on ship A has a choice. It can either seek to recover 100 per cent of its loss from the carrying ship A under the contract of carriage, or it can choose to make claims against both ships. If it chooses to sue the carrying ship A, that claim will normally be subject to contractual terms contained in the relevant contract of carriage. Therefore, when cargo is carried under contracts of carriage that are subject to the Hague or Hague-Visby Rules or to domestic rules of law that are based on those Rules (which is usually the case), the carrier may be able in most circumstances to rely on the negligent error in navigation exception in Article IV Rule 2 (a) of the Rules as a defence to the claim. On the other hand, if the cargo on ship A chooses to bring a claim against ship B in tort, that claim is not subject to any contractual defences since there is no contract between the cargo on ship A and ship B. However, under the 1910 Collision Convention, the claim against ship B can only be made for that ship's proportion of blame for the collision. Therefore, the cargo on ship A can only recover 30 per cent of its loss from ship B and is unable, because of the 'error in navigation' defence, to recover the remaining 70 per cent from ship A.

The position may be different if the owners of the cargo on ship A are able to prove that the loss or damage was caused by the failure of ship A as carrier to exercise due diligence to make the ship seaworthy before and at the commencement of the voyage (e.g. due to the incompetence of the officers and navigators) since, in such circumstances, the carrier may not be able to rely on this defence.<sup>23</sup> Similarly, if

<sup>20</sup> Article 2. One example might be a collision on the high seas that results in the sinking of both ships with all hands in circumstances in which it is not possible to establish the cause of the collision.

<sup>21</sup> For example, when two ships at anchor break loose and collide as a result of a tsunami.

<sup>22</sup> The position is different under US law pursuant to the 'innocent cargo rule' that is considered in Chapter 6.3.2.1 below.

<sup>23</sup> For more detailed commentary see Chapter 3.2.9.2.1(Cargo Claims).

the contract of carriage is governed by the Hamburg Rules or the Rotterdam Rules (if and when in force) or by domestic rules of law based on those Rules, the error in navigation defence is not available, in which case, the cargo on ship A may be able to recover 100 per cent of its loss from ship A which would then include such payments as part of its claim against the other ship, and recover from ship B 30 per cent of the claim pursuant to the proportional fault rule.

The carrier may also be entitled to limit his liability for claims brought by the cargo that is carried on his ship pursuant to the Hague, Hague-Visby or Hamburg Rules or domestic rules of law (whichever may apply to the contract of carriage)<sup>24</sup> and/or pursuant to any relevant global limitation convention.<sup>25</sup>

Therefore, a cargo claimant will normally have to consider the terms of the relevant contract of carriage carefully before deciding how best to pursue his claim.

#### **6.3.1.2 Liability in Respect of Death or Personal Injury<sup>26</sup>**

Where a collision causes personal injury or death, each ship is jointly and severally liable in full for such claims without prejudice to the right of a vessel that has paid more than its proven proportion of blame to recover contribution from the other vessel or vessels at fault according to the proportion of blame that can be attributed to the other ship. This principle is enshrined in Article 4 of the 1910 Collision Convention and also applies in the USA.<sup>27</sup>

However, for similar reasons to those discussed in Chapter 6.3.1.1 in relation to cargo, it is necessary when considering such claims to draw a distinction between claims that affect passengers that are carried on board pursuant to a contract (e.g. passengers on a ferry or a cruise liner) and claims that affect other personnel (e.g. crew members, stevedores, repairers etc.) whether or not they are carried on board.<sup>28</sup>

Liability for causing death or personal injury to a passenger that is carried pursuant to a contract is governed by the Athens Convention on the Carriage of Passengers and their Luggage by Sea 1974 (The Athens Convention),<sup>29</sup> Article 1.4 of which defines a passenger as:

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24 For more detailed commentary see section Chapter 3.2.9.4 (Cargo Claims).

25 The Hague, Hague-Visby and Hamburg Rules all provide that the package limitation rules contained therein do not prevent the carrier from also relying on global limitation rights should this be necessary.

26 For more detailed commentary see Chapter 11 (People Claims).

27 See Chapter 6.3.2.

28 For more detailed commentary see Chapter 16 of the *Gard Handbook on P&I Insurance* and Chapters 11.2.2 and 11.2.3 (People Claims).

29 For more detailed commentary on the Athens Convention and the 2002 Protocol thereto see Chapter 11.3.2 (People Claims).



“... any person carried in a ship:

- (a) under a contract of carriage; or
- (b) who, with the consent of the carrier, is accompanying a vehicle or live animals which are covered by a contract for the carriage of goods not covered by this Convention.”

Article 14 of the Athens Convention expressly provides that any passenger (or next of kin) who wishes to bring a claim against the carrier for personal injury or death must do so pursuant to the rules of the Convention and that such claims cannot be brought against the carrier on any other basis. However, the Athens Convention does not prevent such claims being brought against the non-carrying vessel if the negligence of the latter has caused or contributed to the collision.<sup>30</sup> Therefore, where the collision has been caused by the fault of both ships, the claimant has a choice and in making that choice the claimant may need to consider the following:

- Proving fault. Whereas it is necessary to prove fault if a claim is to be brought against the non-carrying vessel, a carrier is presumed to be at fault under Article 3 of the Athens Convention if the injury or death is caused by a collision incident;
- Jurisdiction. The jurisdiction for claims against the non-carrying ship may be uncertain whereas Article 17 of the Athens Convention gives the claimant a discretion to bring his claim against the carrier: (i) where the defendant is domiciled or carries on business, or (ii) where the contract was made, or (iii) in the country of departure or destination specified in the contract, or (iv) where the claimant is domiciled if the defendant carries on business in that country;
- Limitation of liability. Individual claims for personal injury and death are subject to limitation under the Athens Convention<sup>31</sup> whereas this form of limitation does not apply to individual claims that are brought against the non-carrying ship. However, the non-carrying ship may be entitled to limit liability in respect of such claims under whichever global limitation convention that may be applicable;<sup>32</sup>
- Security. If security is required to support a claim against the non-carrying ship then it will be necessary to arrest or to threaten the arrest of that ship or a sister-ship to secure whatever funds the value of those ships can provide. However, if a claim is brought against the carrier, then (following the entry into force of the 2002 Protocol to the Athens Convention) such claim may be brought directly against the provider of the guarantee for the carrier’s liability under the Convention, which in most circumstances will be the P&I club.<sup>33</sup>

30 For a similar situation affecting cargo claims see Chapter 6.3.1.1 above.

31 This form of limitation is similar to the package limitation that applies to individual cargo claims under the Hague, Hague-Visby, Hamburg and Rotterdam Rules. See Chapter 3.2.9.4 (Cargo Claims).

32 See Chapter 6.5 below.

33 A similar form of guarantee (the so-called FMC Section 2 Guarantee) is provided pursuant to US law in the case of ships that operate in the USA.

However, should the claimant decide to bring his claims against the carrier, there is nothing to prevent the carrier from seeking recourse from the other colliding vessel in accordance with the principles outlined above.

### 6.3.1.3 Liability to Other Parties

The apportionment of liability under the 1910 Collision Convention is only binding as between the ships that are involved in the collision and the owners of the cargo or any other property that is on board the ships. Therefore, the convention does not restrict the traditional right of the owners of any other ship or property or any other personnel that have suffered loss or damage or injury as a result of the collision, to sue either of the colliding ships jointly or severally for its entire loss. For example, if ship A has been soiled by bunker oil that has escaped from ship B after ship B has been involved in a collision with ship C, ship A may claim a full recovery from either ship B, or from ship C, or from both ships provided that there is some degree of fault on the part of both ships.<sup>34</sup>

## 6.3.2 Collision Liability under US law

The United States has not ratified the 1910 Collision Convention but in 1975 the US Supreme Court ruled that the similar proportional fault rules should be applied under US law.<sup>35</sup> However, there are still substantial differences between US law and the 1910 Collision Convention in relation to claims for cargo loss or damage resulting from both-to-blame collision cases. In such cases, the so-called 'innocent cargo rule' prevails in the USA.

### 6.3.2.1 The 'Innocent Cargo' Rule in the USA<sup>36</sup>

When cargo is lost or damaged as a result of a collision that has been caused by the negligence of both ships, the 'innocent cargo' rule provides that the cargo interests are entitled to recover 100 per cent of their damages from the non-carrying vessel, even if this vessel is only 1 per cent to blame. In such a case, the non-carrier who pays, or is obliged to pay, such cargo claims, has the right to include such payments as part of its claim for damages against the other colliding ship for subsequent apportionment between them in accordance with their respective proportions of fault for the collision. This leads to the anomaly that the carrier who satisfies the claims of the non-carrying ship will indirectly bear a greater proportion of the loss suffered by cargo that he has carried than he would have done if such cargo

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34 Article 5 of the Bunker Convention, 2001 states the following: "When an incident involving two or more ships occurs and pollution damage results therefrom, the shipowners of all the ships concerned, unless exonerated under article 3, shall be jointly and severally liable for all such damage which is not reasonably separable."

35 *United States v Reliable Transfer Co*, 421 U.S.39, S.Ct.1708, 44 LEd. 2d, 251, 1975 AMC 541.

36 See also Chapter 9.3.1 of the *Gard Handbook on P&I Insurance*, 5th edition.

interests had brought their claim against him, rather than against the non-carrying ship, and he could have relied on the error in navigation defence in the contract of carriage of the cargo.

### 6.3.2.2 The Both-to-Blame Collision Clause

In order to avoid such disproportionate indirect liability, carriers will normally include a Both-to-Blame Collision Clause in their contracts of carriage which provides as follows:

*"If the ship comes into collision with another ship as a result of the negligence of the other ship and any act neglect or default of the master, mariner, pilot or the servants of the carrier in the navigation or management of the ship, the owners of the goods carried hereunder will indemnify the carrier against all loss or liability to the other or non carrying ship or her owners in so far as such loss or liability represents loss of, or damage to, or any claim whatsoever of the owners of the said goods, paid or payable by the other or non carrying ship or her owners to the owners of the said goods and set off, recouped or recovered by the other non carrying ship or her owners as part of their claim against the carrying ship or her owners as part of their claim against the carrying ship or carrier. The foregoing provisions shall also apply where the owners operators or those in charge of any ship or objects other than, or in addition to the colliding ships or objects are at fault to a collision or contract."*

In brief, this clause provides that the cargo owners will indemnify the owner of the cargo-carrying vessel against any liability that they will incur for such claims in the context of their overall liability to the other vessel which exceeds the proportionate fault of the cargo-carrying ship.

The Both-to Blame Collision Clause has been declared invalid and unenforceable in the United States when included in bills of lading but may be considered valid if the contract of carriage is a voyage charterparty.<sup>37</sup> Nevertheless, the clause is invariably included in contracts of carriage of all types since it is usually considered to be valid and enforceable in other jurisdictions. Furthermore, the Rules of most P&I clubs specify that cover may not be available if the assured does not include the clause in their contracts of carriage.<sup>38</sup>

<sup>37</sup> See Chapter 9.3.1 of the *Gard Handbook on P&I Insurance*, 5th edition.

<sup>38</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 55 (Terms of Contract)).

## 6.4 Recoverable Damages

When considering the amount of damages that a ship is entitled to recover from another colliding ship it is necessary to consider two separate questions:

- 1 What items of loss or damage qualify in principle as part of the claim? and
- 2 What proportion of that claim is recoverable from the other ship?

This Chapter will consider the first question as the second question has already been discussed in Chapter 6.3 above. However, it should always be remembered that although a claimant may be entitled to include the items discussed below as elements of recoverable damages which can be included in his claim against the other colliding ship, he will only be entitled to recover that proportion of the overall claim that represents the other ship's proportion of blame for the collision, i.e. if ship A is 70 per cent is to blame for the collision and ship B is 30 per cent to blame, ship A can only recover 30 per cent of its damages from ship B and Ship B can only recover 70 per cent of its damages from Ship A.

Most systems of law award damages not only in respect of the loss or damage that has been caused to the ship itself but also by way of indemnity in respect of the liability that the ship may have incurred to third parties as a result of the collision (such as, for example, liability to third party claimants as a result of the spillage of oil following a collision.) Damages are normally awarded pursuant to the principle that the injured party should, whenever possible, be restored to the same financial position that he was in before the occurrence of the relevant event. Therefore, if a vessel is lost as a result of the fault of another vessel, the owners of the lost vessel are entitled to claim for its market value, if there is one.<sup>39</sup> However, if the damage is partial, the owner is entitled to claim for the reasonable cost of restoring the vessel to the condition that it was in before the collision even if this is greater than the depreciation in the ship's market value as a result of the collision (the technical term being *restitutio in integrum*).

The owner is also entitled to include as part of his claim any additional losses that he has incurred as a result of the collision which are deemed to be foreseeable. If the ship has been lost this may include the cost of wreck removal or the cost of raising its cargo or preventing or cleaning-up pollution. However, if the ship is repairable then the additional costs may include the cost of salvage or towage, drydocking, pilotage, survey fees etc. The claim may also include any income or trading profits that have been lost as a result of the incident.

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<sup>39</sup> In the case of warships or other public service vessels, where there is no market value, its value must be established in some other way, e.g. by a formula based upon reconstruction cost, less depreciation.

In general, it is only those losses that arise as a “*direct and immediate result of the collision*” that may be claimed. Therefore, if a shipowner has taken the opportunity whilst repairing the collision damage to also repair damage that has been caused by a preceding and separate event, it will be necessary in many cases to distinguish and separate the repair costs. However, if the predominant reason why the ship has been taken to the repair yard was to repair the collision damage, then deduction will normally be made only for any additional costs, time and expense that can be clearly attributable to the other repairs. Nevertheless, difficult issues can often arise when attempting such distinctions.

Difficult issues can also arise when considering losses that are foreseeable (and therefore, normally recoverable) and losses that are too remote (and therefore, not normally recoverable). In one sense, it can be said that there may be many losses that would not have arisen but for the collision. However, the law of most countries recognizes that for public policy reasons it is necessary to draw a line between losses that should have been foreseeable to the guilty party as a natural consequence of his actions, and losses which, although the result of the collision, are too remote in terms of causation to be considered as the natural and foreseeable consequence of the negligence. For example, a claimant may argue that, as a result of the collision, he has lost the opportunity to conclude a valuable charterparty that he was in the process of negotiating, and therefore, claims his projected loss of profit in this regard. No general rule can be stated as to whether such a loss would be considered claimable or not. The court that is seized of the case would have to determine the issue based on the particular facts and the applicable rules of law.<sup>40</sup>

A claimant is also expected to mitigate his losses, i.e. to do whatever is reasonably possible to minimise his losses. Therefore, if a party that is claiming damages is deemed by the court to have failed to take reasonable steps to avoid or minimise his liability or loss, it may determine that the party should only recover the liability or loss which would have been incurred if such reasonable steps had been taken.

#### 6.4.1 The Lisbon Rules<sup>41</sup>

Because of the divergent approaches to the recoverability of damages that are adopted by different systems of national law, the CMI promulgated the Lisbon Rules on Compensation for Collision Damage in 1987, in an effort to unify the widely varying methods of assessing damages in collision cases. The Lisbon Rules are neither statutory in form nor intent, but are designed to serve as a set of recommended principles that can be voluntarily adopted by shipowners, insurers and courts, or as model laws by countries.

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<sup>40</sup> See Chapter 6.6 below.

<sup>41</sup> See Chapter 9.2.3 of the *Gard Handbook on P&I Insurance*, 5th edition.

The Rules include a practical set of guidelines for the assessment of damages that are payable in the event of a collision where there is the total or partial loss of a vessel. The Rules also deal with claims for the loss of use of a vessel whilst undergoing repairs, interest, currency exchange and salvage and general average where there is loss or damage to cargo. Although these Rules do not have the force of law they can often be usefully used in negotiations as guidance to what should, and what should not, be recovered. In this respect, the Rules can make a contribution to a more efficient, practical handling of collision claims.

### **6.5 Limitation of Liability**<sup>42</sup>

Collision claims can often be made for very large sums of money. However, the party that is at fault and liable may often be entitled to pay less than the total amount of damages that may be assessed in accordance with the principles discussed in Chapters 6.4 and 6.4.1 pursuant to the doctrine of the limitation of liability.

There are two types of limitation which may apply in collision cases:

- Limitation of individual claims of a defined character; and
- Limitation of all claims of a defined character which arise “*on any distinct occasion.*”

The limitation that may apply in relation to cargo claims that are subject to the Hague, Hague-Visby or Hamburg Rules, or for personal injury or loss of life claims that are subject to the Athens Convention, apply only in respect of claims that are brought under the relevant contract of carriage against the ship that carries the cargo or passengers. Therefore, the owner of the non-carrying ship is not entitled to rely on such limitation rights if individual cargo and/or passenger claims are brought against him by cargo owners or passengers of the carrying ship.

However, the owners of both ships may be entitled in certain circumstances to limit liability pursuant to one of the relevant global limitation conventions which specify that all liability for all claims of a defined character that arise “*on any distinct occasion*” may be limited. In the majority of cases, the right to global limitation will arise pursuant to the provisions of the 1976 Limitation Convention or its 1996 Protocol, or the 1957 Limitation Convention – although most maritime countries have now ratified one of the former two. Some countries (notably the USA) do not apply either convention, but may have domestic rules of law concerning rights to limit liability.

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<sup>42</sup> For more detailed commentary see Chapter 21 (Limitation of Liability) and Chapters 27-30 of the *Gard Handbook on P&I Insurance*, 5th edition.

A detailed commentary on such limitation rights can be found in Chapter 21. However, the key aspects of limitation that are relevant in relation to collision claims are itemised below:

- Article 5 of the 1976 Limitation Convention states as follows:  
*“Where a person entitled to limitation of liability under the rules of this Convention has a claim against the claimant arising out of the same occurrence, their respective claims shall be set off against each other and the provisions of this Convention shall only apply to the balance, if any.”*

In other words, the paying party may limit his liability only in respect of his net liability to the other party after setting off his liability to the other party against whatever liability the other party has to him. If this ‘single net liability’ does not exceed the tonnage-based limit of liability, no limitation will apply;

- Both loss of life/personal injury, property damage and delay in the carriage of cargo or passengers, which arise in consequence of the collision, are claims in respect of which a shipowner has the right to limit liability according to the limitation conventions;<sup>43</sup>
- If, following a collision between ship A and ship B, ship A spills oil, ship B may be entitled to limit its liability for claims brought against it by ship A for the pollution prevention, clean-up and environmental damage claims that it has paid to third party claimants when such payments are included as part of its collision claim against ship B.<sup>44</sup> This is so even if the owner of ship A was not entitled to limit its liability to third parties in relation to the same categories of claim;
- If, following a collision between ship A and ship B, efforts to salvage ship A do not succeed and it becomes necessary to remove the wreck of ship A, ship B may be entitled to limit its liability for claims brought against it by ship A for salvage and wreck removal costs incurred by ship A when such payments are included as part of its collision claim against ship B. This is so even if the owner of ship A was not entitled to limit its liability to third parties in relation to the same categories of claim.

Under the conventions limitation applies to all limitable claims which arise on each distinct occasion. Therefore, if a ship were to have two collisions during the course of a voyage, there would be two distinct occasions and hence the limitation rights would apply to claims arising from each of these occasions.

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<sup>43</sup> Article 2.1. (a) and (b) of the 1976 Convention on Limitation of Liability for Maritime Claims. (LLMC)  
Article 2.1 includes the phrase “whatever the basis of liability may be.”

<sup>44</sup> Article 2.2 of LLMC.

## 6.6 Jurisdiction and Governing Law<sup>45</sup>

Whenever a collision occurs the parties should give early thought to the question of the relevant jurisdiction and governing law. This is because there is no one jurisdiction and law which applies in all countries of the world and the law of individual countries differ. Furthermore, many collisions take place on the high seas where no individual country has jurisdiction. Therefore, the merits of the various claims that may arise as a result of the collision will depend very largely on the law of the forum where these claims are determined. An attempt to cure this difficulty was made in the Collision (Civil Jurisdiction) Convention 1952 but this convention has been adopted by relatively few countries and suffers from the fact that its provisions do not prevent parties from agreeing an alternative jurisdiction. Consequently, the convention has little practical application.

Decisions relating to jurisdiction and law will be largely influenced by the expectation of the parties (based on whatever assessment of fault and damages is possible at an early stage) as to who will be 'the overall paying party' at the end of the day, i.e. who between the parties is likely to be the net payor. That 'paying party' would normally prefer the claims to be subject to a law that allows liability to be limited and to be heard by courts that are well versed in collision or other admiralty cases. The 'receiving party', on the other hand, can often be expected to take the opposite view in order to maximise the prospects of a full recovery from the 'paying party.' Finally, both parties may share an interest in resolving their differences in a forum where the litigation process can be expected to proceed fairly and expeditiously, and where litigation costs are reasonable and can be reasonably estimated in advance. It is also true that litigating in a jurisdiction where the outcome is predictable is often helpful in achieving an amicable settlement, which is often in the interests of both parties to a collision.

The parties may also distinguish between jurisdiction for consideration of the merits of the claim and jurisdiction for limitation of the claim. The two issues are different. The question of limitation does not normally arise unless and until it has been established that the person seeking to limit is liable for the relevant claims. In some circumstances, however, a court may be prepared to assume that there is liability in order to consider whether the party liable can limit that liability. This is normally done if it is considered that a limitation decree may assist the parties to reach an early settlement and thereby, avoid incurring substantial and unnecessary costs in establishing liability. Traditionally, a person who seeks to limit his liability for qualifying claims is entitled to choose the jurisdiction where to do so. Therefore,

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<sup>45</sup> For more detailed commentary see Chapter 19 (Law and Jurisdiction).



in some cases liability and limitation are determined in one jurisdiction whereas in other cases the liability is determined in one jurisdiction and limitation in another jurisdiction.

Overall, each party may try to secure the jurisdiction which serves its interests best and may try to move quickly to do so since, in many instances, the party who establishes jurisdiction first may have a tactical advantage. The court first seized in such a case may rule that it has exclusive jurisdiction to rule over the dispute between the parties, and this may be accepted (although it is not a certainty) by a court subsequently seized, which would, but the ruling of the court first seized, have considered to be competent to rule over the dispute. This process is called 'forum-shopping.' In many cases, however, parties to collision cases prefer to conclude agreements<sup>46</sup> relating to law and jurisdiction.

## 6.7 Criminal Charges and Penal Proceedings

In some serious collision cases, criminal charges may be brought against various people that may be involved, especially if personal injury, loss of life, pollution or other damage to public property is the result. In such situations, the master, crew members and other persons<sup>47</sup> responsible for the conduct of the vessel (e.g. the pilot) may be alleged to have committed a criminal offence. However, the countries that have ratified UNCLOS (1982) have agreed that no penal proceedings may be commenced against the navigating officers of a vessel except before the authorities of the vessel's flag state or the state of which such persons are nationals.<sup>48</sup>

It is less likely that such penal proceedings may be brought against the shipowner personally, or his *alter ego* in the higher management of the organisation responsible for the operation of the ship. However, the responsible authorities of the country where the collision has occurred may impose fines or penalties on one or both of the owners of the colliding ships for violations of navigation rules or rules relating to safety at sea.<sup>49</sup> In some cases, such fines or penalties may be substantial. However, the rules of the International Group P&I clubs specify that P&I cover is available only if the relevant association exercises its discretion to provide cover.<sup>50</sup>

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46 The City of London Admiralty Solicitors Group has created a template *Collision Jurisdiction Agreement* which use has become widespread in the industry.

47 It would be more unusual, but not impossible, for the shipowner personally, or his *alter ego* in the higher management of the organisation responsible for the operation of the ship, to be accused of a criminal offence.

48 UNCLOS, Art. 97(1).

49 See Chapter 22.3.1.1 (Maritime Regulation and Compliance).

50 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 47.2 (Fines)).

## 6.8 Relevant Insurances<sup>51</sup>

The following claims normally arise as a result of a collision:

- Property claims;
- Liability claims;
- Delay claims.

Claims that are the result of collisions often involve several different types of insurance cover, such as Hull and Machinery (H&M), Hull Interest / Increased Value (IV) insurance, P&I etc. Furthermore, the terms of any one particular type of insurance cover may differ, particularly in the case of cover for collision liability risks. Therefore, it is important to have a clear idea of which claims are covered by which insurance, particularly since the assured has the duty to notify the relevant insurer promptly of any claim and may prejudice rights of recovery under the terms of insurance if he does not do so.

The assured should also be aware that if he is indemnified by the relevant insurer, the insurer is entitled to exercise his rights in subrogation. Subrogation is the right that the insurer has to 'step into the shoes of the insured' when a loss has been paid and to take over all rights that the assured may have to claim against a third party that has caused the loss or damage. For example, if the H&M insurer has settled a claim that has been brought by an assured shipowner for damage to the ship's hull as a result of a collision, the insurer is entitled to take over the right of the shipowner to bring a claim against the other colliding vessel to recover that proportion of the damage that can be attributed to the other ship's negligence. Therefore, the assured has a duty to ensure that he takes whatever reasonable steps that may be necessary to safeguard the insurer's subrogated rights and runs the risk of prejudicing his insurance cover if he does not do so.<sup>52</sup>

### 6.8.1 Hull and Machinery Insurance<sup>53</sup>

#### 6.8.1.1 Cover for Loss of, or Damage to, the Insured Ship

Compensation for the financial loss that is incurred by a shipowner as a result of damage to, or loss of the ship<sup>54</sup> caused by a collision is normally payable by the ship's Hull and Machinery (H&M) insurers. Typical items of compensation include

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51 See also Chapter 26 (The Structure of Marine Insurance), Gard News 178 *The Interface between Hull and Machinery Insurance and P&I from the P&I Claim handler's perspective and Guide to Hull Claims* by Richards Hogg International which can be accessed at <http://www.rhlg.com/pdfs/guidetohullclaims0703.pdf>.

52 For further commentary see Chapter 25.5 (The Fundamental Principles of Marine Insurance).

53 See also Chapter 26.3.1.1 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 71 (Other Insurances)).

54 For these purposes 'ship' normally includes the hull and the machinery, equipment, spare parts, bunkers and lubrication oil.

the cost of damage surveys, the ship's share of salvage<sup>55</sup> and general average<sup>56</sup> expenses, the cost of any temporary repairs that may be needed in order to obtain the approval of the ship's classification society for moving (possibly towing) the ship to a yard for permanent repairs, the cost of permanent repairs including harbour and docking fees, as well as any legal costs and expenses that may be necessary to assess potential collision liability and to take action to secure rights of compensation from the other ship.

In the case of the actual or constructive total loss<sup>57</sup> of the insured ship, the H&M insurers will normally pay the sum insured to the party or parties that have been nominated by the assured as the parties that are entitled to receive such compensation.<sup>58</sup> The limit of compensation will normally be specified and agreed in the policy (i.e. the insured value). However, the insured value may sometimes prove to be insufficient cover for the assured since the market value of the ship may be greater than the insured value. For such reasons, the shipowner will usually take out additional cover in the form of Increased Value (IV) Insurance.<sup>59</sup>

#### **6.8.1.2 Collision Liability Cover**

Shipowners will normally require cover not only for the loss of, or damage to, the ship as a result of a collision but also for the liability that the shipowner may incur to the owner of the other ship or to other third parties if it can be said that the collision has been caused in full or in part by the assured's fault. However, the manner in which such insurance has been allocated between various insurers has been quite diverse.

In some cases, the shipowner may have placed all collision liability cover with the P&I insurer, in which case the H&M insurers do not cover the collision liability of the assured at all. On the other hand, the H&M insurers may agree to cover such collision liability in full or in part, in which case the H&M insurers will be liable to compensate the assured both in respect of damage or loss to the insured ship and in respect of the liability that the assured has to the other ship. Indeed, in some cases, the collision liability may be greater in financial terms than the sum to which the

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55 If the ship is carrying cargo at the time that the salvage services are rendered, the owners of the cargo are obliged to contribute to the salvage remuneration according to the proportion that the value of the cargo bears to the total property values that have been saved. For further detailed commentary see Chapter 14 (Salvage Claims).

56 The principle described in footnote 55 above also applies in relation to general average, but the time when the valuation is calculated may differ. For further detailed commentary see Chapter 10 (General Average Claims).

57 For more detailed commentary see Chapters 5.3 and 5.4 (Claims for the loss of, or damage to, ship).

58 The ship will frequently be subject to a mortgage that will entitle the mortgagees (i.e. the lenders) to receive whatever proportion of the sum insured that may be necessary to cover the balance of the loan(s).

59 See Chapter 26.3.1.2 (The Structure of Marine Insurance) and Chapter 6.8.1.2 below.

assured is entitled in the event of damage to, or even the loss of, the insured ship. For example, this could happen if the damage to the insured ship is limited, but the insured ship has caused major damage to, or perhaps even the loss of the other ship, and bears a high proportion of fault for the collision.

Whilst the liability of the insurers for collision liability is limited to the sum insured, it must be appreciated that this is a separate and distinct type of cover that does not restrict the right that the assured has to receive indemnification for the loss of, or for damage to, the insured ship. Therefore, the H&M insurers may have to pay one sum insured for the loss of the ship and a further sum insured for the collision liability. In a worst case scenario, they may have to pay three times the sum insured, because a separate sum insured applies to the cost of measures to minimise loss, e.g. salvage.

It is also possible that the sum insured for collision liability under the H&M insurance will prove to be insufficient to cover the total liability incurred by the assured. In such cases, the excess liability may be covered either by the Hull Interest/Increased Value (IV) insurance<sup>60</sup> and/or the P&I insurance.<sup>61</sup>

### **6.8.1.3 H&M Insurers**

H&M insurance can be obtained from various insurers around the world on different terms and conditions. In the majority of cases, the standard terms of insurance will be the Nordic Marine Insurance Plan (NMIP), the English Institute Time Clauses Hulls (ITC Hulls), or American, German, Japanese or French terms.<sup>62</sup> However, the collision cover that is provided by such standard terms differs in some important respects. It is not possible to comment in detail in this publication on each set of terms, but a comparative table demonstrating the collision claims and liabilities that are covered under the most common standard terms, is attached as Annex 1 to this chapter. It is very important to check and understand exactly how the chosen terms affect collision liability to ensure that there is no gap in the insurance cover or – perhaps more likely – no case of double insurance.

Under the NMIP, the H&M insurers cover 100 per cent collision liability, but this does not mean that all potential liabilities are covered since there is no liability cover for loss of life, personal injury or pollution. Therefore, such liabilities need to be covered

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<sup>60</sup> See Chapter 26.3.1.2 (The Structure of Marine Insurance).

<sup>61</sup> See footnote 60.

<sup>62</sup> For further commentary see Chapter 26.3.1.1.1 (The Structure of Marine Insurance).

by P&I insurance.<sup>63</sup> However, unlike the ITC Hulls and American hull terms, the NMIP provides liability cover for removal of the wreck of the other ship if it is lost, as well as for the removal of property on board.<sup>64</sup>

Under the English ITC Hulls terms, the H&M insurers cover  $\frac{3}{4}$ ths of the collision liability, subject to the sum insured. The remaining  $\frac{1}{4}$ th collision liability will usually be covered by the P&I insurer. This divergence of cover can sometimes create difficulties, particularly when it is necessary to provide security to third party claimants. The provision of security in the form of P&I letters of undertaking is widely accepted around the world and is a cheap and effective means to release a ship from arrest. However, where collision liability cover is split between different insurers, the P&I insurer is not normally prepared to provide such security unless it has firstly received counter-security for the  $\frac{3}{4}$ ths liability that is not covered under the P&I terms of entry. However, that proportion of cover may be shared between several H&M insurers that have different credit ratings and who are located in different jurisdictions. Therefore, it may prove difficult in some cases to obtain adequate counter-security in a timely manner. Furthermore, although a Nordic H&M claims leader will often be prepared to provide security on behalf of all H&M insurers as a service to the client, if the H&M insurers do not manage to provide an acceptable guarantee, the assured may yet again be faced with the challenge of providing security by way of a bank guarantee, surety bond or, possibly, even by cash deposit.

Costs incurred in pursuing collision claims will normally be shared between, and covered proportionally, by the relevant insurers and, in the event that there are uninsured losses by the assured himself. However, if uninsured claims are made against the other ship (for example, claims that are below the applicable H&M insurance deductible), such costs are not recoverable from the H&M insurers but may be compensated under the Defence cover if such insurance has been placed by the shipowner.<sup>65</sup>

#### **6.8.1.4 Hull Interest/Increased Value (IV) Insurance<sup>66</sup>**

If a ship is totally lost the sum that is recoverable under the H&M policy may not be sufficient to provide the assured with a complete indemnity since the market value of the ship may be more than the insured value, particularly when market prices are increasing. Therefore, a shipowner may wish to obtain further protection against such an eventuality by obtaining Hull Interest/Increased Value (IV) insurance which

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<sup>63</sup> The H&M insurance covers pollution that is caused to the other ship by collision. Therefore, costs incurred to remove oil from, and to clean the other ship as part of the preparation for repairs will be covered by the H&M insurance if brought as part of the collision claim.

<sup>64</sup> See Annex 1.

<sup>65</sup> See Chapter 6.8.4 below.

<sup>66</sup> See also Chapter 26.3.1.2 (The Structure of Marine Insurance).

provides such additional cover in the event of the total loss of the insured ship (whether it be an actual or constructive total loss). The sum that is insured under a standard IV insurance is usually 25 per cent of the sum insured under the H&M insurance and a standard IV insurance also covers excess collision liability where the sum insured in the underlying H&M insurance proves to be insufficient to cover such liability. The cover that is provided in this regard is also normally capped at 25 per cent of the sum that is insured by the H&M insurance. However, whilst the liability of the IV insurer for collision liability is limited in this way, it must be appreciated that this is a separate and distinct type of cover that does not restrict the right that the assured has under the IV insurance to receive indemnification for the loss of the insured ship.

If the ship's collision liability exceeds the aggregate of the collision liability limits that are insured under the combined H&M and IV insurances, the excess liability will normally be covered by P&I insurance.

### 6.8.2 P&I Insurance<sup>67</sup>

P&I insurance is designed to indemnify the assured member against collision liabilities that either fall outside the scope of cover that is provided by the H&M insurance and/or the IV insurance, or which exceed the aggregate sums insured under those insurances. Consequently, it is important to ensure that the scope of cover that is provided by the relevant H&M and IV insurances is fully understood in order to ensure that the scope of the accompanying P&I cover and, consequently, the assured's risk exposure overall, is fully understood.

The following collision liabilities are normally covered under standard P&I terms, if the H&M insurance for the ship is on standard ITC Hulls terms:

- i Liability for claims for the death of, or injury to, crew members, passengers and others on board the other ship;
- ii Liability for claims for pollution from the other ship;
- iii Liability for, and costs incurred in respect of, the removal of the wreck of the other ship and/or property on board the other ship;
- iv That proportion of the ship's liability for collision damage that is not covered under the ship's H&M insurance (and IV insurance if applicable) or which exceeds the combined limit of those insurances, subject to the ship being fully insured for a sum equivalent to its market value;<sup>68</sup>

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<sup>67</sup> See Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 36 (Collisions with other Ships)).

<sup>68</sup> Pursuant to Rule 71.1.a of the *Gard P&I Rules for Ships*, cover is not available in respect of "... liabilities, losses, costs and expenses which are covered by the Hull Policies or would have been covered had the Ship been fully insured on standard terms, without deductible, for an insured value which is at all times not less than the market value from time to time of the Ship without commitment."

- v The cost of measures that are taken to avert or minimise losses that are covered under the P&I insurance;
- vi Costs incurred in order to pursue or defend claims that are covered under the P&I insurance.

The most extensive form of liability cover that may be available from P&I insurers is the so-called full, or 4/4ths, collision liability cover. If this has been agreed, the P&I insurer will, subject to any agreed excess, cover 100 per cent of the assured's residual liability to the other colliding vessel after the claims of each ship and/or their respective H&M and/or IV insurers have been set off against each other.<sup>69</sup> However, under the English ITC Hulls terms, ¾ths of collision liability is normally placed with H&M insurers whilst the remaining ¼th of such claims and any collision claims that are not recoverable under the H&M insurance are covered by P&I insurers. Finally, under the NMIP and German DTV terms, 4/4ths (i.e. 100 per cent) of collision liability cover is placed with H&M and IV insurers.<sup>70</sup>

### 6.8.3 Loss of Hire Insurance<sup>71</sup>

When ships are damaged as a result of a collision they are likely to have to spend some time in a repair yard or to be out of commission as a result of salvage, towage to the repair yard etc. H&M and P&I insurances do not indemnify the assured against any loss of his own income that may be caused by delay but such loss can be covered under loss of hire (LOH) insurance, e.g. when a ship that is on time charter is off hire as a result of the need for repairs. However, LOH insurers only cover such loss when the ship has suffered physical damage or other accident that would give the assured a right of recovery under the ship's H&M insurance. Furthermore, cover is available only in respect of time that has been lost as a result of physical damage to the ship. Therefore, cover is not available for time lost as a result of other circumstances even if connected to the collision incident, e.g. the ship being detained by authorities or arrested by a claimant.

### 6.8.4 Defence Cover,<sup>72</sup> i.e. Legal and Other Expenses Cover

The legal and other expenses that an assured will normally incur in pursuing or defending claims that arise after a collision will normally be divided between, and covered by whichever insurers (whether H&M, IV, LOH or P&I) wish to pursue or defend such claims. However, if uninsured claims are made against the other ship (such as, for example, claims for freight, hire or demurrage or claims that are below the applicable H&M insurance deductible), such costs are not recoverable from the

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<sup>69</sup> See Chapter 6.3.1 above and the Case Study in Chapter 6.10 below.

<sup>70</sup> See also Chapters 6.8.1.3 and 6.8.1.4 above.

<sup>71</sup> For more detailed commentary see Chapter 26.3.1.3 (The Structure of Marine Insurance).

<sup>72</sup> For more detailed commentary see Chapter 26.3.1.6 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules (Guidance to Part IV Rule 65 (Defence Cover))*.

H&M insurers but may be compensated under the Defence cover if such insurance has been placed by the shipowner. Such cover is offered by most P&I clubs as a separate class of cover but the assured would normally, however, be obliged to bear a proportion of the expenses so incurred (usually 25 per cent).

Most Defence cases are handled directly by in-house lawyers working for the relevant P&I or Defence club who can offer comprehensive claims handling and advisory services in relation to a variety of disputes that arise in connection with the operation of ships. Such in-house lawyers frequently act on behalf of the Member when corresponding and/or negotiating with opponents, and may, in certain circumstances, represent the Member in arbitration proceedings.

### **6.8.5 Cargo Insurance<sup>73</sup>**

In the event of a collision, the owners of cargo are likely in the first instance to make a claim under the relevant cargo policy since, by doing so, they avoid some of the difficult issues that arise were they to claim instead against the carrying and/or non-carrying ship, e.g. the avoidance of exception clauses, limitation of liability, difficult jurisdictions etc. Once the cargo owner has been indemnified by the cargo insurers, such difficulties are then transferred to the cargo insurers in the context of subrogation.

The most common forms of cargo insurance are those that are placed on the basis of standard forms such as the Institute Cargo Clauses (ICC) A, B and C. The relevant ICC forms are incorporated into the marine insurance contract by express reference but the parties may amend the standard terms and it should be remembered that the scope of cover may differ substantially depending on the particular version of the ICC clauses that is chosen.

## **6.9 Claims Management<sup>74</sup>**

Major collision incidents are among the most complex maritime incidents to manage, because they may involve a host of different parties and stakeholders, as well as a multitude of operational, legal and insurance issues. However, not all collision cases are complex. At the other end of the scale are the small, below insurance deductible 'bumps and scrapes' that arise in the normal course of doing business and which are usually settled directly between the parties without the need for much involvement on the part of their insurers or other parties.

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<sup>73</sup> For more detailed commentary Chapter 26.3.3 (The Structure of Marine Insurance).

<sup>74</sup> See also Gard News 173 *Collisions – why do they occur?*



It is invariably necessary in collision cases not only to evaluate the various legal and other issues that are discussed in this chapter but also to quickly analyse and understand the potential issues that may arise, and to plan a good course of action to deal with those issues in a timely fashion. Early notification to, and proper consultation with, expert claims handlers working for the H&M insurer and/or P&I club will assist greatly in planning such a course of action. It is also important that ship board staff follow the recommendations that can be found in the Gard Guidance to Masters.

It is equally important in large cases to retain the services of an expert casualty lawyer at an early stage to obtain advice and assistance particularly in relation to the acquisition and preservation of evidence from the ship and from shore. The ready availability of electronic systems and data means that there are often many sources of evidence (sometimes of an indisputable nature) that may record the events leading up to the collision. However, although such data may provide a good answer to 'what happened', it is still crucial to understand 'why and how it happened', which is why it is important to obtain witness statements from the officers and other crew members that were involved in the navigation, voice recordings of ship to ship or ship to shore communication etc.

Finally, the collision may have caused loss or damage to third parties such as the owners of cargo or death or personal injury to personnel on board or ashore. Therefore, care must be taken to collect together all the relevant contracts and other documents that may be relevant to firstly, evaluate the merits of any third party claims, and secondly, to defend such claims in due course.

It follows that it is likely to take some time in order to obtain all the information that is necessary to form a preliminary view of the relevant events and of the relative blameworthiness of the ships that were involved in the collision. Meanwhile, it will be important for owners and their insurers to make tactical claims management decisions, sometimes based on limited information, concerning issues such as choice of jurisdiction, law and exchange of security for claims. Finally, constructive cooperation with governing authorities will be crucial.

### 6.10 Case Study

Ship A collides with ship B. Ship A is found 70 per cent to blame for the collision whereas ship B is found 30 per cent to blame.

Ship A suffers damage of	USD 3,000,000
Ship B suffers damage of	USD 20,000,000
Cargo on ship A suffers loss and damage of	USD 1,000,000
Cargo on ship B suffers loss and damage of	USD 16,000,000
Total loss and damage to property for both ships	<u>USD 40,000,000</u>

#### Hull claims

Ship A pays to ship B 70 per cent of USD 20 million	USD 14,000,000
Ship B pays to ship A 30 per cent of USD 3 million	USD 900,000
On balance ship A pays to ship B	<u>USD 13,100,000</u>

#### Cargo Claims

Both ships are able to rely on the error in navigation defense under the Hague-Visby Rules in relation to claims that may be brought by their own cargo for loss of or damage to that cargo. Therefore, those cargo interests do not get a full recovery of all claims.

Ship A pays to cargo on ship B 70 per cent of USD 16 million	USD 11,200,000
Ship B pays to cargo on ship A 30 per cent of USD 1 million	USD 300,000

Assuming that ship A has a right to limit liability for property claims to USD 16 million, the claims against ship A's fund would be shared '*pari passu*' as follows:

Claims against ship A:	
Net liability to ship B after set-off	USD 13,100,000
Liability to cargo on ship B	USD 11,200,000
Total claims against ship A	<u>USD 24,300,000</u>

Limitation fund for property claims	USD 16,000,000
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The limitation fund is shared '*pari passu*' as follows:

Ship B hull (13.1/ 24.3 x 16)	USD 8,625,514
Ship B cargo (11.2/ 24.3 x 16)	USD 7,374,486
Total Limitation fund	<u>USD 16,000,000</u>

**ANNEX**

Liabilities covered by Hull Policies – collision with other ships

	English conditions (Institute Time Clauses-Hulls 1983, 3/4ths cover)	Nordic conditions (The Nordic Marine Insurance Plan 2013)	United States conditions (American Institute Hull Clauses)	German conditions (DTV Hull Clauses)
Damage to other vessel and cargo on board the other vessel	√	√	√	√
Loss or damage resulting from entanglement of anchors (no contact between the hulls of the two vessels)	√		√	√
Loss or damage to property (other than cargo) on board other vessel	√	√	√	√
Delay or loss of use of other vessel	√	√	√	√
Collision with another vessel which causes collision between that vessel and another ship	√	√	√	√
Damage to third-party property (other than a vessel)		√		√
Removal of wreck of other vessel or property on same (as consequence of collision)		√		√



## Chapter 7

# Dangerous Goods Claims<sup>1</sup>

### 7.1 Introduction

It is often said that ships are not obliged to carry dangerous goods. However, coal, chemicals, gases etc. are dangerous, and even seemingly innocuous commodities such as grain can be dangerous in certain conditions. Nevertheless, ships carry such goods every day of the year and international trade as we know it would have to stop if ships were not allowed to do so. Therefore, the main thrust of international regulation is not to prevent the carriage of dangerous goods but to ensure that such goods are carried safely and that carriers are given sufficient information to enable them to decide whether or not to carry such cargoes at all, or if they decide to do so, to enable them to take the necessary safeguards.

#### 7.1.1 What is Meant by 'Dangerous'?

Historically, there has been no generally accepted definition of what is meant by 'dangerous goods'.<sup>2</sup> However, the IMO has promulgated many codes that identify and describe cargoes of various types that are known to have dangerous characteristics. For example, the International Marine Dangerous Goods Code (IMDG Code)<sup>3</sup> deals principally with packaged goods and lists those cargoes that are known to be dangerous according to various classifications such as flammability, explosiveness, corrosiveness, toxicity etc., and prescribes minimum standards for labeling, marking, notification, packaging, handling, stowing etc. Similar codes deal with solid bulk cargoes (The International Maritime Solid Bulk Cargoes (IMBC) Code),

1 For more detailed commentary see Chapter 6.45 to 6.62 and 6.88 to 6.98 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007, Chapters 9.6 to 9.35 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008 and paras 10.318 to 10.332 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006.

2 However, Article 32 of the Rotterdam Rules defines dangerous goods as "goods by their nature or character are, or reasonably appear likely to become, a danger to persons, property or the environment."

3 For more detailed commentary see *Thomas' Stowage: The Properties and Stowage of Cargoes* by Capt. G.M.Pepper and Capt. R.E.Thomas, Brown, Son and Ferguson Ltd, 6th edition 2012 and the IMO website at <http://www.imo.org/Publications/IMDGCode/Pages/Default.aspx>.

grain (The International Code for the Safe Carriage of Grain in Bulk (International Grain Code)), chemicals (The International Bulk Chemical Code (IBC Code)) and gases (The International Code for the Construction and Equipment of Ships Carrying Liquefied Gases in Bulk (IGC Code)). These provisions are updated every two years or so and have the force of law under Chapter VII (Carriage of Dangerous Goods) of the Safety of Life at Sea (SOLAS) Convention and the International Convention for the Prevention of Pollution from Ships (MARPOL 73/78)<sup>4</sup> as incorporated into the national laws and statutes of most countries. Breach of these provisions attracts fines under the civil and/or criminal law of such countries and substantial commercial liability either in contract or in tort.

However, the mere fact that a particular cargo does not appear in the IMDG Code list does not necessarily mean that such a cargo is considered to be safe. The question of what is or is not dangerous is a question of fact in each case particularly since 'new' cargoes are often being presented for shipment. Therefore, it is important to understand that a cargo can be dangerous if it poses a threat to:

- human life; or
- any object other than itself; or
- the environment.

Objects other than itself can include the ship, other cargo that is being carried, or shore-based property.

Goods may be 'dangerous' because they are either:

- inherently dangerous (e.g. explosives); or
- have a propensity to become dangerous when shipped. For example, coal was extracted in the 1980s from lakes in Florida and carried by ship to Asia. The coal was perfectly safe in its natural environment but started to self-ignite during the voyage to Asia since it reacted with oxygen in the air for the first time in millions of years.

In the majority of cases, goods are dangerous if they pose a physical threat. However, goods can also be dangerous even if they do not cause a physical threat but, nevertheless, subject the ship, crew, cargo or other property to the risk of detention or extraordinary expenditure if their carriage results in a breach of the law of a country or causes offence to the political sensibilities of a country. The most common examples include breaches of import regulations or government embargoes or political 'blackening'.

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4 For more detailed commentary see Chapter 22.3.2 (Maritime Regulation and Compliance).

## 7.2 The Basis of Liability

### 7.2.1 Criminal Liability

A person who causes dangerous goods to be shipped in breach of the IMDG Code may be in breach of the criminal law and/or the civil or administrative law of different countries and such a breach may attract a substantial fine and possible detention of the ship pursuant to the SOLAS or MARPOL Conventions.<sup>5</sup>

### 7.2.2 Commercial Liability

Breaches may also result in substantial commercial liability. Many charterparties expressly forbid the shipment of certain specific types of goods. In such cases, the mere shipment of such cargoes gives rise to liability.

#### 7.2.2.1 The Need to Notify the Carrier of the Danger<sup>6</sup>

If the charter or other contract either has no express terms forbidding the carriage of dangerous goods or has more general words such as “*No injurious, inflammable or dangerous goods to be shipped*”, a shipper or charterer is not automatically liable if dangerous goods are shipped. However, such parties have the obligation not to ship dangerous goods without first notifying the carrier of the dangerous characteristics of that cargo. The purpose of such notice is to provide carriers with sufficient information to enable them to decide whether or not to carry such cargoes at all, or if they decide to do so, to enable them to take the necessary safeguards. Detailed requirements relating to the content of notices and the manner in which notice should be given is contained in the IMDG Code.<sup>7</sup>

Notice is not required when the carriers know or ought to know of the dangerous nature of the goods in any event. In considering whether the carriers should have the requisite knowledge, the courts recognise that carriers are not expected to have the knowledge of an expert scientist. However, they are expected to avail themselves of all the information that is available to an ordinarily experienced and skilful mariner. In particular, ships are required to have on board updated copies of the IMDG Code and to consult it in detail.<sup>8</sup> The SOLAS Convention also requires ships to have on board Material Safety Data Sheets (MSDS) which describe the hazards of a product and enable users to take the measures that may be necessary for the protection of human health and safety at the workplace, and for the protection of the environment.

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<sup>5</sup> See footnote 4.

<sup>6</sup> See Chapters 6.52 to 6.55 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007, Chapter 9.11 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008 and paras 10.318 to 10.319 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006.

<sup>7</sup> See footnote 3.

<sup>8</sup> It would also be good practise for ships to keep on board updated copies of *Thomas' Stowage: The Properties and Stowage of Cargoes* – see footnote 3.

For example, it would not normally be necessary to inform carriers that coal is combustible. However, if a cargo of coal has a special characteristic which makes it more hazardous than usual (e.g. the pond coal problem discussed above), the carrier should be informed of the additional hazard.

### 7.2.3 Strict Liability<sup>9</sup>

Liability for breach of the duty to notify is strict. Therefore, if the shippers or charterers have a duty to notify the carrier of the dangerous nature of the goods and have not done so, they are liable even if they themselves had no knowledge of the dangerous nature of the goods, or even if they had no means of ascertaining its dangerous nature. The rationale for this seemingly harsh approach is that the law often has to choose in such circumstances between two innocent parties, and the courts have determined that the risk should be borne by the cargo side of the contract of carriage since it is the cargo interests who are more likely to have most knowledge of the characteristics of the cargo.

### 7.2.4 The Relevance of the Hague or Hague-Visby Rules<sup>10</sup>

The Hague or Hague-Visby Rules will normally apply to most contracts of carriage either compulsorily (in the case of bills of lading) or by agreement (in the case of charterparties or sea waybills). Article IV Rule 6 of both the Hague and the Hague-Visby Rules provides that:

*“Goods of an inflammable, explosive or dangerous nature to the shipment whereof the carrier, master or agent of the carrier has not consented with knowledge of their nature and character, may at any time before discharge be landed at any place, or destroyed or rendered innocuous by the carrier without compensation and the shipper of such goods shall be liable for all damages and expenses directly or indirectly arising out of or resulting from such shipment. If any such goods shipped with such knowledge and consent shall become a danger to the ship or cargo, they may in like manner be landed at any place, or destroyed or rendered innocuous by the carrier without liability on the part of the carrier except to general average, if any.”*

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9 See Chapters 6.48 and 85.436 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007 and Chapter 9.15 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

10 See Chapter 85.423 to 85.456 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007, paras 10.320 to 10.332 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006 and Chapter 9.16 to 9.21 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.



The Rules adopt and follow the strict liability approach but provide more specific guidance as to the rights of the parties. Article IV Rule 6 draws a distinction between situations when dangerous goods are carried without or with the knowledge of the carrier.

#### **7.2.4.1 When Dangerous Goods are carried Without the Knowledge of the Carrier**

In these circumstances:

- the carrier is entitled to land or render innocuous or even destroy the cargo as soon as he learns of its dangerous nature;
- the carrier is not liable to the goods' owner for the damage or loss caused to the goods by the action taken by him to avoid or diminish the risk; and
- the shipper is liable to indemnify the carrier against any expenses or damages that he may have suffered as a result of the shipment, whether such damages or expenses result directly or indirectly from the shipment.

#### **7.2.4.2 When Dangerous Goods are carried With the Knowledge of the Carrier**

In these circumstances:

- the carrier is entitled to land or render innocuous or even destroy the cargo only if and when the goods actually "*become a danger to the ship or the cargo*";
- neither party is liable to the other in damages for losses or expenses incurred in rendering the cargo harmless; but
- the parties may have to contribute in general average to losses or expenditure incurred by the other party.

### **7.3 Who is Liable?**

The party who ships goods that are dangerous without giving the necessary notice to the carrier is normally liable either in contract or in tort.<sup>11</sup> Therefore, for the reasons given above, a charterer may be liable for the shipment of cargo under a charterparty even if he is not informed by the shipper of the dangerous nature of the cargo. This is a particular problem in the case of containerised cargo since the container is normally sealed at the shippers' premises but not delivered to the charterers' charge until it has reached the load port which may be a considerable distance away. The charterers are not able to check the contents of the container when it is received by them and therefore, have to rely heavily on the information

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<sup>11</sup> For more detailed commentary on liability in tort see Chapter 14 of the *Gard Handbook on P&I Insurance*, 5th edition and Chapter 3.3 (Cargo Claims).

and documents provided by the shippers when presenting the container to the ship for loading.<sup>12</sup> If that data is incorrect the charterers may incur substantial liability even though they are not personally at fault.

The laws of some countries (for example, the UK) provide that when a bill of lading is transferred from one lawful holder to another (usually pursuant to a contract for the sale of the cargo) the final holder (usually the receiver of the goods) will, on taking delivery of the cargo from the ship, or on making a demand for such delivery, assume the same liabilities under the bill of lading as those assumed by the shipper.<sup>13</sup> Therefore, in some instances, a carrier may have the right to bring claims for loss or damage incurred as a result of the shipment of dangerous goods against the shipper, the charterer or the receiver. The shipowner is likely to bring a claim against whichever party is the most likely to be able to satisfy the claim and that party (if not the shipper) may in turn seek an indemnity from the shipper if the dangerous nature of the cargo has not been properly declared by the shipper even if the shipper is not in fact the manufacturer of the product.

#### **7.4 Limitation of Liability<sup>14</sup>**

Large claims often arise as a result of the shipment of dangerous goods and, in view of the strict liability which is imposed by law, shippers, receivers and charterers often have no defence to such claims. Consequently, they may wish to limit their liability. However, shippers and consignees are not “*persons entitled to limit liability*” under the 1976 Limitation Convention or the 1996 Protocol thereto (or the 1957 Limitation Convention which is still in force in some countries). Furthermore, whilst a charterer is a “*person entitled to limit liability*” under such limitation conventions, charterers are not entitled to limit their liability for damage caused to the vessel as such a claim is not a claim which is “*subject to limitation*” under Article 2 of the 1976 Convention or the 1996 Protocol thereto, or probably, under the 1957 Convention.<sup>15</sup>

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12 Shippers are obliged under SOLAS 74, Chapter VII, Regulation 4 and MARPOL 73/78, Annex III, Regulation 4 to give full and accurate details of the contents of a container in a Multimodal Dangerous Goods form (which can be accessed on the IMO website at <http://www.imo.org/Publications/IMDGCCode/Pages/Default.aspx>).

13 See paras 8.86 to 8.99 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006.

14 For more detailed commentary see Chapter 21.3.3.2 (Limitation of Liability), Chapters 27 to 30 of the *Gard Handbook on P&I Insurance* and pages 18 to 19 of the *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, Inform, 4th edition 2005.

15 For a similar discussion in the context of safe ports see Chapter 13.7 (Safe Ports Claims).

## 7.5 Liability of the Carrier

If the cargo causes loss or damage to other property interests disputes often arise as to whether the loss or damage has been caused by the dangerous nature of the cargo (in which case the shippers or charterers will normally be liable) or by negligence or breach of contract on the part of the carrier (in which case the carrier will normally be liable). Technical evidence is normally crucial to decide that issue but the carrier is not absolved of his separate duty to take care of the cargo simply because the shippers or charters have not complied with their duties. Furthermore, the technical evidence may sometimes conclude that although the cargo was dangerous, the negligence of the crew also contributed to the loss or damage by, for example, not taking the precautions that would normally be necessary to make the ship's holds or tanks fit and safe to receive and carry goods that were not dangerous. In such circumstances, the carrier may find it difficult to escape (at least some) liability for the loss or damage.<sup>16</sup>

It should also be appreciated that if the ship has loaded dangerous cargo and then proceeds to load further cargo for other different shippers in that same hold, the shipowner may be found liable to the owners of the second cargo if that cargo is damaged by the first (dangerous) cargo since the carrier will in effect have offered to carry the second cargo on an unseaworthy ship (i.e. a ship which does not have holds *"which are fit and safe for their reception, carriage and preservation"* pursuant to Article III Rule 1 of the Hague-Visby Rules.) However, if the carrier's own staff have taken reasonable steps to check the safety of the cargo but have been misled by wrong or misleading declarations made by the shipper or the shipper's staff, the carrier may be able to prove that it has exercised due diligence to make the ship seaworthy, and that it is entitled in the circumstances to rely on the defence in Article IV Rule 2 (q) of the Hague or Hague-Visby Rules *"Any other cause arising without the fault or neglect of the carrier or without the fault or neglect of the agents or servants of the carrier."* Furthermore, the carrier should be able to claim an indemnity from the shippers of the first (dangerous) cargo.

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<sup>16</sup> See Chapter 7.8 Case Study 1 below.

## 7.6 Insurances

### 7.6.1 Hull and Machinery Insurance<sup>17</sup>

Claims for physical damage to the ship caused by the carriage of dangerous goods are normally expressly excluded from the P&I<sup>18</sup> cover since they will normally be covered by the shipowner's Hull and Machinery insurers. However, the Hull and Machinery insurers will normally have the subrogated right to take over whatever rights the shipowner may have to claim an indemnity from any third party who may be liable for the shipment of dangerous goods.<sup>19</sup>

Should Hull and Machinery insurers decide to pursue claims against third parties either in their own name or in the name of the shipowner, costs incurred by the shipowner in that respect are normally recoverable from the Hull and Machinery insurers and are, for that reason, excluded from the Defence cover that may be provided by the shipowners' P&I insurers.<sup>20</sup>

### 7.6.2 P&I Insurance

If cargo becomes, or is likely to become, a danger to the ship then the shipowner may have the right under the Hague, Hague-Visby or Hamburg Rules or under the common law to "land" or "destroy" or "render innocuous" the cargo.<sup>21</sup> Therefore, the shipowner may have to incur unexpected and additional handling costs in doing so. The Rules of the International Group clubs normally provide cover for such costs provided that the shipowner does not have the right to recover such costs from any other party.<sup>22</sup>

If such cargo has been loaded without the knowledge of the shipowner, the shipowner is likely to have a right of recourse against either the charterer or the shipper of the goods pursuant to the Hague, Hague-Visby or Hamburg Rules. However, if the goods have been loaded with the knowledge of the shipowner then the shipowner's right of recourse lies in general average.<sup>23</sup> In such circumstances, the shipowner would normally be able to recover cargo's proportion of the expenses from the cargo interests and their insurers and the ship's proportion from their hull and machinery insurers.<sup>24</sup> Therefore, in the majority of cases, P&I insurance is not likely to be relevant except in limited circumstances where for technical reasons, recovery cannot be made from these third parties.<sup>25</sup>

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17 For more detailed commentary see Chapter 26.3.1.1 (The Structure of Marine Insurance).

18 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 63.1a (Excluded losses)).

19 See Chapter 25.5.5 (The Fundamental Principles of Marine Insurance).

20 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 71 (Other insurance)).

21 See Chapter 7.2.4 above.

22 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 35 (Extra Handling Costs)).

23 See Chapter 7.2.4 above.

24 For more detailed commentary see Chapter 10 (General Average Claims).

25 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 41 (General Average)).

### 7.6.3 Cargo Insurance<sup>26</sup>

Cargo insurance is essentially property insurance not liability insurance. Therefore, cargo insurers would not normally insure the cargo owners against any liability that they might have to indemnify the carrier for loss or damage caused by the carriage of dangerous goods.

However, the incident that causes damage to the ship may also cause damage to or the loss of the goods themselves. On the face of it, the standard cargo insurance terms ICC provide cover for at least some of the likely claims since the ICC A terms insure the goods against 'all risks' whereas ICC B and C insure the goods against fire or explosion. However, the various clauses exclude cover when loss or damage has been caused by:

- the wilful misconduct of the Assured; or
- the insufficiency or unsuitability of packing or preparation of the subject matter insured to withstand the ordinary incidents of the insured transit where such packing or preparation is carried out by the Assured or their employees or prior to the attachment of this insurance; or
- the inherent vice or nature of the subject-matter insured.

### 7.6.4 Charterers' Liability Insurance<sup>27</sup>

Charterers can insure their liabilities to third parties resulting from the carriage of dangerous goods under two separate forms of insurance:

- Liability to shipowners for damage caused to the ship (Charterers' Liability for Hull (CLH) or Damage to Hull (DTH)) cover; and
- Liability to other parties such as the owners of other cargo on board, i.e. P&I cover.

Such insurances are normally provided on a fixed premium basis by P&I clubs or by other market insurers. For example, Gard's Comprehensive Charterers' Liability Cover provides cover for the liability of charterers for, *inter alia*:

- Damage to or loss of the ship;
- Damage to or loss of cargo;
- Salvage of the ship or cargo or wreck removal;
- Pollution;
- Shipowners' claims for consequential losses such as demurrage, detention, loss of hire or loss of use, or for an indemnity for any liability that shipowners may have to third parties.

<sup>26</sup> See Chapter 26.3.3 (The Structure of Marine Insurance).

<sup>27</sup> For more detailed commentary see Chapter 26.3.2 (The Structure of Marine Insurance).

Many charterers are traders who take out charterers' liability insurance for protection when it is their responsibility under the cargo sale contract to provide the transportation of the cargo. This would be the case if they were sellers under CIF sales or buyers under FOB sales. However, they may incur liability for damage caused by the carriage of dangerous cargo even if they are not charterers (as may be the case if they are buyers under CIF sales or sellers under FOB sales.)<sup>28</sup> They face difficulties in such circumstances since, not being charterers, they are not able to take advantage of the standard charterers' liability insurances that are available. However, some insurers offer a form of charterers' liability insurance which will give traders protection in such circumstances even if they are not charterers in the particular circumstances. For example, the Comprehensive Charterers' Liability Cover that is provided by Gard can be extended by agreement to provide cover for a charterer or affiliate that is held liable in its capacity as owner of cargo rather than as charterer.<sup>29</sup>

## 7.7 Claims Management

Although shippers have a statutory duty to comply with and to provide all the information that is required by the IMDG Code,<sup>30</sup> the reality of life is that it is the carrier who is likely to suffer if these duties are not complied with. If personnel are injured, or the ship or other property is lost or damaged as a result to the carriage of undeclared dangerous cargo, it is the shipowner or charterer who must respond, at least in the first instance. Furthermore, although there will usually be a right to be indemnified by the shipper, that right may be illusory if the shipper is a small entity of dubious financial standing resident in a 'difficult' location.

Therefore, it is very important that both the cargo and the compulsory declarations that are required from shippers under the IMDG and other Codes are rigorously checked whenever possible before shipment and that if there is any doubt, the cargo should be rejected unless the shippers can produce satisfactory explanations. This is particularly important in the case of containers in view of the fact that the containers are normally sealed when presented to the ship with the result that the contents of the containers cannot be checked. The IMO has also acknowledged that care should be taken by the shippers to verify the weight of the container since, if the weight declared by the shipper is incorrect, container stowage limitations may be exceeded and lashing arrangements may be compromised, which can create serious problems for a vessel, especially in bad weather. If the master has reasonable grounds to doubt the weight provided by the shipper, the relevant

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28 See Chapter 7.2.3 above, Chapter 4.1 (Charterparty Claims) and Chapter 7.8 Case Study 2 below.

29 See, for example, the Gard Comprehensive Charterers' Liability Cover and Chapter 7.8 Case Study 2 below.

30 See footnote 12.

port or coastguard authorities will normally support the carrier's right to weigh containers before agreeing to load them. The carrier should also ensure that the crew are provided with up-to-date hard or electronic copies of the IMDG Code and of the various codes of safe practise and guidances which are issued periodically by the IMO<sup>31</sup> and the ship's P&I club<sup>32</sup> and that the crew do consult such materials when necessary.

Finally, the carrier should ensure whenever possible that he includes in his contracts of carriage any protective clauses that may periodically be recommended by their insurers or by industry bodies.<sup>33</sup>

Any failure by the carrier to engage in such due diligence may not only prejudice his rights to an indemnity from the shippers but also his rights under the relevant insurances.

## 7.8 Case Studies

### Case Study 1<sup>34</sup>

An explosion took place in the no. 3 hold of the ACONCAGUA causing widespread damage to the vessel and her cargo. The explosion was caused by the self-ignition of a container of calcium hypochlorite, which is stated in the IMDG Code to be a dangerous cargo which is required to be stowed 'away from' sources of heat. Nevertheless, the cargo had been stowed next to a bunker tank which was heated during the voyage

Clause 8 of the charterparty provided that the *"Charterers are to load and stow the cargo at their expense under the supervision of the Captain."* The contents of the container had been declared as calcium hypochlorite by the shippers pursuant to the requirements of the IMDG Code but it was found that the container probably contained a 'rogue' batch which had an abnormally high thermal instability and was prone to self-heat at ordinary carriage temperatures. This information was not communicated by the shippers to either the shipowners or the time charterers and, consequently, was not communicated by the time charterers to the shipowners since the time charterers did not know, and had no means of knowing, that this was a 'rogue' batch.

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31 See, for example, the International Maritime Solid Bulk Cargoes (IMBSC) Code.

32 See Chapters 2.12.4.4, 2.12.7.1, 2.12.9.2 and 2.12.9.3 of the *Gard Guidance to Masters*.

33 See, for example, the *BIMCO Solid Bulk Cargoes that Can Liquefy Clause for Charter Parties 2012*.

34 *The Aconagua*, [2011] 1 Lloyd's Rep. 683.

The explosion of the container resulted in a huge fire and the crew abandoned the ship and were picked up by another vessel, the TRAVE TRADER. Subsequently, the shipowners brought claims against the time charterers for damage to hull and for shipowners' proportion of salvage<sup>35</sup> and general average<sup>36</sup> in the sum of approximately USD 40 million. London arbitrators found that, notwithstanding their ignorance of the dangerous nature of the cargo, the time charterers were obliged to indemnify the shipowners against the consequences of complying with the charterers' orders to load and stow the cargo, and that the stowage of the cargo was in breach of the IMDG Code and of their obligations under Clause 8 of the charter. For the reasons explained in Chapter 7.4 above, the time charterers were not entitled to limit their liability and consequently, they paid the sum of USD 27.75 million in settlement of the claims brought by the shipowners.

The bill of lading was issued by the time charterers as carriers and incorporated the Hague Rules including Article IV Rule 6.<sup>37</sup> Therefore, the time charterers brought an indemnity claim against the shippers who argued that the real cause of the damage was not the dangerous nature of the cargo but the negligence of the shipowners and/or time charterers in stowing the container next to a bunker tank which was subsequently heated during the course of the voyage contrary to the IMDG Code requirement that calcium hypochlorite should not be stowed next to a source of heat. The court held on the facts that the heating of the bunkers in the adjoining bunker compartment was not causative of the explosion since the ambient temperature in the hold meant that the explosion would have occurred even if the bunkers had not been heated. Furthermore, even if the crew had acted negligently in heating the bunkers, this was "*an act, neglect or default of the master, mariner ... or the servants of the carrier in the ... management of the ship*" for which the carrier had a defence under Article IV Rule 2 (a) of the Rules. Consequently, the time charterers were entitled to an indemnity from the shippers. However, the court went on to state that if the crew had been negligent in the manner that they had stowed the cargo, with the result that the damage had been caused partly by the dangerous nature of the cargo and partly by the actionable negligence of the crew, the time charterers would not have been entitled to an indemnity from the shippers.

The liability of the time charterers to the shipowners and the time charterers' legal costs were shared between the time charterers' liability insurers for damage to hull (DTH), the time charterers' (different) liability insurers for other risks, and the time charterers themselves.

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35 For more detailed commentary see Chapter 14 (Salvage Claims).

36 For more detailed commentary see Chapter 10 (General Average Claims).

37 See Chapter 7.2.4 above.



### Case Study 2

The assured, a trader, buys a cargo on CIF terms at a terminal. The seller is responsible for transporting the cargo to the buyer and charters a vessel for that purpose. The cargo settles and damages the tanks during the carriage. The shipowner brings a claim under the charterparty against the seller of the cargo and a claim in tort against the assured for the damage that the cargo has caused to the vessel. The assured's liability to the shipowner for damage to the vessel and the legal costs of defending the claim are recoverable under the optional extension that the cargo owners/'traders' have under Gard's Comprehensive Charterers' Liability Cover. Gard may have a subrogated claim against the cargo seller if the tank damage was caused by the fact that the cargo was off-spec.



## Chapter 8

# Fines and Criminal Sanctions Claims<sup>1</sup>

### 8.1 Introduction

Given the international nature of shipping and the fact that the relevant laws and regulations vary from country to country, it is an inevitable fact of life that, from time to time, ships and ship operators will find that they have violated, or are alleged to have violated, the criminal or administrative regulations of a particular country and that, consequently, a fine or criminal penalty may be imposed on them. It should also not be forgotten that the imposition of a fine may be seen in some countries as a useful method of revenue-raising. Most fines are 'administrative', that is, civil, in nature and do not give rise to potential criminal liability. However, in more serious cases, often involving alleged pollution, both civil and criminal fines may be imposed.

The fact that the particular violation may have been committed by a member of the crew or some other employee without the knowledge of the ship operator is not normally relevant if the violation has been committed during the scope of their employment. The laws of many countries make the employer vicariously liable in such circumstances. Indeed, it must also be said that prosecutions may be brought against the ship or ship operator in some countries even if it can be shown that the violation was not committed by the crew member or other employee during the course of their employment.

Fines are commonly imposed after a casualty when the vessel has spilled oil<sup>2</sup> or run aground, or for failing to report an incident to the relevant local authority (for example, when stopping to carry out work on the main engine). However, they are often imposed in a wide range of circumstances and even if there has been

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1 For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 47 (Fines)) and *Port State Control* by Ozcayir, Informa, 2nd edition, 2004.

2 For more detailed commentary see Chapter 12 (Pollution Claims).

no casualty. As is described below, many fines are routinely imposed as a result of an apparent difference between the manifested quantity of something on board the vessel and the actual quantity. The 'something on board' may be (and often is) cargo, but it may also be the number of tins of paint in the forepeak store or the quantity of bunkers on board. Other examples include fines imposed for illegal fishing by members of the crew or for the failure by the vessel to timely serve a document required at the port or place in question.

In some instances, such penalties may be imposed for violations of known, internationally accepted, standards as would be the case, for example, if there were violations of widely adopted international conventions or agreements such as:

- the Safety of Life at Sea (SOLAS) Convention; or
- the MARPOL Convention; or
- a Port State Control Memorandum of Understanding.<sup>3</sup>

It has also become common for rules to be established by regional authorities such as the European Union or United States which are not international conventions in the above sense in that other countries do not consider themselves bound by them but which, nevertheless, have substantial extra-territorial impact. Classic examples are the regulations that have been imposed by the EU on all entities that are subject to EU jurisdiction prohibiting the purchase, import or transport of Iranian oil or oil products and the provision of insurance relating to the same<sup>4</sup> and the similar Iran Threat Reduction and Syria Human Rights Act 2012 of the USA.<sup>5</sup> Similar regulations have also been promulgated from time to time in relation to trade involving other countries such as the Ivory Coast, Libya and Syria.

In addition to such international conventions or regional regulations, virtually all countries have in place legislation which allows for the imposition of fines and the criminal prosecution of the shipowner and/or responsible members of the crew when the ship is found to have engaged in activities such as gun-running or the smuggling of drugs or other narcotics. Such legislation may also allow the country in question to confiscate the ship.

However, in other cases, the ship or ship operators may find that, despite their best endeavours, they will be held to have contravened local criminal or administrative regulations which were unknown to them. For example, the customs laws and regulations of many countries empower the local customs authorities to impose

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3 For more detailed commentary see Chapter 22.3.3 (Maritime Regulation and Compliance) and Chapters 13 and 14 of the *Gard Handbook on Protection of the Environment*, 3rd edition.

4 See EU Council Regulation No. 267/2012 which can be found at: <http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2012:088:SOM:EN:HTML>.

5 The full text can be accessed at <http://www.govtrack.us/congress/bills/112/hr1905/text>.

a fine or some other penalty on a carrier of cargo in the event that there is a discrepancy between, on the one hand, the marks, number, quantity or weight of cargo described in the bill of lading, waybill, manifest etc., and, on the other hand, the actual marks, number, quantity or weight of cargo ascertained by those authorities after discharge of the cargo from the ship. This may occur even when the discrepancy is unavoidable given the nature of the cargo, e.g. where a dry bulk cargo loses weight during the course of transit as a result of the inevitable evaporation of the moisture content of the cargo. Similarly, a ship operator may find that he has unknowingly contravened the immigration rules of a country when arranging a crew change in that country at short notice.

Finally, particular difficulties can arise when the contravention is not the result of any wrong-doing on the part of the shipowners themselves but the result of the wrong-doing of the charterers or shippers. For example, there have been a number of cases in which drugs or stowaways have been found either at the load port or the discharge port to be concealed inside sealed containers. In the majority of cases, this has occurred without the knowledge of the shipowners. Nevertheless, heavy fines or other penalties have been imposed on the shipowners on the basis that their property (i.e. the ship) is vulnerable to arrest and a view is taken by the local authorities that either the shipowners should have been more careful, or that they can, in any event, recover an indemnity from the charterers or shippers.<sup>6</sup> However, in many cases, neither assumption is correct. Similarly, a shipowner may become subject to such fines or penalties if a crew member or stowaway absconds from the ship without the knowledge of the shipowner and is subsequently apprehended by the local authorities.

In such cases, there is a range of penalties that can be imposed either directly by the local executive or coastguard authorities or by the local court. Such penalties include:

- Fines or similar financial penalties imposed on the ship and/or her operators;
- The confiscation of the ship; and even
- The criminal prosecution of crew members.

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<sup>6</sup> For more detailed commentary on the shipowners' right to claim an indemnity see Chapter 4.5.2 (Charterparty Claims).

## 8.2 The Criminal Prosecution of Crew Members<sup>7</sup>

Historically, mariners who caused serious maritime incidents were required to answer for their actions or omissions before a court of enquiry and, if found guilty, would lose their licences resulting in most cases in a loss of their livelihoods. However, such action was not taken unless and until it was proved that the mariner had acted with intent, or recklessly, or with gross negligence. Furthermore, it was only if the mariner could be proved to have acted with criminal intent that he would face more serious criminal charges.

However, in recent years, many legal systems around the world have started to treat maritime accidents routinely as crimes, particularly when environmental damage has taken place. For example, US authorities regularly bring prosecutions both against the crewman and the relevant company in such circumstances.

## 8.3 Insurance

In general terms, the law of most countries forbids insurers to provide cover for criminal acts. However, there are limited exceptions to this rule and P&I clubs have provided cover for their members' liability in some limited circumstances for many years.

### 8.3.1 Fines or Similar Financial Penalties<sup>8</sup>

The Rules of most P&I clubs give the club the right to place restrictions on the cover that is provided if a substantial increase in risk has occurred as a result of new international or national legislation or any other circumstance that the club believes may be to the detriment of the membership as a whole.<sup>9</sup> The recent spate of international, regional and national sanctions relating to trading activity involving countries such as Iran and the provision of insurance relating to such activity is considered by the International Group P&I Clubs to give rise to such an increased risk. Consequently, the Rules of such clubs entitle the club to terminate the entry of any of their members who either break the relevant sanctions or engage in activities which run the risk of breach.<sup>10</sup> and also entitle the club to refuse to indemnify the member against any fines or liabilities that the member incurs as a result of engaging in such activities.<sup>11</sup>

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7 For more detailed commentary see Chapter 12.4.2.2 (Pollution Claims) and Chapter 14.4 of the *Gard Handbook on Protection of the Environment*.

8 For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 47 (Fines)).

9 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 92 (Amendments to the Rules)).

10 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 24 (Termination by the Association) and Rule 25 (Cesser)).

11 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 77.2 (Administrative Costs, Insolvency etc.)).

The cover that is provided by P&I clubs in other circumstances is based on an agreed 'model Rule' which is designed to strike a balance between, on the one hand, accidental or non-deliberate law infringements which are considered difficult to avoid given the trading environment in which ships normally operate, and those infringements which a member should and could have taken steps to avoid. The first category of infringement is considered to be a mutual risk which should be shared by the membership and, therefore, covered by the club, whilst the second category of infringement is not considered to be a mutual risk but a risk which should be for the member's own account.

The infringements which fall within the first category are the following:

- The short or over-delivery of cargo, or the failure to comply with regulations relating to cargo documentation or declaration;
- Breaches of immigration laws or regulations;
- The *accidental*<sup>12</sup> escape or discharge of oil or any other substance, or the threat thereof;
- Smuggling or any infringement of any custom law or regulation other than in relation to cargo carried on the ship.

Clubs may also have the discretion under the 'Omnibus Rule' to provide cover for other fines or penalties provided that the member is able to satisfy the club that he has taken such steps as appear to the club to be reasonable to avoid the event that has given rise to the fine or penalty.<sup>13</sup>

The Rules of most P&I clubs provide that cover is also available even if the fine or similar financial penalty is imposed not on the member directly but on other individuals who may be employed, engaged or appointed by the member if the member is legally obliged to indemnify those individuals or, alternatively, such indemnification is provided with the agreement of the club. Such individuals include not only the master and any crew member (who are normally, but perhaps not always, entitled to be held harmless pursuant to the terms of their contract of employment) but also independent contractors that are entitled to be held harmless pursuant to the terms of the contract between them and the member provided that the terms of such contract are usual and customary terms.<sup>14</sup>

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12 P&I clubs will not provide cover for an intentional discharge even if this is done by a crew member without the knowledge of the ship operator. See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 47.1(c) (Pollution)).

13 See Chapter 26.2.3 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Article 9.3 b and Rules 47.2 and 47.3).

14 See the *Gard Guidance to the Statutes and Rules* (paragraph (C) of the Guidance to Rule 47).

The limited degree of insurance cover reflects the fact that every member of a P&I club is expected to operate his ships in compliance with the laws and regulations of those countries where his ships are trading. He is expected in particular to have, or to obtain knowledge about, all such laws and regulations, and to ensure to the best of his ability that he complies with them. Therefore, a distinction is drawn between serious offences or violations of regulations that are committed with the knowledge or connivance of the member, and less serious offences or violations which are caused without the connivance of the member but are caused by the acts or omissions of the master or crew during the course of their duties and employment. Therefore, cover is not available for liabilities, losses, costs and expenses incurred by the member as a result of the use of the ship for the carriage of contraband, for blockade running or for unlawful trades or voyages, even if the member was unaware that the ship was being employed in this manner.

### 8.3.2 The Confiscation of the Ship

It would be rare for a country to take the draconian measure of confiscating a ship, or to impose a fine equivalent to the value of the ship. However, some countries (such as Venezuela) have the right to do so in some circumstances. Furthermore, the US authorities are entitled under the US Anti-Drug Abuse Act 1986 to confiscate a ship which has been involved in drug smuggling or the infringement of other customs laws or regulations.

#### 8.3.2.1 Hull and Machinery Insurance

The confiscation of a ship in such circumstances is not normally an insured peril under *standard* marine Hull and Machinery policy terms and it is unlikely that the infringement of such laws or regulations would be considered to be a war peril for the purpose of a *standard* War Hull Policy. However, it must be emphasised that the degree of cover that is available even under standard Hull and Machinery and War Hull policies can be variable.<sup>15</sup> Consequently, the terms of the particular insurance policy must always be checked.

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<sup>15</sup> For example, see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 36 (Collision with other ships) and Rule 37 (Damage to fixed or floating objects)) for examples of how the degree of cover can differ under standard policies.



### 8.3.2.2 P&I Insurance

The rules of most P&I clubs give the club the discretion to compensate the member either in full or in part in some limited circumstances. Such cover is normally available only if the reason for the confiscation of the ship or of a fine corresponding to the value of the ship is the infringement of customs laws or regulations.<sup>16</sup> The power to exercise such discretion is usually vested in the Board of Directors of the club concerned.

Such discretion can normally be exercised only when the confiscation has become final in the sense that the ship has become the property of the confiscating authority and the shipowner has no further right of appeal to avoid or revoke the confiscation. Furthermore, the club will normally exercise its discretion in favour of the member only if it is satisfied that the member has taken all reasonable steps to prevent the infringement which led to the confiscation.

### 8.3.3 The Criminal Prosecution of Crew Members<sup>17</sup>

If fines or similar financial penalties are imposed on crew members, they are sometimes, but not always, entitled to be indemnified by their employer under the terms of their contract of employment if the relevant acts or omissions were committed by them within the scope of their employment and duties on board. Therefore, although P&I clubs do not normally provide direct cover for crew members, shipowners are entitled to be indemnified by the club once they have indemnified the crew member.

However, the detention or imprisonment of crew members poses a far more difficult problem. None of the standard maritime insurances (i.e. Hull and Machinery, War or P&I) provides a ready solution. On any basis, insurers can only provide financial assistance and cannot force the release of crew members. Furthermore, the degree of financial assistance that can be provided is also limited. In particular, insurers will not normally provide bail or other security to release a crew member who is detained pending criminal investigation and possible prosecution.

P&I clubs may be able to reimburse the shipowner for the living and other related expenses incurred by the crew member whilst being detained and may be prepared to exercise their discretion to put up bail in order to secure the release of the crew member pending trial. However, further long-term assistance may not be possible.

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<sup>16</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 49 (Confiscation of the Ship)).

<sup>17</sup> See also Chapter 12.4.2.2 (Pollution Claims).

## 8.4 Claims Management

When ships trade to a particular country ship operators should ensure that they are fully briefed not only about the impact of any international or regional or national regulations that relate to such trade but also about the customs, immigration, pollution and other regulations that normally apply to shipping operations in that country. The local ship's agents and the local representatives of the ship's P&I club are very useful sources of such information.

If there is any evidence to suggest that a criminal prosecution may be brought either against the ship or the ship operator or any crew member the necessary protective measures should be taken immediately. Crew members should follow the recommendations set out in Chapters 3.6 and 3.7 of the *Gard Guidance to Masters* and the vessel's P&I club and local representatives should be consulted promptly since it may be necessary to consult an experienced local lawyer as a matter of urgency. Depending on the nature of the accusations, it may be necessary to appoint both civil and criminal lawyers to co-operate with any investigation whilst at the same time protecting their clients' rights. Furthermore, ship operators should ensure that seafarers understand fully that any statements that are made to port, coastal or flag state authorities or investigators, may be used in a future criminal prosecution. Finally, evidence should be preserved wherever possible as this may minimise the need to detain seafarers unnecessarily.

## 8.5 Case Studies

### Case Study 1

During the course of a voyage to deliver grain in the Far East bunker fuel leaked into one of the cargo holds and contaminated a quantity of grain. The vessel owner (a US corporation) decided not to report the incident nor to properly record it in the Oil Record Book. However, the oil soaked cargo was dumped en route. This was subsequently reported to the US Coast Guard by a crew member and a criminal prosecution was commenced against the ship's operator and officers. The President of the company was imprisoned for 33 months and a fine of USD 2 million was imposed on the company. Such a liability is not covered by insurance since the discharge was intentional and also arose as a result of the wilful misconduct of the ship's management.

### Case Study 2

A crew member has deserted in a foreign country and is apprehended by the police after three weeks. The authorities issue a deportation order and the expenses incurred by the shipowner in complying with such an order and in sending a replacement crew member are recoverable under the ship's P&I cover. However, the shipowner is entitled to deduct some of the expenses from the outstanding wages due to the deserting crew member.

## Chapter 9

# Fixed or Floating Objects (FFO) Claims<sup>1</sup>

### 9.1 Introduction

During the course of their trading activities ships will sometimes come into contact not only with other ships but with other fixed or floating objects (FFO) and may face claims from the owners or operators of such objects if they are thereby damaged. Such contact is sometimes referred to as damage to FFO.

A 'fixed object' is either a man-made structure that does not float and, therefore, is not designed to move or be moved on water, e.g. a harbour, quay, dock, pier, jetty, crane or bridge or a fixed offshore platform, subsea pipeline or power or telecommunication cable, or a natural habitat resource with direct or derived economic value which can be damaged by physical contact with ships, e.g. coral reefs, and which may result in a claim for restoration costs and natural resource damages.

A 'floating object' is normally defined to be a man-made structure other than a ship that is designed to have buoyancy, e.g. a buoy or a semi-submersible drilling rig, and that may be designed to move on water, e.g. a floating storage and off-loading vessel. It can be a difficult question in some cases to decide whether the particular floating object is a ship or not a ship since some floating objects are multi-purpose.<sup>2</sup>

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<sup>1</sup> For further commentary see Chapter 9.4 of the *Gard Handbook on P&I Insurance*, 5th edition.

<sup>2</sup> See Chapter 9.5 Case Study 2 below.

## 9.2 Liability for Damage to Fixed or Floating Objects

The distinction between ship collisions as opposed to damage to FFO is of legal significance. If the damaged object is considered to be a ship, then liability will normally be determined in accordance with international conventions such as the International Regulations for Preventing Collisions at Sea, 1972 (COLREGS) and the International Convention for the Unification of certain Rules of Law with Respect to Collision, 1910 (The 1910 Collision Convention).<sup>3</sup> On the other hand, there is no international convention which regulates liability for damage to fixed or floating objects.

A claim concerning damage to an FFO is therefore likely to be determined in the courts of the country where the damage occurred in accordance with the local law.<sup>4</sup> Such liability may arise:

- in tort (i.e. non-contractual liability for negligence); or
- under contract; or
- under local statutes or other regulations.

### 9.2.1 Liability in Tort<sup>5</sup>

The law of most countries provides that a shipowner has the duty to exercise care to ensure that his ship does not cause damage to others. This applies both personally and through his servants and agents, including pilots and harbour tugs assisting the ship in and out of port and during berthing operations. Therefore, if the ship has not exercised sufficient care and has come into contact with a fixed or floating object, it is likely that the Member will be held liable to compensate the owner of that object for losses sustained as a result. Where a ship in motion makes contact with an object that is stationary, particularly where the object is fixed or, if floating, incapable of moving to avoid contact, there will usually be a presumption that the ship is to blame for having caused the contact. For example, where a ship makes contact with a fixed object such as a jetty, buoy or dolphin, it is likely that the shipowner will be held liable for any damage that may have been caused to that object as a result. However, depending on the applicable local law, the shipowner may be able to avoid liability if it can be proved that the contact was not caused by any fault on the part of the ship, e.g. as a result of some extraordinary and irresistible event beyond the control of the ship, such as a tsunami causing the ship to be pushed heavily against a berth.

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<sup>3</sup> See Chapter 6.2.1 (Collision Claims).

<sup>4</sup> For more detailed commentary see Chapter 19.10.2 (Law and Jurisdiction).

<sup>5</sup> For more detailed commentary Chapter 3.3 (Cargo Claims) and Chapter 14 of the *Gard Handbook on P&I Insurance*, 5th edition.

Alternatively, the shipowner may be able to avoid liability, or at least reduce the amount of his liability, if it can be proved that there was some degree of contributory negligence on the part of the owner of the fixed or floating object. The fact that an object is stationary on or in the water does not necessarily mean that the owners of that object do not have their own separate responsibilities. The owner or operator of that object is normally bound to record the position of the object on the charts that are generally available to ships, to bring the object to the attention of navigators by adequate lighting and/or sound emission systems and generally, to warn ships of any danger. Therefore, if it is found that contact would have been avoided or, at least, that the likelihood of contact would have been reduced if such safeguards had been taken, this may have a bearing on the apportionment of liability for the incident.

### 9.2.2 Liability under Contract

Liability for loss of or damage to fixed and floating objects may also arise under contract, e.g. under a contract between the operator of an oil platform and the owner of an anchor handling vessel providing services to the platform. However, many offshore service contracts provide protection against such liability in the form of a mutual hold harmless agreement (frequently called 'knock-for-knock terms' whereby each of the parties agrees to absorb the risk of damage to own property even if caused by negligence of the other party.

In many places in the world, a ship is not entitled to use a dock, port, berth, terminal or similar facility unless the ship agrees to conclude a contract with the owner or operator of that facility on a variety of standard 'terms and conditions of use.' Even if no formal contract is signed on a particular occasion such terms may be considered to be binding under the applicable law if the shipowner has used the facility on previous occasions subject to similar contractual terms, i.e. as a result of a prior course of dealing. Alternatively, the local law may provide that the mere use of the facility constitutes an implied acceptance of the facility's standard 'terms and conditions of use' provided that the shipowner has been made aware of them before agreeing to use the facility either on that occasion or on a previous occasion.

Although 'terms and conditions of use' differ substantially both in relation to the basis of liability and in relation to the degree of liability imposed on the 'user' such terms normally impose strict liability for any damage caused by the 'user' and give the owner or operator of the facility the right to be indemnified by the ship in respect of any resulting loss or damage. Such 'terms and conditions of use' often seek to impose liability on the ship even when it is proved that the owner or operator of the facility is solely to blame for the incident, e.g. due to the negligence of harbour tugs and/or the mooring master during berthing operations.

### 9.2.3 Liability under Statute or other Regulations

The law of some countries imposes strict liability on the shipowner even if it can be proved that the contact and damage was not caused by his negligence or fault. For example, under English law, a shipowner may be held liable for damage caused by his ship to a harbour, dock or pier, or any quay or associated works under the Harbours, Docks and Piers Clauses Act 1847 even if neither he nor his ship is at fault. Similarly, under Norwegian law, the shipowner is strictly liable for damage to fixed or floating objects caused by a technical failure of the ship's reversing mechanism.

### 9.2.4 Recoverable Damages

The damages that are normally recoverable by the owner or operator of a fixed or floating object as a result of contact with a ship include:

- The reasonable cost of both temporary and permanent repairs to the object and any ancillary equipment or, where the object has become damaged beyond economic repair, its insured value, or market value, or replacement cost;
- Compensation for the loss of use of the object, i.e. the loss of revenue suffered by its owner or operator by reason of the fact that the object is out of (normal) use as a result of the damage caused by the ship;
- Third party liabilities, whether arising under contract, statute or in tort, which are incurred by the owner or operator of the object as a result of the contact damages. For example, a terminal operator may be liable under contract to pay compensation to other users of the terminal as a result of the inoperability of loading and discharging equipment caused by the contact incident;
- Various costs and expenses reasonably incurred by the owner or operator of the object as a result of the damage caused, e.g. survey and inspection fees and costs.

### 9.2.5 The Right to Limit Liability<sup>6</sup>

Damage to fixed or floating objects can result in very substantial claims particularly when the object is expensive and is normally used continuously as part of a production process. The resulting claim for physical damage and loss of revenue if the production process is interrupted may be very large indeed. However, since the relevant local laws or terms of use will often impose strict or nearly strict liability, the shipowner may not be able to escape liability. Consequently, it is important to be aware of any rights that the shipowner may have to limit his liability.

Limitation rights depend on whether the country in which the claim arises is either a party to one of the international limitation conventions or has a local statute<sup>7</sup> that gives the right to limit liability. Most but by no means all countries are parties to

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<sup>6</sup> For more detailed commentary Chapter 21.3 (Limitation of Liability).

<sup>7</sup> See comments in Chapter 9.2.5.1 below concerning the position in the United States.

either the 1976 Limitation Convention (or the 1996 Protocol thereto) or the 1957 Limitation Convention. Article 2.1 (a) of the 1976 Limitation Convention entitles a shipowner to limit his liability whether such liability arises in tort or in contract or under statute or other regulations in respect of:

*“Claims (for) ... damage to property (including damage to harbour works, basins and waterways and aids to navigation) occurring ... in direct connection with the operation of the ship ... and consequential loss resulting therefrom.”*

Therefore, it is likely that a shipowner will be entitled under the 1976 Limitation Convention to limit his liability both for physical damage to harbour works or navigational aids and for any consequential loss of use. Furthermore, although the Convention does not refer expressly to other fixed or floating objects such as an oil exploration platform, it is likely that such objects will be considered to be “property” for the purposes of Article 2.1 (a) thereby entitling the shipowner to the same limitation rights. Similar rights are also given under the 1957 Limitation Convention.

The limit of liability applies to all claims that arise “on any distinct occasion”.<sup>8</sup> Therefore, difficult questions may arise if the ship comes into contact with the fixed or floating object on more than one occasion (e.g. during heavy swell or heavy weather) since the claimant may then argue that the shipowner cannot limit his liability to all claims by establishing one fund but must establish a separate fund equivalent to the ship’s limit of liability for the claims that have arisen on each separate occasion. The question of whether or not there has been one or more occasion depends in most cases on whether the second occasion or subsequent damage can be said to be the inevitable result of the first occasion.

In (the probably rare) circumstances where the fixed or floating object is held liable for damage caused by it to the ship, the owners or operators of the fixed or floating object will normally not be able to limit their liability under the international conventions discussed above since it is only ‘ships’<sup>9</sup> that have the right to limit their liability under such conventions.<sup>10</sup>

Nevertheless, it is possible that a right of limitation may be available to the owners of fixed or floating objects under the local law. For example, Section 191 of the United Kingdom Merchant Shipping Act 1995 allows a harbour authority,

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<sup>8</sup> See Chapter 21.3.2 (Limitation of Liability).

<sup>9</sup> There is no universal definition of a ‘ship’ but one common definition is that used in Paragraph 12 of Part II to Schedule 7 of Section 185 (1) of the Merchant Shipping Act 1995 of the United Kingdom, i.e. “any structure (whether completed or in the course of completion) launched and intended for use in navigation as a ship or part of a ship.”

<sup>10</sup> See Chapter 21.3.3.1 (Limitation of Liability).

a conservancy authority and the owners of any dock to limit their liability for any loss or damage that they may cause to a ship by reference to the tonnage of the largest UK registered ship that has visited the relevant installation within the preceding five years.

#### **9.2.5.1 Limitation in the United States of America**

The United States is not a party to any of the international limitation conventions but a shipowner is entitled in principle to limit liability under the Limitation of Liability Act, 46 U.S.C. 30501, *et seq.* so long as the relevant conduct was not committed with the 'privity or knowledge'<sup>11</sup> of the shipowner. However, US courts are, in general, reluctant to allow limitation and can justify their refusal to do so on a number of factual or legal grounds. Furthermore, some US cases suggest that the Limitation of Liability Act is not applicable in the case of damage to federal navigation installations (e.g. locks).

If the incident results in claims being brought by more than one claimant the Limitation Act has a special procedure ('*concursum*') which requires the claimants to proceed through the medium of a single lawsuit in the federal court. However, if the incident results in merely one claimant (such as the owner of the FFO) the claimant may proceed in the forum of its own choice.

### **9.3 Insurance<sup>12</sup>**

When ships come into contact with fixed and floating objects damage may be caused:

- By the ship to the FFO; and/or
- By the FFO to the ship.

The following claims normally arise as a result:

- Property claims;
- Liability claims;
- Delay claims;
- Claims for loss of income.

Claims resulting from damage to FFOs may therefore involve several different types of insurance cover, such as Hull and Machinery (H&M), Hull Interest/Increased Value (IV) insurance, P&I or Defence. If the incident causes damage to cargo on board the ship or ashore, cargo insurance may also come into play. It is important to know which claims are covered by which insurance, particularly since the assured has the duty to notify the relevant insurer promptly of any claim and may prejudice rights of recovery

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<sup>11</sup> For further commentary see Chapter 21.3 (Limitation of Liability).

<sup>12</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).



under the terms of insurance if he does not do so. The assured should also be aware that if he is indemnified by the relevant insurer, the insurer is entitled to exercise his rights in subrogation. Subrogation is the right that the insurer has to 'step into the shoes of the insured' when a loss has been paid and to take over all rights that the assured may have to claim against a third party that has caused the loss or damage.

### 9.3.1 Hull and Machinery Insurance<sup>13</sup>

Claims for damage to the ship and any consequent salvage services as a result of contact with an FFO are normally covered by the ship's H&M insurances, subject always to the sum insured. If the ship becomes a total loss as a result of such an incident, the shipowners will normally be covered for the insured value of the ship under the H&M insurers and/or IV insurance when applicable.<sup>14</sup> However, liability for wreck removal would normally be covered by the ship's P&I insurers.<sup>15</sup>

H&M insurance terms differ substantially in the manner in which they provide cover for damage caused by the ship to an FFO. They also differ in the manner in which they identify the relevant perils that qualify for cover and the consequential losses that are covered. The standard Nordic, German or French terms provide cover when the damage has been caused by physical contact between the hull of the ship and the FFO<sup>16</sup> and the Nordic and German terms both provide liability cover for the wreck removal of the FFO, as well as financial loss sustained by the owner of the FFO for 'loss of use,' which term includes loss of profit. The German terms are wider than other terms in that cover is available also for damage caused to an FFO by contact with the ship's anchor, mooring or towing lines, or gangways, even if not caused by the movement of the ship itself and even when there has been no physical contact with the ship, e.g. surge damage.

English, American and Japanese terms do not provide cover for FFO damage. This distinction is also relevant in the context of P&I insurance.<sup>17</sup> For a comparison of the scope of cover provided between the most commonly used insurance terms, reference is made to the Annex that can be found at the end of this chapter.

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<sup>13</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>14</sup> See Chapter 9.3.2 below and Chapter 26.3.1.2 (The Structure of Marine Insurance).

<sup>15</sup> For more detailed commentary see Chapter 16.4.1 (Wreck Removal Claims) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 40 (Liability for obstruction and wreck removal)).

<sup>16</sup> As noted in Chapter 9.1 above, an FFO is defined as a 'man-made structure.' The Norwegian Marine Insurance Plan originally provided cover for damage caused by physical contact between the ship and a coral reef, but this was subsequently removed from the scope of cover, because it was considered that this is environmental damage which is covered by P&I insurance.

<sup>17</sup> See Chapter 9.3.3.

The liability cover that is available for FFO damage is limited to the sum insured in the H&M policy, but it should be remembered that such liability cover is separate and distinct from the cover for damage to (or loss of) the ship. Therefore, in a major case, the H&M insurers may have to pay one sum insured for the loss of the ship and a further sum insured for the FFO liability.<sup>18</sup> It is also possible that the sum insured under the H&M policy for liability for FFO damage may prove to be insufficient to cover the total liability incurred by the assured. In such cases, the excess liability may be covered either by IV insurance<sup>19</sup> and/or by the P&I insurance.<sup>20</sup>

### 9.3.2 IV Insurance

The main purpose of the IV insurance is to provide the assured with a complete indemnity in case of the total loss of the ship since the market value of the ship may be more than the insured value, particularly when market prices are increasing. The sum that is insured under a standard IV insurance is usually 25 per cent of the sum insured under the H&M insurance.

The IV insurance also provides additional cover for the assured's liability for damage caused to an FFO where the sum insured in the underlying H&M insurance proves to be insufficient to cover such liability. Such cover is normally capped at 25 per cent of the sum that is insured by the H&M insurance and it does not provide cover for liabilities that do not fall within the scope of the underlying H&M insurance. However, this is a separate and distinct type of cover that does not restrict the right that the assured has under the IV insurance to receive indemnification for the loss of the insured ship.

### 9.3.3 P&I Insurance<sup>21</sup>

The P&I insurance will indemnify the assured member in respect of liabilities for damage to FFO that either fall outside the scope of cover provided by the H&M insurance, or which exceed the sum(s) insured under the H&M (and IV insurance). It follows that the scope of P&I cover for such liability is directly dependent on the scope of cover that is available under the H&M and IV insurances of the ship. Consequently, it is important that a shipowner should fully understand the scope of those insurances in order to fully understand the scope of his P&I cover.

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18 In a worst case scenario, they may have to pay three times the sum insured, because a separate sum insured applies to the cost of measures to minimise loss, e.g. salvage.

19 See Chapter 9.3.2.

20 See Chapter 9.3.3.

21 For more detailed commentary see Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 37 (Damage to fixed or floating objects)).

Cover is available for the assured's legal liability for damage to FFO, as well as its liability for consequential losses, which arise either in tort or pursuant to local statutes or regulations. However, cover is subject to the following restrictions:

- the damage must have been caused by physical contact between the ship and the FFO.<sup>22</sup> In this regard the 'ship' means not merely the hull, but any part of the ship's fixed structure as well as anchors, chains, mooring or towing ropes etc.;
- cover is not available in respect of liability that would not have arisen but for the terms of a contract or indemnity entered into by the assured member or by another person acting on his behalf, unless the terms have previously been approved by the P&I insurer, or the P&I insurer exercises its discretion to indemnify the assured member.<sup>23</sup> Since the liabilities that are imposed by such terms can be very onerous for the assured member, the P&I insurers may well be reluctant to approve certain terms. For example, liabilities arising solely as a result of the fact that the 'user' has agreed to indemnify the owner or operator of the port or terminal for loss or damage caused by the intentional acts or the gross negligence of the owner or operator, or his servants or agents, or which have the effect of depriving the 'user' of a right to limit liability that would otherwise apply under the applicable law, are not likely to be approved by the P&I insurer.

Examples of recoverable damage are discussed above in Chapter 9.2.4.

#### 9.3.4 Loss of Hire Insurance<sup>24</sup>

If the contact with the FFO causes physical damage to the ship it may need to be moved to a repair yard and will be out of commission until repaired. In such cases Loss of Hire insurance is intended to provide cover for any loss of income that may be incurred by the assured for the time lost as a result of the damage and repairs. However, cover is not available for income that may be lost as a result of other circumstances even if connected to the incident, e.g. if the ship were to be detained by local authorities or arrested by the owner of the damaged FFO.

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<sup>22</sup> If damage is caused to the FFO in other circumstances, e.g. that the ship's anchor drags and damages a pipeline or cable on the seabed, the liability of the shipowner may be covered by the P&I insurance, however, not as an FFO damage, but pursuant to Rule 39 concerning loss of or damage to property.

<sup>23</sup> See *Gard Guidance to the Statutes and Rules* – Rule 55.a.

<sup>24</sup> See also Chapter 26.3.1.3 (The Structure of Marine Insurance).

### 9.3.5 Defence Cover,<sup>25</sup> i.e. Legal and Other Expenses Cover

If the ship causes, or is alleged to have caused, damage to the FFO the assured will usually be obliged to incur legal and other expenses to defend itself against claims that may be brought by the owner of the FFO, local authorities and/or other third parties that claim to have suffered loss. Such legal and other expenses will normally be covered by whichever insurers cover the potential liabilities, i.e. the H&M, IV or P&I insurers. However, such expenses may also be incurred in relation to (that proportion of) claims that are not covered by any insurance, e.g. those retained by the assured pursuant to whatever deductibles have been agreed for those insurances.<sup>26</sup> Such expenses may be recoverable under the Defence cover that is offered by most P&I clubs as a separate class of cover. The assured would, however, be obliged to bear a proportion of the expenses so incurred (normally 25 per cent).

## 9.4 Claims Management

Most claims that arise as a result of contact with fixed or floating objects can be classified as mere 'bumps and scrapes' that arise in the normal course of operations, particularly when berthing at a quay or jetty. Such claims are usually not of major significance and are settled directly between the parties without the need for much involvement on the part of their insurers or other parties.

However, some claims can be very substantial because significant damage has been caused to an FFO of high value and which has also caused substantial consequential business interruption. Therefore, parties are strongly urged to consult their P&I or H&M insurers as soon as such an incident has occurred so that the necessary protective measures can be taken without delay. In many cases, the prompt attendance of an experienced surveyor or naval architect and an experienced local lawyer can prevent costs escalating and prevent or minimise the detention of the ship.

Shipowners should also consult their P&I insurers prior to concluding contractual terms of use to ensure that the terms of such contracts do not impose unusually onerous terms which might thereby prejudice their insurance cover.

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25 See Chapter 26.3.1.6 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV Rule 65 (Defence Cover)).

26 Costs relating to claims for damage sustained by the ship may be covered under the Defence cover only to the extent that such damage is not recoverable under the H&M policy by reason of a deductible which is normally not to exceed one per cent. See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 71.1.a (Other Insurance)).

## 9.5 Case Studies

### Case Study 1

The product tanker T was entered with her P&I club for 4/4 collision and FFO risks. Her owners informed the club that the master had reported that, while under compulsory pilotage, the vessel had 'run over' a jetty at a terminal in a country in North Africa. Investigations soon revealed that the vessel had approached the jetty at too high a speed and that the jetty was very badly damaged. International expert civil engineers confirmed that the jetty was very badly damaged and would require substantial repairs. The vessel suffered little damage, but was detained by the owners of the jetty (a government-controlled company) pursuant to their demand for security for some USD 90 million, comprising USD 10 million for physical damage and USD 80 million for alleged loss of use. The form of security demanded was a bank guarantee.

The expert civil engineers appointed by the club and owners assessed the cost of repairing the jetty (which was nearly 20 years old) at around USD 6 – 7 million. They also advised that the jetty was little used and that there were other facilities nearby which could be used to offset any alleged loss of use. Legal advice indicated the country in question had ratified the 1976 LLMC, under which the tonnage limitation of the vessel was some USD 7.5 million. The market value of the vessel was in the region of USD 20 million.

The vessel and her crew remained under detention while discussion concerning security took place. Owners and the club agreed the claimants' security demand was unreasonable and should be rejected. This led to an impasse with claimants, as they were unwilling to reduce their demand. Local legal advice indicated that it would take months, possibly years, for the local courts to reach a decision on the issue of the amount and form of security which should be provided and that it was likely the claimants, as an arm of the government, would win. The advice also indicated that, although the court had ratified the 1976 LLMC, the language in which the convention had been enacted into local law meant that claimants had good prospects of defeating owners' attempts to limit their liability.

In these circumstances, the decision was taken early on to try to settle the case. Representatives from owners and the club, together with international and local legal advisers, met claimants in the country in question. After two meetings, the entire claim (including loss of use) was settled for USD 10 million. The case was concluded less than four months after the incident, allowing the vessel – which was not fixed at the time of the incident – to meet her next fixture.

### Case Study 2

A shuttle tanker was due to lighter crude oil from a floating storage unit (FSU) in the North Sea. The FSU was a purpose built storage unit classed as a 'Ship-shaped Oil Storage unit'. The unit, while shaped like a traditional tanker did not have forward propulsion machinery. When approaching the FSU, the shuttle tanker experienced technical problems resulting in her bow making contact with the FSU. The impact resulted in a significant claim for physical damages and consequential losses. Fortunately no personal injury or pollution resulted.

The shuttle tanker was insured for fixed and floating objects (FFO) liabilities by her P&I insurer, while collision (RDC) liabilities were covered by the hull insurer. Both policies were subject to Norwegian law and jurisdiction. This raised the question of whether the incident was to be considered an FFO or RDC matter, and the crux of the question was whether the FSU fell within the legal definition of a 'ship.' This point was submitted to an arbitrator, who held that under Norwegian law the FSU was not to be considered a ship and consequently that the resulting liabilities should be covered by the P&I insurer, under their FFO cover.

**ANNEX**

## FFO liabilities and Hull Policy Cover

	English conditions (Institute Time Clauses-Hulls 1983, 3/4ths cover)	Nordic conditions (The Nordic Marine Insurance Plan 2013)	United States conditions (American Institute Hull Clauses)	German conditions (DTV Hull Clauses)
Damage to a fixed or floating object (FFO) caused by striking* by the ship		√		√
Loss of use of FFO (as consequence of striking by the ship)		√		√
Removal of wreck of FFO (as consequence of striking by the ship)		√		√
Damage to FFO without any physical contact with the ship (e.g. surge damage)				√
Damage to FFO resulting from use of the anchor, mooring or towing lines, gangways etc., caused by any movement** of the ship, or by navigational measures*** whilst the ship is in transit				√

\* Striking means physical contact between the hull of the ship or any appliances fixed to the hull of the ship, and the FFO.

\*\* Any movement of the ship includes unintended movement, e.g. that the ship breaks its moorings in heavy weather whilst berthed.

\*\*\* Navigational measures includes measures taken to keep the vessel stationary whilst in transit, e.g. at anchor clearance to enter the port.





## Chapter 10

# General Average Claims<sup>1</sup>

### 10.1 Introduction

General Average is one of the oldest rules of maritime law and practice. It is an equitable doctrine which is intended to balance between the owners of property at risk the cost of any extraordinary sacrifices that have been made, or extraordinary expenses that have been incurred, in order to avert a peril or to release the property from the grip of a peril that threatens the entire voyage. The rule applies by operation of law irrespective of contract but it is invariably the case that contracts of carriage will incorporate the York-Antwerp Rules which set out various principles and rules for the adjustment of the parties' rights. Rule A.1 of the York-Antwerp Rules describes general average succinctly as follows:

*"There is a general average act when, and only when, any extraordinary sacrifice or expenditure is intentionally and reasonably made or incurred for the common safety for the purpose of preserving from peril the property involved in the common maritime adventure."*

Any party making such sacrifice or incurring such expenditure is considered to have conferred a common benefit on all parties to the maritime adventure and is entitled to receive a contribution from those other parties. The contribution is based on that proportion of the value of the property saved that the extraordinary sacrifice or extraordinary expense bears to whatever the value of the property may be at the time and place where the common adventure or voyage ends.

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<sup>1</sup> For more detailed commentary see Chapter 12 of the *Gard Handbook on P&I Insurance*, 5th edition, Lowndes & Rudolf: *The Law of General Average and the York-Antwerp Rules*, Sweet & Maxwell, 13th edition (2008) and *A guide to General Average* by Richard Cornah which can be accessed at the website of Richards Hogg Lindley Ltd: [www.rhlg.com/pdfs/GAGuide.pdf](http://www.rhlg.com/pdfs/GAGuide.pdf).

In the event of peril the following property<sup>2</sup> is normally at risk:

- The ship;
- The cargo;
- Bunkers;
- Containers;
- Freight.

Therefore, if, for example, cargo is jettisoned in order to prevent the ship getting into difficulty the owners of the jettisoned cargo are entitled to receive contribution in general average from the owners of the ship, bunkers, containers or any other property on board towards the value of the jettisoned cargo. Similarly, if the ship has run aground and incurs tug or other salvage assistance in order to refloat the ship and save a valuable cargo, the shipowners are entitled to a contribution in general average from the owners of the cargo and any other property that may be at risk towards the cost of the towage or salvage services.<sup>3</sup>

The following is a simple example of an adjustment:

#### Loss

Jettisoned cargo (i.e. G.A. sacrifice)	USD	135,000
Freight lost to owners by reason of jettison	USD	21,000
Towage cost (i.e. G.A. expenditure)	USD	45,000
Total	USD	<u>201,000</u>

#### Net contributory values

Ship	USD	900,000
Freight	USD	200,000
Cargo	USD	910,000
Total	USD	<u>2,010,000</u>

Contribution proportion: USD 201,000/USD 2,010,000, i.e. 10 per cent

#### General average contribution

Ship pays	USD	90,000
Freight pays	USD	20,000
Cargo pays	USD	91,000
Total	USD	<u>201,000</u>

<sup>2</sup> These are the same interests that are obliged to contribute to a salvage award. See Chapter 14.2 (Salvage Claims).

<sup>3</sup> However, if general average is adjusted under the York-Antwerp Rules 2004, salvage payments are not to be re-adjusted in general average – see Chapter 10.5 below.

To qualify for general average:

- There must be an extraordinary sacrifice or extraordinary expenditure;
- The act must be incurred in the interests of common safety in order to preserve the property involved in the common maritime adventure from a grave and imminent peril;
- The act must be intentional;
- The act must be reasonable; and
- The act must be successful.

Because general average is an equitable doctrine which is intended to preserve the rights of all property which is at risk, all interested parties have the right, but the shipowner has a *duty* to all such parties, to ensure:

- That general average is declared in appropriate circumstances;
- That general average security is obtained from all property at risk before it is released; and that
- A general average adjustment is drawn up.

If the shipowner fails to comply with his obligations in this respect he may be liable to the other parties for any contributions that they should have received from other parties at risk and which they have not received as a result of the shipowner's failure.

## 10.2 Examples of General Average Sacrifices and Expenditures

General average sacrifice includes:

- The jettison of cargo carried on deck or the discharging of cargo overboard;
- Damage to machinery and/or the ship's bottom and the loss of equipment during attempts to refloat the ship;
- The loss of freight due to jettison of cargo at risk.

General average expenditure normally includes the cost of:

- Salvage and necessary repairs;
- Lightening the vessel to enable it to be refloated or repaired;
- Entering, staying at and leaving a port of refuge;
- Raising the necessary funds to safeguard the overall maritime adventure;
- Payment of ransom to release ships and cargoes that have been detained by pirates.<sup>4</sup>

However, loss or damage sustained by the ship or cargo because of delay does not qualify in general average.

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4 See *The Lehmann Timber*, [2012] 2 Lloyd's Rep. 73. It has been held by the English court that such payments are not contrary to public policy and can, therefore, be the subject of insurance cover. See *Masefield v Amlin Corporate Members Ltd*, [2011] EWCA Civ. 24.

### 10.3 General Average Calculation

The calculation of the right to contribution in general average is called the general average adjustment. The calculation is made by professional average adjusters appointed by the shipowner in accordance with the terms of the relevant contract of carriage. In most cases, the adjusters are members (Fellows) of the Association of Average Adjusters and the adjustment is normally drawn up in accordance with the Rules of Practice of the Association<sup>5</sup> at one of the major shipping centres around the world. However the general average adjustment is not legally binding and the basis of the adjustment and the adjuster's calculations are open to challenge by the interested parties.

### 10.4 The Relevance of Fault

The adjustment is initially calculated without consideration of fault in relation to the event which has given rise to general average. However, once the adjustment has been made and the contributions from each property interest established, it is open to any interest which is to make a contribution to challenge the obligation to do so on the grounds that the event giving rise to general average has been caused by the fault of the party claiming contribution. One common example is where cargo interests object to claims for general average contribution made by shipowners where the cause of the general average event can be attributed to the unseaworthiness of the vessel or the crew's failure to properly and carefully carry the cargo. However, under the law of most countries<sup>6</sup> the mere fact that the event has been caused by the conduct of the party claiming contribution should not be equated with fault for these purposes. There is no fault for these purposes if the terms of the contract of carriage exempt the party claiming contribution from liability for such conduct, and in such circumstances, the party claiming contribution is entitled to contribution.

Therefore, if a collision occurs due to the negligent navigation of the master and it becomes necessary thereafter to run the ship aground in order to prevent her foundering, the shipowner is likely to be entitled to claim contribution from the owners of the cargo at risk towards the cost of any towage or salvage that may be necessary to refloat the ship since a carrier has no liability for negligent navigation under Article IV Rule 2 (a) of the Hague or Hague-Visby Rules which are likely to apply to the contract of carriage. However, if the contract of carriage is subject to the Hamburg Rules, the carrier has no defence for negligent navigation with the result that he is unlikely to have the right to receive contribution.<sup>7</sup>

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5 A list of Fellows and the Rules of Practice of the Association of Average Adjusters can be accessed at the Association's website [www. average-adjusters.com](http://www.average-adjusters.com).

6 However, the law of the United States is different – see Chapter 10.4.1.

7 For more detailed commentary see section 2.9 (c) (ii) of Chapter 3.2.9.3.2 (Cargo Claims).

### 10.4.1 The Relevance of Fault under the Law of the USA<sup>8</sup>

Under the law of the USA a party whose negligence has caused the event giving rise to general average is not entitled to general average contribution even if there is a clause in the contract of carriage which exempts him from liability for such negligence. However, US law does not prevent parties from agreeing clauses which specifically allow parties to claim general average contribution, notwithstanding the fact that the relevant event has been caused by the claimant's negligence. Therefore, it has become customary to insert the following New Jason Clause into contracts of carriage in the event that general average is to be adjusted in the USA:

*"In the event of accident, danger, damage or disaster before or after the commencement of the voyage, resulting from any cause whatsoever whether due to negligence or not, for which, or for the consequences of which the carrier is not responsible, by statute, contract or otherwise, the goods, shippers, consignees or owners of the goods shall contribute with the carrier in general average to the payment of any sacrifices, losses or expenses of a general average nature that may be made or incurred and shall pay salvage and special charges incurred in respect of the goods."*

In many cases, it may be clear some time before the adjustment is completed that the event giving rise to general average has been caused by the default of the party which will ultimately be claiming contribution. Nevertheless, the adjusters will normally proceed with their calculation since any contributions thereby lost may, nevertheless, be covered by insurance and it will be necessary in due course to differentiate between the obligations of different insurers.<sup>9</sup>

### 10.5 The York-Antwerp Rules (YAR)

In practice, the relevant general average principles are set out in the York-Antwerp Rules which were first introduced in 1864 and which have been regularly updated ever since. These Rules have statutory force of law only in some countries.

Nevertheless, they are incorporated by agreement into almost all contracts of carriage and charterparties. Currently, there are three versions of the Rules in force – YAR 1974, YAR 1994 and YAR 2004.<sup>10</sup> It is important to establish which version is applicable under the relevant contract of carriage since there are some material differences between the various Rules. In particular, salvage payments made by the various interests at risk are to lie where they fall and are not to be re-adjusted

<sup>8</sup> See also Chapter 12.3 of the *Gard Handbook on P&I Insurance*, 5th edition.

<sup>9</sup> See Chapter 10.7 below.

<sup>10</sup> Copies of the York-Antwerp Rules 1974 and 1994 can be accessed in Appendix 1 to *A guide to General Average* by Richard Cornah at: [www.rhlg.com/pdfs/GAGuide.pdf](http://www.rhlg.com/pdfs/GAGuide.pdf) and copies of the York-Antwerp Rules 1994 and 2004 can be accessed at the website of The Association of Average Adjusters of the United States at: [www.usaverageadjusters.org](http://www.usaverageadjusters.org).

in general average under YAR 2004, unless one party to the salvage has paid all or any of the proportion of salvage due from another party. It is fair to say that YAR 2004 has not received a universally favourable reaction from the industry and many P&I clubs and BIMCO have notified their members that they do not advise their use.<sup>11</sup> However, the Comité Maritime International (CMI) has established a Working Group to conduct a general review of the YAR to ascertain whether amendments are necessary.

The YAR fall into two parts:

- The first part, consisting of seven lettered rules, sets out the general principles outlined above. For example, Rule A provides the basic definition of general average:

*“There is a general average act when, and only when, any extraordinary sacrifice or expenditure is intentionally and reasonably made or incurred for the common safety for the purpose of preserving from peril the property involved in a common maritime adventure. General average sacrifices shall be borne by the different contributing interests on the basis hereinafter provided.”*

- The second part, consisting of 22 numbered rules, deals more specifically with the types of sacrifice or expenditure that qualify in general average.

The numbered Rules are very detailed and complex and they need to be closely studied in the event of an incident to ensure that the cost of any action that may be taken will qualify for contribution in general average from the other interests at risk in due course. In the event of a conflict, the numbered Rules take precedence over the lettered Rules.

## **10.6 The Enforcement of General Average Contribution**

General average contributions become legally enforceable when the cargo is delivered at the final port of discharge or, if the voyage is frustrated at an earlier point in time, when the common adventure comes to an end as a result of that frustration. However, the general average adjustment is not normally completed until some time later. Therefore, the shipowner has a duty to ensure before the cargo and other property is released that security is provided by those interests for any general average contribution that the adjusters may calculate to be payable by them

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<sup>11</sup> See also the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 41 (General Average)).

in due course. To assist that process, the shipowner normally has a right to exercise a lien on the property to either enforce payment of general average contributions or to obtain the appropriate security.<sup>12</sup>

However, in practice, it is not usually necessary to exercise a lien since the general average adjuster will normally obtain security from the owners of the other property at risk on behalf of the shipowner in the form of a cash deposit or a general average bond supported by a general average guarantee from their insurers,<sup>13</sup> which documents contain a promise by the signatory to pay the appropriate contributions after the adjustment has been completed. However, if the cargo is uninsured, a cash deposit may be required.

Contributions in respect of freight at risk will be borne either by the shipowners and their insurers or by the cargo owners and their insurers depending on whether the freight is payable on completion of the voyage or after loading. If freight is payable on completion of the voyage it will be at the risk of the shipowners and their insurers whereas, if it is payable in advance after loading and non-returnable (ship and/or cargo lost or not lost), it will be at the risk of the cargo owners and their insurers. In the latter event, the value of the freight will be included in the value of the cargo and freight will not contribute separately.

### 10.6.1 Non-Separation Agreements

The underlying rationale of general average is that the owners of all property share the risk of a common adventure from beginning to end. Normally, the common adventure commences at the load port and terminates at the discharge port. However, difficulty can arise if the common adventure is abandoned at an intermediate port of refuge but the cargo is on-carried and delivered at the contemplated discharge port by another vessel. In such circumstances, the relevant contributory values should normally be the value of the relevant properties at the time when the original carrying ship and the cargo parted company at the intermediate port. Therefore, the cargo will usually be required as a condition of its release for on-carriage to provide a Non-Separation Agreement<sup>14</sup> in addition to the other securities to which reference is made above. The Non-Separation Agreement normally provides that the general average shall be adjusted as though the forwarding had not taken place. The result, therefore, is, that the shipowner will continue to be entitled to receive contributions from the cargo interests for crew wages, bunkers and port charges incurred during repairs, but any additional cost

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<sup>12</sup> See Chapters 24.3.1.2 and 24.3 (Security Enforcement Measures).

<sup>13</sup> Copies of these documents can be accessed in Appendices B and C to *A guide to General Average* by Richard Cornah at: [www.rhlg.com/pdfs/GAGuide.pdf](http://www.rhlg.com/pdfs/GAGuide.pdf).

<sup>14</sup> A copy of a Non-Separation Agreement can be accessed in Appendix D to *A guide to General Average* by Richard Cornah at: [www.rhlg.com/pdfs/GAGuide.pdf](http://www.rhlg.com/pdfs/GAGuide.pdf).

of forwarding the cargo to the destination in the other vessel that exceeds the cost that would have been incurred in any event if the damaged ship had completed the voyage herself, is recoverable in general average as a substitute expenses under YAR Rule F only up to the extent that such forwarding has saved the general average expenditure that would otherwise have been incurred.

## **10.7 Insurance**

### **10.7.1 Cargo Insurers<sup>15</sup>**

General average contributions from cargo are normally covered by standard cargo policies such as the ICC clauses and cargo insurers are normally prepared to put up security for such claims when demanded by general average adjusters.

### **10.7.2 Hull and Machinery Insurers<sup>16</sup>**

General average contributions from ships are normally covered by standard hull and machinery policies and hull and machinery insurers are normally prepared to put up security for such claims when demanded by general average adjusters. However, where there are numerous cargo receivers and/or the claims for general average contributions from individual cargo receivers or the owners of freight, bunkers, containers or other property are small, the cost of producing a general average adjustment and collecting individual contributions may be uneconomic. Therefore, it has become common for hull and machinery policies to include General Average Absorption Clauses<sup>17</sup> which give the assured the option to require the underwriters to 'absorb' up to an agreed amount a claim that the insured shipowner has against other interests for general average contribution. Such clauses also avoid the delay which might otherwise occur at ports of discharge whilst general average securities are negotiated and provided. Therefore, such clauses are used particularly often in the container trade and normally provide that hull and machinery insurers will 'absorb' general average claims up to a mutually acceptable figure (which is normally in excess of USD 100,000).

### **10.7.3 Marine Container Insurers**

There are various specialist insurers who provide cover for the liability of container owners to pay general average contributions pursuant to standard clauses such as the Institute Containers Clauses-Time 1/1/87 or the Institute Container Clauses – Time Total Loss, General Average, Salvage, Salvage Charges, Sue and Labour 1/1/87.

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<sup>15</sup> For more detailed commentary see Chapter 26.3.3 (The Structure of Marine Insurance).

<sup>16</sup> For more detailed commentary see Chapter 26.3.1.1 (The Structure of Marine Insurance).

<sup>17</sup> A commentary on different forms of General Average Absorption Clauses can be found in Gard News 170 (2003).



### 10.7.4 P&I insurers<sup>18</sup>

P&I insurers will normally provide cover for the following claims:

- General average contributions which are not recoverable from cargo or other interests because of the shipowner's breach of the contract of carriage;
- General average contributions from the ship which are not recoverable under the hull and machinery cover of the ship (including any excess liability policy) because the valuation of the ship for the purposes of general average contribution is deemed to be higher than the sum insured under such policies. However, such cover may be available only if the P&I insurer exercises its discretion to provide cover in the particular case.<sup>19</sup>

It is not unusual for the preparation of a general average adjustment (and the subsequent litigation) to take a number of years. Therefore, where the shipowners' efforts to recover contributions have failed or are unlikely to succeed without significant delay, P&I insurers may have the discretion to advance funds to shipowners in appropriate cases provided that countersecurity is provided by the shipowners in the event that the insurers are entitled to recovery of the advance in due course.

### 10.8 Special Charges

Special charges are expenditures which are incurred in safeguarding or preserving property even where there is no common danger to the maritime adventure. Therefore, the York-Antwerp Rules have no relevance to them. The most common example is the expenditure incurred initially by shipowners in storing damaged cargo ashore. Such charges are not subsequently shared between other members of the common adventure but are ultimately borne in full solely by the cargo owner. However, if the special charges have been caused by a breach of contract on the part of the carrier, the cargo owners may be entitled to refuse payment.

Whilst special charges are expenditures which are incurred where there is no common danger, they may in some instances be incurred after there has been a general average incident and in circumstances where it is not yet completely clear whether the relevant expenditure constitutes a general average expenditure or special charges. In such circumstances, the general average adjustment will usually make a distinction between the two types of expenditure.

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18 See also Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rules 41 and 63.1.i).

19 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 41 b (General Average)).

The shipowner normally has a right to exercise a lien on the cargo to either enforce payment of special charges or to obtain the appropriate security.<sup>20</sup> However, in practice, if the general average adjusters are to consider whether the expenditure constitutes a general average expenditure or special charges, the general average securities that they obtain from the cargo interests will normally also secure payment of special charges.

## 10.8.1 Insurances

### 10.8.1.1 Cargo Insurance<sup>21</sup>

Claims for special charges on cargo are normally covered by standard cargo policies such as the ICC clauses and cargo insurers are normally prepared to put up security for such claims when demanded by shipowners or general average adjusters.

### 10.8.1.2 Hull and Machinery Insurers<sup>22</sup>

Special charges on the ship are normally covered by the standard hull and machinery policies depending on the nature of the charges and the terms of the policy.

### 10.8.1.3 P&I Insurers<sup>23</sup>

P&I insurers will normally provide cover for claims for special charges which are not recoverable from cargo or other interests because of the shipowner's breach of the contract of carriage.

## 10.9 Claims Management

Shipowners have a duty in appropriate circumstances to declare general average and to appoint suitably qualified adjusters. Failure to do so may not only incur liability to other interested parties but also prejudice the shipowners' insurance cover. Therefore, shipowners should take care to ensure that their contracts of carriage contain suitable general average clauses and that the ship's crew is instructed to follow the guidance recommended in Chapter 3.9.2 of the *Gard Guidance to Masters*. Furthermore, a failure by the shipowners to ensure that they take all steps that may be reasonably necessary to protect the shipowner's rights in general average (such as the failure to obtain the necessary security from cargo interests before the cargo is released) may also cause losses and expenditure which are not insured.<sup>24</sup>

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<sup>20</sup> See Chapter 24.3.1.2 (Security Enforcement Measures).

<sup>21</sup> See Chapter 26.3.3 (The Structure of Marine Insurance).

<sup>22</sup> Chapter 26.3.1.1 (The Structure of Marine Insurance).

<sup>23</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 41 (General Average)).

<sup>24</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 41.a General Average)).

### **10.10 Case Study**

A vessel experiences an engine breakdown during heavy weather. Cargo on deck and below deck is damaged and the vessel lists heavily. As a result the master orders the jettisoning of several heavy containers on deck in order to correct the list before entering a port of refuge. As a result the shipowner incurs liabilities and costs due to the diversion to the port of refuge and for carrying out temporary repairs. The owners of the cargo in the jettisoned containers sustain a total loss. The beneficiaries of this general average sacrifice or expenditure are the shipowner, the owners of the cargo that remained on board and any other party with property at risk that was saved (i.e. time charterers with bunkers at risk). Therefore, contributions to general average are made by their respective insurers.



## Chapter 11

# People Claims<sup>1</sup>

### 11.1 Introduction

People claims are one of the most frequently occurring types of maritime claims and liability can arise in relation to the following different categories of people, who have different roles to play in relation to the ship:

- Crew members;
- Passengers;
- Persons other than crew or passengers that are carried on board such as pilots, repair gangs, supernumeraries and stowaways; and
- Other persons that are not carried on board such as stevedores, port officials and even local residents.

Claims can also arise in many forms, the most significant of which are the following:

- Personal injury and death;
- Employment terms;<sup>2</sup>
- Leisure claims;
- Fines and criminal liability.<sup>3</sup>

### 11.2 Liability to Crew Members

Significant efforts have been made to ensure higher standards of safety on board ships and this has led to a reduced number of incidents resulting in death, injury or illness. However, such incidents nonetheless continue to occur and have to be dealt with promptly and diligently by the shipowner and his insurer – usually the P&I club – whether the victims are crew members, passengers or other persons.

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1 For more detailed commentary see Chapters 15 to 17 of the *Gard Handbook on P&I Insurance*, 5th edition and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 27 (Liabilities in respect of crew), Rule 28 (Liabilities in respect of passengers) and Rule 29 (Liability for other persons on board)).

2 For more detailed commentary on these issues see Chapter 22.5 (Maritime Regulation and Compliance).

3 For more detailed commentary on these issues see Chapter 8 (Fines and Criminal Sanctions Claims).

Following any maritime casualty, the first priority is to take steps to ensure the safety of the crew and other persons who are either on board or in the vicinity of the ship and who may be in potential danger. This may prove to be challenging since shipboard personnel may have died or been injured or may be otherwise incapable of carrying out their duties. Furthermore, if the incident has occurred in a remote location, it may not be possible to provide assistance easily and promptly. Alternatively, the situation may be equally challenging if a serious casualty occurs in a populated area where other persons, property and infrastructures may be significantly affected.

It is also important to ensure that the steps that are taken to ensure the safety and well-being of personnel are co-ordinated with other actions which may be necessary to protect the environment and the salvage of the ship and other property.

On 20 August 2013, the Maritime Labour Convention 2006 (MLC)<sup>4</sup> will come into force, which will mean that, for the first time, there will be an international convention that includes provisions that govern liability for the illness of, injury to, or the death of crew members.

The MLC consolidates and updates more than 68 international labour standards related to the maritime sector which have been adopted over the last 80 years and aims to be globally applicable, easily understandable and uniformly enforced. Title 4 of the convention is of particular interest to shipowners and their P&I clubs in that it imposes minimum standards for:

- Medical care on board ship and ashore;
- Shipowners' liability in respect of the financial consequences of illness and injury;
- Health and safety protection and accident prevention;
- Access to shore based welfare activities;
- Social security.

The minimum standards imposed by the convention mean that crew contracts of employment, seafarer's articles or collective bargaining agreements (CBAs) which do not meet those standards cannot be enforced in countries that have ratified the convention and incorporated it into domestic law. However, if the relevant articles or CBAs do satisfy the minimum standards imposed by the convention, they will continue to govern the liability of the employer.

Pending implementation of the MLC, liability will continue to be governed by national domestic laws.

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<sup>4</sup> For more detailed commentary see Chapter 22.5.1 (Maritime Regulation and Compliance).

### 11.2.1 Contractual Liability

Shipowners will normally conclude legally binding contracts with crew members and/or the labour organisations that represent them in the form of individual contracts of employment, seafarer's articles of agreement or collective bargaining agreements (CBAs). Such contracts normally include not only the terms of the employment but also provisions establishing a right of assistance and financial compensation in the event of illness, injury or death.

#### 11.2.1.1 Individual Employment Contracts

Such contracts can be concluded either directly between shipowners, managers or operators and the crew members or as a result of the involvement of a crewing agency which can act as an agent for either party. The relevant contract may be for a single voyage or for longer-term service but, unlike a CBA or Seafarer's Articles, it is a private agreement negotiated solely between the employer and the crew member.

#### 11.2.1.2 Collective Bargaining Agreements (CBAs)

Collective bargaining agreements are normally negotiated between a shipowner or a shipowners' association and the corresponding national seafarers' unions, many of which are affiliated with the International Transport Workers' Federation (ITF). Collective agreements of this type contain detailed terms and conditions of employment for all relevant union members, including terms that regulate the compensation that is payable in the event of illness, injury or death. Some CBAs also contain law and jurisdiction clauses, the effect of which is to incorporate the statutory provisions of the chosen forum into the contract.

One important example is that which regulates the employment of Filipino crew members. The Philippines supplies the largest number of crew members to ocean-going vessels and the employment of such crew members is subject to the minimum standards set out in the Standard Employment Contract of the Philippine Overseas Employment Administration (POEA). Employers are not permitted to reduce these statutory benefits including the amount of compensation that is payable in the event of death or personal injury and the dispute resolution forums for crew claims in the Philippines (Labor Arbiter, National Labor Relations Commission and the Filipino Courts) are normally very vigilant in seeking to protect the rights of Filipino crew members.

#### 11.2.1.3 Seafarer's Articles

In many countries, the local law requires employers and crew members to agree to enter into seafarer's articles which normally take the form of a single agreement between the shipowner or manager and all members of the crew on board a particular ship for one or more voyages.

### 11.2.2 Statutory Obligations

The local legislation of the flag state will often protect certain fundamental labour rights including the duty of employers to provide a safe working environment, to restrict working hours and to ensure that compensation is available in cases of illness, injury or death. Local social security schemes may also oblige employers to take out compulsory insurance (frequently from a P&I club) to cover such obligations.

However, the matter can be more complicated in the event of a maritime casualty, since the shipowner may also incur liability pursuant to the statutory law of the following countries:

- The country where the crew member is a citizen and/or is domiciled;
- The country where the employer, shipowner, manager or operator of the ship is domiciled or has their principal place of business;
- The country where the incident, or the act which caused such incident, occurred;
- The country where the crew member entered into the relevant employment contract;
- The country designated to have jurisdiction in the contract of employment.

In the final analysis, the law which will be applied, and the weight that is to be given to each source of law in any particular dispute, will depend upon the law of the country where the court or arbitration panel determining the claim is situated. Therefore, claims arising as a result of the illness of, injury to, or the death of crew members may be subject to complex issues of international private law and result in much forum-shopping.<sup>5</sup>

### 11.2.3 Common Law Liability

In some countries, such as the United Kingdom and the United States, a crew member may be entitled to claim damages in tort in addition to his entitlements under contract if it is established that the illness, injury or death has resulted from the negligence of the employer.<sup>6</sup>

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<sup>5</sup> For more detailed commentary see Chapter 19.2 (Law and Jurisdiction).

<sup>6</sup> For more detailed commentary relating to liability for negligence or tort see Chapter 14 of the *Gard Handbook on P&I Insurance*, 5th edition.



### 11.2.4 Liability in the United States

Claims are often brought in the United States for very large monetary awards both under local statutes and under what is known as the 'General Maritime Law'.

#### 11.2.4.1 Statutory Liability

The Jones Act, 1920 entitles a seaman (or his next of kin) to claim certain damages from his employer if the latter is guilty of negligence resulting in injury to (or death of) the seaman during the course of his employment. For the purpose of the Act a 'seaman' is any person who is employed on board the ship, which includes, in the case of cruise ships, hotel and catering staff, regardless of nationality or the ship's flag. Consequently, claims may be brought in US courts by crew members (or their next of kin) who are not US citizens and not serving on US flag ships if the incident which caused the injury (or death) occurred in US waters.

Damages recoverable under the Act may include medical expenses, lost wages and claims for loss of future earning capacity. In case of death, the next of kin may claim damages for funeral expenses, loss of direct financial support, as well as compensation for the value of lost services in the household. In the event of the death of a US seaman caused by a wrongful act outside US territory, the next of kin may alternatively bring a claim *in rem* against the ship or a claim *in personam* against the person or corporation that is responsible for the death under the Death on the High Seas Act (DOHSA). Claims that are brought under the Jones Act can only be brought against the employer whereas any other person or corporation may be sued pursuant to the DOHSA. The provisions and scope of the two acts are not identical and therefore, in appropriate circumstances, the estate of a deceased seafarer can sue the employer under the Jones Act and any other person or corporation under the DOHSA.

#### 11.2.4.2 The General Maritime Law

Under the general maritime law of the United States a seaman who becomes injured or suffers illness whilst in the service of the ship within the jurisdiction of the USA is entitled to receive 'maintenance and cure'. Such rights apply regardless of the nationality of the seaman or the flag of the ship and regardless of whether the illness or injury was caused by the negligence of the employer. 'Maintenance' is the right to a daily subsistence allowance, primarily for food and lodging, and 'Cure' is the right to receive whatever medical and other treatment that may be necessary until the crew member reaches the so-called stage of 'maximum medical cure', which is the stage when further treatment is deemed not to have further curative effect. The seaman's employer is obliged to take all reasonable steps to ensure that the ill or injured seaman receives proper care and treatment and is responsible for the

payment of reasonable medical expenses in this regard. Callous and deliberate failure to pay the cost of maintenance and cure may expose the employer to punitive damages.

Furthermore, the seaman may be entitled to claim damages if he is able to prove that the illness or injury was caused by the unseaworthiness of the ship or by the negligence of a third party (e.g. the owners of another ship with which the carrying ship has collided).

Whilst some crew employment contracts purport to limit the amount of compensation that is payable in the event of injury or death, such provisions may not protect the employer when liability is incurred pursuant to statute or the general maritime law.

### **11.3 Liability to Passengers**

Liability to passengers can arise under:

- Contract;
- International conventions;
- Local statutes;
- The common law.

#### **11.3.1 Contractual Liability**

The primary source of the legal relationship between a passenger and the carrier is the contract of carriage. However, contractual provisions may be superseded by international conventions, national statutes or the common law depending on the laws that are applied in any given forum.

##### **11.3.1.1 The Passenger Ticket Contract**

In most cases the contract of carriage for passengers, will be the terms and conditions stated in the ticket issued by the carrier to the passenger. However, if the contract of carriage is concluded with a tour operator or a travel agent acting on behalf of an undisclosed principal, that tour operator or travel agent may be held to be the contractual carrier and to be contractually liable to the passenger. However, the operator of the passenger ship will, nevertheless, be the 'performing carrier' and may incur direct liability to passengers in such capacity under statute or in tort, and may furthermore, be liable to indemnify the tour operator or travel agent in respect of liabilities incurred by them to passengers pursuant to the terms of their contract.

The terms and conditions that are included in the passenger ticket normally impose liability on the carrier for the death, injury or illness of passengers caused by incidents that occur after embarkation and before disembarkation of the passenger from the ship, whether the incidents are 'marine-type' incidents such as collision, stranding, explosion or fire, or 'hotel-type'<sup>7</sup> incidents related to guest cabins, catering, leisure services or entertainment. However, the passenger ticket may seek to exonerate the carrier from liability for services or activities that are not provided on board (such as, for example, shore excursions), or for services and activities that are provided on board by independent contractors who are not the servants or agents of the carrier.

#### 11.3.1.2 Limited Freedom of Contract

Most contracts for the carriage of passengers are subject to the provisions of The Athens Convention on the Carriage of Passengers and their Luggage by Sea 1974 (The Athens Convention)<sup>8</sup> which has mandatory rules that regulate liability, compensation and limitation rights in the event of the death, injury or illness of passengers. Where applicable, the Athens Convention renders 'null and void' any passenger ticket terms that are in conflict with the mandatory provisions of the convention. The passenger ticket may also include an express choice of law and jurisdiction clause but the enforceability of such a clause depends to a large extent on the rules of law and/or public policy and/or attitude of the court in the country where the claim is asserted.<sup>9</sup> Such clauses may also be considered to be 'null and void' to the extent they are in conflict with the provisions of Articles 17 and 18 of the Athens Convention which gives the claimant the option of bringing claims in a choice of four different jurisdictions.

The United States<sup>10</sup> is not a signatory to the Athens Convention, but under US law contractual terms included in the passenger ticket cannot be enforced unless they have been brought to the passenger's attention in a very clear and timely manner.

#### 11.3.2 International Conventions

The convention binds only those countries that have adopted the convention<sup>11</sup> and applies to international carriage where:

- 1 The ship is flying the flag of, or is registered in, a Convention State;
- 2 The contract of carriage was made in a Convention State;
- 3 The carriage commences or terminates in a Convention State.

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<sup>7</sup> See Chapter 11.3.3 below.

<sup>8</sup> See Chapter 11.3.2 below.

<sup>9</sup> See also Chapter 19.5 (Law and Jurisdiction).

<sup>10</sup> See Chapter 11.3.3.1 below.

<sup>11</sup> A list of the countries that have adopted the convention can be accessed via the IMO website at: <http://www.imo.org/About/Conventions/StatusOfConventions/Pages/Default.aspx>.

However, courts in other countries such as the United States have been prepared to enforce the provisions of the Athens Convention when the convention is incorporated into the passenger ticket contract by agreement.<sup>12</sup>

The convention provides that "*the carrier*" (and/or "*performing carrier*") is liable if a passenger dies, is injured or suffers illness as a result of the carrier's fault or neglect or that of his employees or agents acting in the course of their employment. However, when such events occur as a result of a 'shipping incident' which is defined as a shipwreck, collision, stranding, explosion, fire or defect in the ship, fault or neglect is presumed and the onus is on the carrier to prove the contrary. Therefore, in the majority of cases, the claimant will normally be required merely to prove that the event occurred as a result of one of such occurrences and the carrier will then have the difficult task of proving that he was not guilty of fault or neglect. However, if injury has been caused by other risks such as slipping or falling on deck, or if illness has been caused by the lack of proper hygienic standards in the preparation of food or the cleaning of bathrooms or swimming pools, the onus of proof is reversed and the onus is on the passenger to prove fault or neglect.

In any event, irrespective of the cause, the passenger has the obligation to prove the extent of the loss or damage, and the liability of the carrier can be reduced, in whole or in part, if the carrier can prove contributory fault on the part of the passenger.

The contractual carrier is exposed to such liability throughout the whole carriage whereas a performing carrier may only be liable in respect of that part of the overall carriage that is actually performed by him. In the majority of cases, the carrier and the performing carrier have joint and several liability under the convention which means that the claimant can choose to bring a claim against either one or both of them.

The Athens Convention also regulates liability to passengers for the loss of, or damage to, their luggage<sup>13</sup> or vehicles. Article 3 stipulates that the carrier shall be liable "*if the incident which caused the loss was due to the fault or neglect of the carrier*" except that, as in the case of claims for personal injury or death, fault or neglect will be presumed if the loss is caused by a 'shipping incident' as defined above.

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<sup>12</sup> See Chapter 16.3.1.6 of the *Gard Handbook on P&I Insurance*, 5th edition.

<sup>13</sup> However, the carrier is not liable for the loss of, or damage to, valuables unless they have been deposited with the carrier for safe-keeping during the transit.

### 11.3.2.1 Limitation of Liability<sup>14</sup>

The Athens Convention permits the carrier to limit his liability as follows:

Claim	Liability Limit
Death or personal injury	SDR 46,666 per passenger
Cabin luggage	SDR 833 per passenger
Vehicles	SDR 3,333 per passenger
Other luggage	SDR 1,200 per passenger

However, countries that have ratified the convention are allowed to increase the above limits.

The limits apply ‘*per carriage*’ not per incident. Therefore, if a passenger were to be injured twice during the same cruise, the carrier would be entitled to rely on the one limit of SDR 46,466 to protect himself against both claims.<sup>15</sup> The limits apply to the individual claims that are brought by individual passengers. However, the carrier may also be entitled to rely on a different form of limitation (global limitation) if the totality of the individual claims (after applying the Athens Convention limits) exceed the global limit.<sup>16</sup>

The right to limit liability is lost only if the claimant proves that the loss, damage or injury has resulted “*from an act or omission of the carrier done with intent to cause such damage, or recklessly and with knowledge that such damage would probably result.*” It follows that the right to limit liability will be unbreakable in most circumstances.

<sup>14</sup> Higher limits apply under the 2002 Protocol to the Athens Convention. See Chapter 11.3.2.4 below.

<sup>15</sup> In contrast, the 2002 Protocol to the convention provides that the (higher) limit applies per incident – see Chapter 11.3.2.4 below.

<sup>16</sup> See Chapter 11.3.2.5 below.

### 11.3.2.2 Jurisdiction for Claims

The convention provides that passengers have the option to bring proceedings in the courts of any convention state that is:

- 1 The principal place of business of the carrier; or
- 2 The place of departure or destination; or
- 3 The passenger's own state; or
- 4 The place where the contract of carriage was made;

provided, in the case of 3 and 4, that the carrier has a place of business in, and is subject to the jurisdiction of that state.

This choice of jurisdiction gives the claimant a valuable litigation advantage.

### 11.3.2.3 Time Limit for Claims

Claims for personal injury, or for the loss of, or damage to luggage, are time barred two years after the date the passenger disembarked and in the case of death claims, two years after the date on which the passenger should have disembarked. Where the claim relates to death that has occurred after disembarkation but has been caused by injury prior to disembarkation, the time limit is three years from the date of disembarkation.

### 11.3.2.4 The 2002 Protocol to the Athens Convention 1974<sup>17</sup>

In 2002 a very important Protocol to the Athens Convention was adopted. The 2002 Protocol includes many of the principles implemented in other international maritime liability conventions, such as the Civil Liability Convention regulating pollution liability and compensation, and its provisions differ significantly from the original convention in several respects:

- The carrier is strictly liable (subject to the limit of liability specified below) in the event of the death of, or personal injury to, a passenger resulting from a "shipping incident" which is defined as the "shipwreck, capsizing, collision or stranding of the ship, explosion or fire in the ship, or defect in the ship", unless the carrier proves that the incident resulted from "an act of war, hostilities, civil war, insurrection or a natural phenomenon of an exceptional, inevitable and irresistible character"; or "was wholly caused by an act or omission done with the intent to cause the incident by a third party." Where death or personal injury is caused by a non-shipping incident, the position remains as it is under the Athens Convention and the carrier is liable only if the claimant is able to prove that the death or personal injury has been caused by the fault or neglect of the carrier.

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17 At the time of writing the 2002 Protocol is not yet in force internationally and will come into force twelve months after it has been ratified by ten States countries. However, EU Regulation 392/2009 makes the 2002 Protocol binding on the member states of the European Union as from the 31 December 2012.

- The liability of the carrier for the death of, or personal injury to, a passenger caused by a “shipping incident” is increased from SDR 46,666 per passenger per carriage to SDR 250,000 per passenger for each distinct occasion on which the passenger may be injured. Therefore, the limit is substantially increased and applies on each occasion that the passenger may be injured during the carriage rather than merely as one limit for all claims that the passenger may have during the carriage. However, if the claim exceeds the limit of SDR 250,000 per passenger, the carrier is liable subject to the increased limit of SDR 400,000 per passenger for each distinct occasion on which the passenger may be injured unless the carrier proves that the incident which caused the loss occurred without his fault or neglect.<sup>18</sup> Finally, the Protocol allows countries to introduce yet higher limits or even unlimited liability not only to their national flag carrying ships but also to foreign flag ships which visit their ports or which are otherwise subject to their jurisdiction.
- The limits of liability for the loss of, or damage to, cabin luggage and other property are increased as follows: cabin luggage to SDR 2,250 per passenger, per carriage; vehicles to SDR 12,700 per vehicle, per carriage; and other luggage to SDR 3,375 per passenger, per carriage.
- Carriers are required to maintain insurance or other financial security (such as the guarantee of a bank or similar financial institution) that is sufficient to underwrite the minimum limit of SDR 250,000 per passenger on each distinct occasion and to provide documentary evidence in the form of a certificate attesting that insurance or other financial security is in force. Such certificates will be provided by the International Group P&I Clubs in so far as concerns risks other than war and terrorism risks. These certificates are referred to as ‘Non-War Passenger Blue Cards’ and are backed by the International Group’s normal pool and reinsurance covers.
- Since the International Group P&I Clubs do not cover war risks, certificates in respect of war and terrorism risks (referred to as ‘War Passenger Blue Cards’) are not backed by the International Group’s normal pool and reinsurance covers, and are therefore provided by other insurers and with distinctly different reinsurance cover.
- Finally, the 2002 Protocol introduces a tacit acceptance procedure that is intended to simplify the procedures for raising limits of liability again in the future.

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<sup>18</sup> See also Chapter 11.2.3 below.

### 11.3.2.5 The 1976 Limitation Convention<sup>19</sup>

The limits of liability that are set out in the Athens Convention and the 2002 Protocol thereto are restricted to the claims that may be brought by individual claimants for death or personal injury. However, the carrier may also be entitled to limit his liability to a specified sum under other international conventions such as the 1976 Convention on Limitation of Liability of Maritime Claims, or the 1996 Protocol thereto, or the 1957 Limitation Convention (which are usually referred to as the tonnage limitation conventions) for all qualifying claims of different types (including claims for death or personal injury) that arise on any one distinct occasion.

Under the 1976 Limitation Convention the shipowner is entitled to limit his liability for loss of life or personal injury to passengers arising on any distinct occasion to SDR 46,666 multiplied by the number of passengers which the ship is authorised to carry, but not exceeding SDR 25 million irrespective of such number of passengers. For example, a ship certified to carry 200 passengers, has a limit of SDR 9,333,200. For ships certified to carry 536 passengers or more, the limit is SDR 25 million. Under the 1996 Protocol to the 1976 Convention the limit is increased to SDR 175,000 multiplied by the number of passengers that the ship is authorised to carry without any overall maximum figure. Therefore, a major casualty involving one of the biggest cruise ships carrying 5,000 passengers could potentially result in a limit of SDR 875 million.

If passenger claims are subject to both the Athens Convention (or the 2002 Protocol thereto) and to one of the tonnage limitation conventions, the carrier is entitled firstly, to reduce his liability to the individual claims that may be brought by passengers under the Athens Convention, and then, if the total of such claims (after application of the Athens Convention limits) exceed the limits specified under the relevant tonnage limitation convention, the individual passenger claims may be further reduced pursuant to the provisions of the relevant tonnage limitation convention on a *pro rata* basis. Similar rules also apply to the limitation of cargo claims.<sup>20</sup>

### 11.3.3 National and Regional Laws

The protection that is afforded to passengers in those countries that have not accepted or ratified the Athens Convention is very diverse. In some countries there is no statutory protection for passengers, whereas in others, such as Germany, the Scandinavian countries, the United Kingdom and the United States, the protection is more generous than that which is provided by the Athens Convention. Furthermore,

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<sup>19</sup> For more detailed commentary see Chapter 21.3 (Limitation of Liability).

<sup>20</sup> An example of the relevant limitation methodology (as it applies to cargo claims) can be found in Chapter 28.5 of the *Gard Handbook on P&I Insurance*, 5th edition.



whilst some countries have no specific legislation for the protection of passengers, claimants may be able to rely on general common law remedies or on consumer protection legislation.

### 11.3.3.1 Liability in the United States<sup>21</sup>

Under the law of the United States a carrier owes a duty of reasonable care to passengers, but in many cases, there is a legal presumption that the carrier has been negligent, thereby requiring the carrier to disprove negligence in order to escape liability. Where the activity is uniquely maritime in nature (e.g. when using tenders or gangways or engaging in safety drills), the carrier is subject to a more stringent duty of care on the basis that passengers require greater protection when engaged in activities that they would not normally encounter ashore. Nevertheless, passengers are required to exercise reasonable care for their own safety.

Should a casualty or other event interfere with, or disrupt, a planned voyage, the provisions of most passenger contracts require the carrier to return the passenger to the port of embarkation or the expected port of disembarkation. Therefore, the duty of reasonable care may well require the carrier to arrange and pay for alternative travel arrangements and, if the passengers are disembarked in a remote port, to provide reasonable assistance through a local port agent.

If a passenger has died whilst on the high seas as a result of the negligence or other wrongdoing of the carrier, liability is governed exclusively by the provisions of the US federal statute, Death on the High Seas Act (DOHSA).<sup>22</sup>

In most cases, US law prohibits a carrier from contractually limiting his liability for negligence. However, a carrier may limit his overall liability by operation of law if there is an adequately worded disclaimer in the ticket contract.

Under the law of the United States the owner or charterer of a passenger ship that either is, or may become, engaged in voyages to or from US ports is required to provide a guarantee from an authorised insurer, surety company or other provider, for legal liabilities that he may incur for the death of, or for injury to, passengers or other persons who are carried on board during such voyages. The guarantee is to be provided to the US Federal Maritime Commission (FMC) and is normally supplied by the ship's P&I club.<sup>23</sup>

<sup>21</sup> For more detailed commentary see Chapter 16.4.2 of the *Gard Handbook on P&I Insurance*, 5th edition.

<sup>22</sup> See Chapter 11.2.1.4.1 above.

<sup>23</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 58.2 i (War Risks)). A specimen FMC section 2 guarantee can be found on [www.fmc.gov/images/pages/fmc133b.pdf](http://www.fmc.gov/images/pages/fmc133b.pdf).

Liability under the FMC guarantee will be triggered if the owner or charterer of the relevant passenger ship has not discharged his liability for such death or injury within 21 days of either a final judgment which is no longer subject to any appeal, or of a compromise settlement which has been approved by the guarantor.

### **11.3.3.2 Liability in the European Union**

The EU has, by means of the EU Passenger Liability Regulation (EC) No 392/2009 (the PLR), sought to extend the provisions of the 2002 Protocol to the Athens Convention to passenger ships that are engaged in domestic seagoing voyages and to certain classes of vessels operating on inland waterways. The PLR is intended to work in tandem with the 2002 Protocol and requires EU member states to ratify or accede to the 2002 Protocol. However, notwithstanding the fact that member states are unlikely to do so by the end of 2012, the PLR is to come into effect throughout the EU on 1 January 2013.

The PLR replicates most of the key provisions of the 2002 Protocol such as the compulsory insurance and certification requirements but also seeks to extend and expand its provisions by, for example, extending the concept of cabin luggage to include mobility equipment and obliging the carrier to make advance payments sufficient to cover immediate economic needs where the death of, or personal injury to, a passenger is caused by a 'shipping incident'. The International Group P&I Clubs have confirmed their agreement to the issuance of blue cards for non-war risk liabilities in respect of both international and domestic trading voyages covered by the PLR. This agreement does not, however, extend to blue cards concerning war and terrorism risks.

### **11.3.3.3 'Hotel-type' Claims**

Large cruise ships provide services to passengers that are akin to those provided by hotels and are distinguishable from the more traditional 'marine-type' services that have been traditionally provided by ships. Such services include catering, beauty treatments, shore excursions, entertainment etc. Therefore, disputes can arise as to whether the shipowner is liable not only for the traditional 'marine-type' risks but also for these 'hotel-type' risks.

Much depends on the type of passenger contract that has been provided by the shipowner to the passenger. However, even if the contract provides for 'hotel-type' services, it is by no means certain that claims relating to such services are regulated by international conventions such as the Athens Convention. For example, the definition of "*carriage*" in Article 8 (a) of the Athens Convention indicates that the convention does not apply to claims for death or injury incurred whilst a passenger is ashore on an excursion whilst Article 3 provides that the "*carrier*" is liable only if the incident that has caused death or personal injury "*was due to the fault or neglect of*

*the carrier or of his servants or agents acting within the scope of their employment.”* Therefore, if the incident has been caused by an independent contractor, such as a hair-dresser, the convention would not seem to apply.

Notwithstanding the lack of clarity that seems to apply under the Athens Convention and/or the 2002 Protocol thereto, shipowners can expect to be held liable for ‘hotel-type’ risks under regional or local laws in many parts of the world. For example, liability may arise in the European Union pursuant to Directive 90.314/EEC (The European Package Travel Directive) which applies to the provision of ‘package’ travel services which include at least two of the following services: transport, accommodation and other tourist services that account for a significant proportion of the package price.

Article 5.1 of the Directive requires the member states of the European Union to take steps to ensure that the party or parties that organise or sell package tours are *“liable to the consumer for the proper performance of the obligations arising from the contract, irrespective of whether such obligations are to be performed by that organiser and/or retailer or by other suppliers of services without prejudice to the right of the organiser and/or retailer to pursue those other suppliers of services.”* Therefore, shipowners who engage directly in the organisation or sale of such packages would appear to run the risk of being held liable for death or personal injury claims occasioned by the acts or omissions of independent contractors that are employed in ‘hotel-type’ activities.

#### **11.4 Liability to Other People**

Persons other than crew members and passengers are often on board ships whilst they are at sea. Some persons are carried on board the ship during the whole or part of the voyage in order to provide services, or are otherwise on board with the consent of the master (e.g. pilots, supercargoes, riding repair crew etc.). Other persons may be carried on board despite the fact that this was not planned or that the master did not originally consent to their presence on board (e.g. stowaways,<sup>24</sup> refugees rescued at sea etc.). Furthermore, some persons may be on board whilst the ship is in port either because they have some function to perform (e.g. stevedores, port agents, government and local officials, ship suppliers etc.) or even when they have no function to perform but are merely visiting the ship or crew members.

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<sup>24</sup> See Chapter 11.4.5 below.

In general terms the shipowner has a duty of care to all of these categories of persons and, since there are no relevant international conventions, the duty may arise either solely or collectively under:

- Contract; or
- Statute; or
- The common law.

The duty of care is not normally absolute since persons that are on board also have a duty to take reasonable precautions for their own safety and to comply with any safety instructions that may be made by the ship's crew. The standard of care that is expected of them will often differ depending on the knowledge and experience that such persons are expected to have. For example, a technical person who has experience in ship operations is normally expected to exercise a greater degree of caution for his own safety than a family member who is visiting one of the crew members.

#### **11.4.1 Contractual Liability**

If the person that has died or become injured is an employee of a company with whom the shipowner has a contractual relationship (e.g. a stevedoring company) the shipowner may either have a direct liability to the person concerned and/or may be liable to indemnify the person's employer in respect of any compensation that is payable by the employer in the first instance. The legal basis for such an indemnity may be set out expressly in the contract between the shipowner and the person's employer, or it may be deemed to be an implied term. In most circumstances, for any such contractual liability to be incurred, the death or injury must have been caused by negligence by the shipowner or his servants or agents and such contracts will also normally have an express law and jurisdiction clause which establishes where claims are to be brought and which law is to govern.

Notwithstanding the contractual relationship between the shipowner and the employer, the injured person may, nevertheless, decide to seek compensation directly from the shipowner by way of a claim in tort. Alternatively, the injured person may deem it advantageous to bring the claim against his employer and leave it to the employer to claim an indemnity from the shipowner under the terms of the contract between them. In order to avoid such complications contracting parties may in some instances enter into mutual indemnity agreements whereby each party assumes responsibility for, and holds the other harmless against liability for, the death or injury of their own employees regardless of which party is actually at fault. Such arrangements, usually called 'knock-for-knock,' are permissible under the laws of most jurisdictions.

### 11.4.2 Statutory Liability

The shipowner is generally obliged to ensure that the ship provides a safe environment for persons, who are either carried on board to provide services, or persons who are visiting or working on board the vessel whilst in port and additional obligations may also be imposed by local statutes, as well as regulations that apply to the particular port or harbour in question. In such circumstances, the shipowner may not only be liable in damages to claimants but may also be subject to civil or criminal liability if such obligations are not observed.

For example, US longshoremen who are injured or killed whilst working on board the ship as a result of the negligence of the shipowner, are entitled to receive statutory compensation from the shipowner under Section 905(b)<sup>25</sup> of the Longshore and Harbour Workers Compensation Act (LHWCA) section 905(b).<sup>26</sup> Similarly, if the person dies whilst on board the ship on the high seas as a result of the negligence or other wrongdoing of the carrier, the carrier may incur liability under the provisions of the US federal statute, Death on the High Seas Act (DOHSA).<sup>27</sup>

### 11.4.3 Liability at Common Law

Even if the death or injury is incurred in a country which has no relevant statutory provisions, it is likely that the shipowner will be held to have a duty of care to ensure that persons attending on board are not injured, and will incur liability to such persons in tort if they are injured as a result of the negligence of the shipowners or their employees.

### 11.4.4 Claims Related to Stowaways

A 'stowaway' has been defined as a person who, at any port or place in the vicinity thereof, secretes himself in a ship without the consent of the shipowner or the master or any other person in charge of the ship and who is on board after the ship has left that port or place.<sup>28</sup> Therefore, stowaways are distinguishable from persons that have been saved at sea.

The presence on board of stowaways may create practical challenges both for the master and crew, particularly if there are many stowaways, as well as for shore-side personnel who may be seeking to ensure that they are disembarked and repatriated

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<sup>25</sup> US case law has served to clarify the shipowner's duties and the standard of negligence to be applied under the LHWCA. A landmark case in this regard is *Scindia Steam Navigation Co. Ltd., v. Lauro De Los Santos et al.*, 451 U.S. 156 (1981).

<sup>26</sup> US case law has served to clarify the shipowner's duties and the standard of negligence to be applied under the LHWCA. A landmark case in this regard is *Scindia Steam Navigation Co. Ltd., v. Lauro De Los Santos et al.*, 451 U.S. 156 (1981).

<sup>27</sup> See Chapter 11.2.1.4.1 above.

<sup>28</sup> This is the definition that is given in the International Convention Relating to Stowaways (Brussels Convention) (1957) which is not in force.

in a proper fashion.<sup>29</sup> A common problem is how to obtain information concerning the true identity and nationality of the stowaways in order to ascertain where to disembark and arrange repatriation.

The shipowner will usually have to fund whatever costs and expenses that may be necessary to obtain permission to disembark and repatriate the stowaways, as well as the actual costs of maintenance ashore pending repatriation and the repatriation itself. Furthermore, if the immigration authorities in the country of disembarkation require an escort for the repatriation, to ensure that the stowaway is properly guided to the immigration point in his country of domicile, such costs may also have to be funded by the shipowner.

Pending arrival at a feasible port of disembarkation, the stowaway will have to be kept on board and extra precautions may be necessary to ensure that the stowaway does not jump ship, since, if this were to happen, the shipowner may be liable to pay substantial fines which may be substantially higher than all other costs and expenses that may have been incurred to ensure proper repatriation.

## **11.5 Insurance**<sup>30</sup>

### **11.5.1 General**

In the event of death, illness or injury, claims may, in some circumstances, be brought by or on behalf of the relevant person directly against the party who is legally responsible for having caused the death, illness or injury. In some jurisdictions, such claims may even be brought directly against insurers. For example, passengers may bring such claims under 'personal accident', 'travel', or similar insurances and workers may bring such claims under compulsory workers' compensation schemes. However, such insurers may then be subrogated to whatever rights the relevant person may have to bring claims against the party who is legally responsible for having caused the death, illness or injury.<sup>31</sup> Therefore, in most cases, claims will be brought either directly or indirectly against the shipowner who will require insurance protection against such liability. Such insurance cover is normally provided by P&I insurers.

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<sup>29</sup> The *Gard Guidance to Masters* provides further advice and recommendation concerning the handling of stowaways on board, including a template questionnaire recommended to obtain information related to the identity and nationality of stowaways.

<sup>30</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>31</sup> For more detailed commentary see Chapter 25.5 (The Fundamental Principles of Marine Insurance).

### 11.5.2 P&I Cover for Crew Members and Passengers<sup>32</sup>

P&I cover is normally available whether the legal liability arises under contract, international convention, local statute or the common law. However, if liability arises under contract, cover may not be available if the liability arises purely as a result of the terms of the contract, and would not have arisen but for the contract, unless the terms of the contract have been approved by the club.<sup>33</sup>

The P&I clubs that are members of the International Group of P&I Clubs normally insure their member shipowners against their legal liability:

- to pay expenses, costs, wages and damages to crew members and passengers in respect of sickness, injury and death;
- to pay the repatriation or travelling costs of crew member and passengers in case of their illness, injury or death;
- for the costs of repatriation of the body or ashes of a deceased crew member or passenger and for the cost of funeral and burial expenses.

### 11.5.3 P&I Cover for Liability to Other Persons<sup>34</sup>

The P&I clubs that are members of the International Group of P&I Clubs normally insure their member shipowners against their legal liability for injury to, or for the illness or death of other persons whether or not they are carried on board the ship.

The P&I clubs also cover costs and expenses directly and reasonably incurred by the shipowner as a result of the ship having stowaways on board, so long as the shipowner is under a legal liability to pay such costs and expenses, or they have been incurred in agreement with the club.<sup>35</sup>

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32 For more detailed commentary see Chapters 15 to 17 of the *Gard Handbook on P&I Insurance and the Gard Guidance to the Statutes and Rules* (Guidance to Rule 27 (Liabilities in respect of crew) and Rule 28 (Liabilities in respect of Passengers)).

33 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 55a (Terms of contract)).

34 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 29 (Liability for other persons carried on board) and Rule 55a (Terms of contract)).

35 For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 29 (Liability for other persons on board)).

## 11.6 Claims Management

Incidents that result in death, illness or personal injury are normally stressful, time-consuming and complicated and incorrect actions or decisions can result not only in substantial financial loss but also in unwelcome and harmful publicity. This is particularly the case if a casualty occurs which causes multiple loss of lives or injuries. Therefore, it is vital that shipowners are able to implement a well thought-out and well prepared emergency response plan with minimal delay and that ship-board personnel follow the recommendations made in Chapter 3.11 of the *Gard Guidance to Masters*. Close liaison and team work between ship and shore personnel is vital. Furthermore, shipowners should ensure that all interested parties whether insurers, authorities, charterers etc., are kept closely advised of developments. In particular, strenuous efforts should be made to ensure that next of kin are kept advised and treated with the utmost sympathy, respect and understanding.

Such incidents may occur in a country where the shipowner does not have his principal place of business or does not have the resources that may be necessary to handle the many challenging issues. Therefore, it will be important to establish a link with local personnel that have the necessary experience and expertise to manage any local and international issues that may be relevant. In this regard, P&I clubs have substantial incident and claims handling experience in virtually all maritime jurisdictions around the world and have access to a very wide network of correspondents and other service providers who may be called into action at short notice to assist the immediate emergency response requirements and the subsequent follow-up needs of the shipowner, whilst, at the same time, ensuring that the shipowner's interests are protected.



## 11.7 Case Studies

### Case Study 1

A Filipino seafarer died on board as a result of heart disease. The body was disembarked when the vessel arrived at the next port of call and an autopsy was carried out to determine the cause of death, following which, the body was prepared for repatriation. The seafarer left behind a widow and two minor children and death compensation was paid to the beneficiaries in accordance with the terms of the applicable Collective Bargaining Agreement for the ship. The payment of repatriation costs, funeral costs, replacement costs and death benefits to the family was covered by the ship's P&I club.

### Case Study 2

During a shore excursion to a plantation in Jamaica a vehicle carrying 23 passengers turned over at speed in a bend on a path. A number of passengers were injured and initially treated at a hospital in Jamaica before being airlifted to Miami. The vehicle was owned and operated by the plantation owners who had liability insurance cover for USD 1 million. However, their liability insurers declined to cover the claim alleging numerous operational breaches. The Athens Convention did not apply but the ship incurred liability under the law governing the passenger ticket since it had either been negligent in selecting a sub-standard shore excursion provider or was vicariously liable for the negligence of that provider. Consequently, the ship's P&I club concluded an agreement with the plantation owners to pay compensation estimated to be USD 2.1 million to the injured passengers and to settle significant additional medical expenses. The club was then subrogated to whatever rights the shipowner member had to seek an indemnity from the plantation owner (and its liability insurance if available) under the contract between them.

### Case Study 3

During discharge operations in Miami, an American stevedore, known locally as a 'longshoreman,' is injured while climbing up a ladder located between the tween-deck and the main deck of a bulker. The ladder's rungs collapse under his weight and he falls down onto the tween deck injuring his ankle, leg and shoulder. He is taken to the local hospital, treated but return home five days later and is placed on 'injury leave' by his employer, the stevedoring company. The longshoreman receives workers' compensation payments during the entire time that he is recovering at home. The workers' compensation insurer also pays for his medical costs during this time.

Under US Federal law (The Longshoreman and Harbor Workers Compensation Act or LHWCA) the insurer obtains a statutory lien on all amounts paid to the longshoreman, which it will attempt to recover from the shipowner in due course. Meanwhile, the longshoreman files a personal injury law suit against the vessel

in US Federal Court. The shipowner immediately files a cross-claim against the stevedore company (employer), claiming that the broken ladder was the property of the company and not the ship. A 'liability triangle' is the result; wherein three separate and distinct parties have a stake in the outcome of the law suit. If the longshoreman can prove that the defective ladder was the property of the vessel, then the shipowner will be liable in negligence to the longshoreman, and will also be liable to the workers' compensation insurer for their lien on the amounts already paid to the longshoreman, plus his medical costs. If, however, the shipowner can convince the court that the ladder belonged to the stevedoring company, then it can successfully deny tort liability to the longshoreman and avoid having to pay the workers' compensation lien to the US insurer.

#### **Case Study 4**

A container vessel leaves Cape Town bound for Recife, Brazil. Three days into the voyage two stowaways are found hiding in a container. They are removed from the container and taken to a secure room in the crew area of the vessel. Because the vessel is three days sailing from South Africa and on a tight schedule, the decision is made to continue the voyage to Brazil. Prior to berthing at Recife the local authorities are advised of the presence of two stowaways on board. During the crossing and after several days of interrogation at sea, the stowaways finally concede that they are Tanzanian. The correspondent in Tanzania is notified and begins the process of obtaining the necessary travel documents/visas in order to effect repatriation. Local authorities in Brazil, meanwhile, demand that the two stowaways be removed from the vessel and taken to a local hotel under 24 hour security watch, pending any request for political asylum, determination of their status in Brazil or deportation. The vessel is ordered to pay all hotel and security costs. After two weeks at the hotel the stowaways are ordered deported, again at the expense of the vessel. Moreover, two escort security guards per stowaway are demanded by local authorities. Plane tickets for six people are arranged and the flights are directed via Europe. The four security guards are then flown home. Total cost to the shipowner is USD 120,000. All above named costs and expenses are covered by the club.

## Chapter 12

# Pollution Claims<sup>1</sup>

### 12.1 Introduction

Pollution is a major cause for concern and the regime of international and national laws that regulate it reflects that concern. Historically, anti-pollution legislation has been directed in the main towards pollution caused by the escape of oil carried as cargo. However, in more recent years, attention has also been given to other forms of pollution. Therefore, there are international conventions and local laws which regulate pollution from ship's bunkers and other hazardous and noxious substances (such as chemicals, gases and other volatile products), garbage and other waste, and even ships which are committed for recycling.

Pollution can give rise to both substantial civil liabilities and severe criminal sanctions and penalties and the legislative regime that governs pollution tends to fall into two categories:

- a Pollution prevention; and
- b Liability for pollution.

### 12.2 Pollution Prevention<sup>2</sup>

There is a body of international conventions that are designed to monitor ship structures and quality control systems, the aim of much of which is to minimise the risk of pollution. There are also similar pollution avoidance measures that regulate ship operation and there is a further body of international conventions that are

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1 For more detailed commentary please refer to the *Gard Handbook on Protection of the Environment*, 3rd edition and to *Shipping and the Environment* by De la Rue and Anderson, Informa, 2nd edition 2009.

2 More detailed commentary can be found in Chapters 22.3.1 and 22.3.2 (Maritime Regulation and Compliance) and in Part II, Chapters 5 and 6 of the *Gard Handbook on Prevention of the Environment*, 3rd edition.

designed to monitor the training of on board personnel, the adequacy of on board and land based pollution emergency plans and management systems linking on board and shore-based personnel.<sup>3</sup>

Compliance with such regulations is enforced by a worldwide system of port state control whereby ships are required to carry compliance certificates that are regularly checked by port authorities at the ports visited by ships.<sup>4</sup> Such authorities are also given the right to inspect the ship, to detain the ship if needs be and also require repairs to be carried out before the ship is allowed to leave. A finding of non-compliance can give rise to criminal sanctions such as the imposition of substantial fines and possibly restrictions on the ship's ability to trade freely. Therefore, non-compliance may also have commercial repercussions including the possible avoidance of the ship's insurance cover.

Finally, a coastal state is entitled to take unilateral action to avoid or minimise a pollution threat. Such action is likely to arise if that state believes that the ship's personnel are either not taking action to avoid or minimise the risk or are not doing so sufficiently promptly.<sup>5</sup>

Not all countries are parties to the various international conventions. Nevertheless, most coastal countries which are not parties to such international conventions tend to have local statutes which impose similar requirements and/or sanctions.

### **12.3 Pollution Response**

Broadly speaking, there are two different types of pollution response regimes. The first is where the affected state takes responsibility for organising and initially paying for the response, although the state will almost certainly seek to recover its expenditure from the responsible shipowner subsequently. The second is where the state requires the shipowner to organise and pay for the response. This is usually done through legislation stipulating that, as a condition of entry to a particular state's waters, the shipowner must have 'pre-contracted' with a company deemed suitable by the relevant state by virtue of having the equipment and competence necessary to respond to an oil spill.

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3 For more detailed commentary see Chapter 22 (Maritime Regulation and Compliance).

4 More detailed commentary can be found in Chapter 22.3.3 (Maritime Regulation and Compliance) and in Part II, Chapter 5.4 of the *Gard Handbook on Prevention of the Environment*, 3rd edition.

5 See Chapter 22.3.2.2.3 (Maritime Regulation and Compliance) and Chapter 16.2.2 (Wreck Removal Claims).

### 12.3.1 State organised Response

Many states take the view that, in the event of a pollution incident, they are best placed to take tactical and strategic decisions as to how and with what personnel and equipment they should respond. To do so, many states will either employ directly, or have available under a standing contract, personnel and equipment, sited at strategic locations. Such an arrangement will, *inter alia*, enable those states to decide quickly whether dispersant should be used as part of the 'at sea' response, or whether any particular sites/areas that are or may become affected by the spill should be protected as a matter of priority. Such sites might be power stations or mariculture sites, or areas deemed to have outstanding natural beauty, or to be of historical or cultural importance. The reasoning behind such an approach is that it is only that state that will be aware of these factors and only that state that can make the sometimes difficult decision as to which resource(s) should be given priority.

### 12.3.2 Shipowner organised Response

A number of states, of which the US is probably the best example, have adopted the view that the responsibility for spill response should rest with the 'responsible party' – almost always the shipowner. Recognising that it is extremely difficult for an owner to organise an effective spill response 'from scratch', these states require the owners of the ships calling at ports or places in that state to have entered into contractual arrangements with recognised and approved spill responders. These responders are called OSROs (Oil Spill Response Organisations) in the US. In China, where similar legislation is in place, they are called SPROs (Spill Response Organisations). In such states, it is the shipowner who is responsible for notifying the relevant authorities of the incident and for instructing the spill response organisation with which he has contracted to attend immediately. The contract between the shipowner and the response organisation will normally contain details of the number of personnel and type of equipment that will be called out in any particular incident and will depend largely on the amount and type of pollutant spilled. The contract will also normally contain a time limit in which the response must be put into effect.

It is normal for such response organisations to be vetted by the relevant state authority prior to their being approved and prior to their being allowed to enter into contracts with shipowners. Usually, they are graded (level 1, level 2 etc.) depending on the number of personnel and amount and type of equipment available.

However, this scheme may prove to have a deficiency if the pollution originates from a vessel that is not due to call at a port or place in the affected country and therefore, does not have such a contractual arrangement in place.

### 12.3.3 Comment

There is no ideal system for spill response. The only really effective method is to keep the pollutant in the ship. Whichever scheme is adopted, there is a fundamental presumption that the state has the final decision over the amount and type of resources deployed and the location in which this deployment takes place, but that the shipowner (in the case of states party to the CLC) and the 'responsible party' (in the US) will pay the cost of the response, subject to the applicable legislation. It is therefore extremely important that, in the event of a spill, there should be early and close co-operation between the owner and his insurers on the one hand and the relevant authorities on the other. The number of authorities with whom an owner has to deal will vary from state to state and confusion can sometimes arise where different state parties wish to take charge of and control the spill response. Identifying the key organisations and personnel is therefore important.

### 12.3.4 Operational Issues

Generally speaking, spill response is either 'at sea' or 'on shore' but it is often a combination of both. 'At sea' response is usually adopted when the pollutant is both 'at sea' and proves to be suitable for effective response in that environment. One common method of response is to use aircraft to spray dispersant to try to break up the oil. However, the use of dispersant has proved to be controversial in some states, notably the US, both because of its effectiveness, or perceived lack thereof, and its alleged impact on the environment. In other states, it remains the main 'at sea' response option. Another possible 'at sea' response is to use skimmers to try to collect the oil, but the type of oil and prevailing weather may sometimes mean that this response is ineffective.

'On shore' response takes place if oil is expected to, or does, come ashore. Booms are often used to try to protect sensitive resources, or to 'corral' the oil into a homogenous mass which can then be collected by skimmers. Unfortunately, many oils have a natural tendency to disperse, so this method is sometimes ineffective. If oil comes ashore, manual cleaning may well be the only option. This may involve beach cleaning, sometimes using bulldozers and/or using high-pressure hoses to wash down rocks or man-made structures such as piers.

In the event of a serious pollution incident, shipowners and their insurers will normally employ experts such as ITOPF (International Tanker Owners' Pollution Federation) to travel to the affected area and provide independent technical advice on the spill response and on any claims for alleged damage to natural resources. Much useful information about spill response can be found at the following website address: <http://www.itopf.com/spill-response/>

Responding to spills, especially serious spills, will be a difficult and challenging task for shipowners. In the event of a threatened or actual pollution incident, no matter how small, owners should immediately notify their P&I club.

## 12.4 Liability for Pollution

Liability may arise under

- The civil law; or under
- The criminal law.

### 12.4.1 Civil Liability

It must firstly be emphasised that whilst there is a substantial framework of international conventions which has been developed to regulate civil liability for pollution, such framework is binding only in those countries which have adopted such conventions. Therefore, civil liability for pollution in countries which have not adopted such conventions may be based on very different principles.<sup>6</sup> For example, the United States of America has not adopted this framework and liability for pollution in the United States is often based on a combination of federal and state law.<sup>7</sup> Therefore, it is important to establish at an early stage whether liability is likely to be subject to the international conventions or local law since this may well determine the manner in which steps should be taken to minimise further pollution or pollution liability.

When considering civil liability for pollution a distinction needs to be drawn firstly between:

- oil pollution; and
- pollution by other products.

However, even in the case of oil pollution, a distinction needs to be drawn between pollution caused by:

- the spillage of cargoes of 'persistent oil'<sup>8</sup> and of bunkers from laden tankers; and
- the spillage of bunkers from non-laden tankers or from non-tankers.

The distinction is important since, as can be seen from the following sections, liability for such pollution is governed by different international conventions.

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6 A detailed commentary on the laws of a very large number of individual countries can be found in Chapter 8.3 of the *Gard Handbook on Protection of the Environment*, 3rd edition.

7 A detailed commentary on the federal and states laws of the USA can be found in Chapter 9 of the *Gard Handbook on Protection of the Environment*, 3rd edition.

8 Article 2.2 of CLC 1992 defines 'oil' as "any persistent hydrocarbon mineral oil such as crude oil, fuel oil, heavy diesel oil and lubricating oil, whether carried on board a ship as cargo or in the bunkers of such a ship." Article 2.1 defines a "ship" for these purposes as a tanker.

### 12.4.1.1 Civil Liability for Oil Pollution Claims under International Conventions

#### 12.4.1.1.1 Pollution caused by Laden Tankers<sup>9</sup>

As a result of the TORREY CANYON incident in 1967 a sophisticated system of inter-linking international conventions and private industry agreements has been progressively developed over the subsequent years which is intended to provide quick and sufficient compensation for pollution claims resulting from spillages of 'persistent oil' from laden tankers. 'Persistent oil' includes crude, fuel, heavy, diesel and lubricating oil but not gasoline, kerosene and distillates.

The system is based on the following inter-linking conventions and agreements:

- The Civil Liability Convention 1969 (CLC 69);
- The Fund Convention 1971 (which is no longer applicable to incidents occurring after 24 May 2002);
- The Civil Liability Convention 1992 (CLC 92);
- The Fund Convention 1992;
- The Fund Protocol 2003 (The Supplementary Fund) (available only to countries that have adopted CLC 92);
- The Tanker Oil Pollution Indemnification Agreement (TOPIA);
- The Small Tanker Oil Pollution Indemnification Agreement (STOPIA).

This structure was originally established by CLC 69 and the later CLC 92, Fund Conventions and Agreements subsequently increased the amount of compensation that is payable. However, there has been no uniform acceptance of all of these conventions and agreements by all countries and shipowners. Some countries are parties to all of the conventions whereas others are merely parties to one or more conventions. Similarly, TOPIA and STOPIA are voluntary not obligatory agreements which are not part of the international conventions, albeit that it is a condition of entry to the International Group P&I clubs that shipowners must accept these agreements.<sup>10</sup>

Therefore, there are three possible tiers of compensation, each tier being subject to a specific limit. The first tier is established by the CLC Conventions, the second tier by the 1992 Fund, and the third tier by the Supplementary Fund. Each tier of compensation is funded by different interests: The first tier of compensation under the CLC Conventions is funded by the shipowners and their P&I insurers, whilst compensation under the FUND 1992 Convention and Supplementary Fund (when applicable) is funded by the international oil industry through a surcharge which

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<sup>9</sup> For more detailed commentary see Part IV Chapter 15 of the *Gard Handbook on Protection of the Environment*, 3rd edition and *Shipping and the Environment* by De la Rue and Anderson, Informa, 2nd edition, 2009.

<sup>10</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 38 (Pollution)) and Chapter 12.4.1.1.1.6 below.



receivers of oil (usually the major oil companies) pay on shipments of oil carried by sea. Finally, the voluntary STOPIA and TOPIA agreements, which were created to correct perceived imbalances in the amounts paid for pollution damage by shipowners/insurers, on the one hand, and the international oil industry on the other, are designed to indemnify the 1992 Fund and Supplementary Fund respectively for a proportion of the compensation that has been paid under such conventions to third party claimants, and such indemnity is funded by shipowners and their P&I insurers. These compensation regimes are all closely related and are designed to provide claimants and shipowners with an almost seamless transition between the various instruments.

The CLC 92/Fund system (The CLC regime) is based on the inter-linking of the following factors:

- The channeling of all claims under the convention to the registered owner of the ship in accordance with the terms of the convention;
- The definition of oil pollution claims;
- The imposition of virtually strict liability with few defences;
- The limitation of the shipowners' liability that is virtually unbreakable;
- The imposition of compulsory insurance for pollution liability;
- The right of a claimant under the convention to bring a claim directly against the shipowners' insurer or "*other person providing financial security ...*"

The combination of these factors has enabled the system to work very well in the main and it is constantly being amended and upgraded in response to changing circumstances and requirements.

However, CLC 69 (which is still in force in some countries) suffers in comparison to CLC 92 from the following deficiencies:

- CLC 69 does not prohibit claims against parties other than the registered owner. Therefore, claims can be brought against charterers or other parties under national or local statutes or under traditional common law or civil law principles such as negligence, nuisance etc.
- The right to limit liability can be lost if there is merely 'fault or privity' on the part of the shipowner.

#### 12.4.1.1.1 Channelling

The channelling provisions debar claimants from bringing claims for "*oil pollution damage*" within the meaning of the convention against parties other than the registered owner and thereby minimise the complications which can arise were claims to be brought against multiple defendants. Therefore, claims for "*oil pollution damage*" cannot be brought against other possible targets such as the servants and agents of the shipowner or the crew, pilot, charterers, managers, operators and

salvors of the vessel unless it is proved that the damage resulted from their personal act or omission committed with intent to cause such damage, or recklessly and with knowledge that such damage would probably result.

Such channelling provisions also assist in the provision of compulsory liability insurance<sup>11</sup> since all available liability insurance resources can be concentrated and thereby provide higher levels of cover than those which could otherwise be provided if such resources were to be dissipated between various defendants.

However, the 'channeling' system can be avoided even in countries that have adopted the CLC regime. For example, in the case of the ERIKA, the European Court of Justice (ECJ) considered whether various parties were liable for the costs incurred in the cleaning-up and disposal of substantial quantities of oil which had been lost from the ERIKA and which had been deposited on the shoreline mixed with water and sediment. The court held that such a mixture constituted 'waste' for the purposes of a EU Directive which imposed strict liability on waste producers and holders for the cost of waste disposal and management if their conduct had contributed to the risk of pollution. The court seems to have recognised that although the 'channeling' provisions of the CLC 1992 enabled Total as charterer to avoid liability for "pollution damage" as defined in the CLC Conventions, a charterer could still be held liable as a 'producer' or 'holder'<sup>12</sup> of the 'waste' under the EU Directive. Consequently, Total was obliged to collect, recover and dispose of the oily mixture.<sup>13</sup>

#### 12.4.1.1.1.2 Claims for 'Oil Pollution Damage'

CLC 1969 applies only to 'oil pollution damage' that has been caused in the territorial waters of states that have accepted that convention, but pollution damage is extended under CLC 1992 to the exclusive economic zone (EEZ) of a contracting state, which normally extends to 200 nautical miles from the baselines from which the territorial sea is measured.

Claims will be subject to the CLC regime only if they are for 'oil pollution damage' as defined in the CLC Conventions. If they are not claims which fall within that definition then the CLC regime does not apply and liability will be determined in accordance with the provisions of other conventions or the provisions of local law in the country where the pollution occurred.

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11 See Chapter 12.4.1.1.1.5 below.

12 However, it should be appreciated that Total was also the cargo owner in this case.

13 *Commune de Mesquer v Total France SA*, (Case C 188/07) (See (2008) C.M.L.R 16).

In the majority of cases, claims will be allowed for:

- Costs and expenses incurred in order to prevent pollution damage following a spill, or to clean up and restore polluted areas and property;
- Loss or damage caused by physical contamination of property, e.g. the soiling of recreational boats or fishing nets, or the clogging of water intakes to a production facility, or economic losses incurred as a result of such events regardless of whether or not the claimants have been directly affected by contamination, e.g. fishery and tourism losses, as well as damage or losses caused by clean-up and restoration activities;
- Costs and expenses incurred in restoring damaged natural resources that have no direct economic value, e.g. beaches, mangroves, marshlands, coral reefs and their wildlife flora and fauna habitats. Even if such restoration cannot be carried out, claims for losses which can be shown to have arisen as a direct result of the incident may be allowed.

However, although CLC 1992 has expanded the scope of qualifying claims, there may still be 'grey areas' where it is uncertain whether or not a particular claim will be covered. The CLC and Fund Conventions do not themselves specify whether claims will or will not be qualifying claims but the IOPC Fund has published a Claims Manual which gives guidance as to the types of claims which are likely to be accepted or rejected and these guidelines will normally be the determining factor. The IOPC Fund also publishes a periodic report itemising Incidents Involving IOPC Funds.<sup>14</sup>

#### 12.4.1.1.1.3 *Strict Liability*

Under the CLC regime claimants do not need to produce evidence to show how the incident happened, or to prove fault on the shipowner's part. The mere occurrence of "*oil pollution damage caused by oil which has escaped or been discharged from the ship as a result of an incident*" is sufficient to establish liability unless the shipowner is able to prove that the damage was:

- The result of an act of war, hostilities, civil war or insurrection; or
- The result of a natural phenomenon of an exceptional, inevitable or irresistible character; or
- Was wholly caused by an act or omission done with intent to cause damage by a third party; or
- Was wholly caused by the negligence or other wrongful act of any government or other authority responsible for the maintenance of lights or other navigational aids in the exercise of that function.

<sup>14</sup> Copies of these publications can be accessed through the IOPC website: [www.iopcfund.org/publications/htm](http://www.iopcfund.org/publications/htm).

#### 12.4.1.1.1.4 Limitation of Liability

The CLC regime provides that the liability of the shipowner is to be capped at the maximum compensation applicable under the various conventions. This can be seen as a measure to counter-balance the virtual strict liability which an owner is likely to face. However, the right of the shipowner to limit his liability in this way may be lost if he is guilty of certain conduct. The nature of the conduct that is necessary to debar the right to limit is different under the two conventions. Under CLC 1969 the right to limit is lost if the incident has been caused by fault and privity on the part of the shipowning company. Therefore, in certain cases, the right to limit could be lost if there were to be personal negligence on the part of the alter ego (i.e. the higher management) of the shipowning company itself (but not, for example, on the part of the master, unless the master was also the owner.) However, under CLC 1992, the right of a shipowner to limit liability will be lost only if it is proved *“that the pollution damage resulted from his personal act or omission, committed with intent to cause such damage, or recklessly and with knowledge that such damage would probably result.”* This is a more difficult test for a claimant to overcome and should in normal circumstances be virtually unbreakable.

In both cases, the relevant conduct must be that of the alter ego of the shipowning company.<sup>15</sup> Therefore, in the majority of cases, it is the conduct of the higher management of the shipowning company which will be relevant. However, it has seldom been necessary in practice for claimants to challenge the shipowner's right of limitation under CLC since even if claims exceed CLC limits, the additional compensation available under the Fund Conventions has normally been sufficient to satisfy such claims in full.

#### 12.4.1.1.1.5 Compulsory Pollution Liability Insurance

All tankers capable of carrying more than 2,000 tons of oil are obliged under the CLC regime to carry evidence that they are insured against pollution liability up to the relevant CLC limit. In the majority of cases, ships are insured against such risks by their P&I club but fixed premium liability insurers also provide such cover. Proof of such pollution liability cover must be evidenced by the carriage on board of a certificate which is normally issued by the tanker's flag state administration, which is itself issued once the flag state is satisfied such insurance cover is in place. The 'blue cards' issued by clubs in the International Group are accepted as satisfactory evidence.

Claimants have the right to bring a direct action against the insurers named in the CLC certificate. Such insurers are entitled to rely on any defences that are available to the shipowners under the CLC Conventions but are not entitled to rely on any

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<sup>15</sup> See also Chapter 28.1.2 of the *Gard Handbook on P&I Insurance*, 5th edition and pages 31-39 of *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, Informa, 4th edition, 2005.

other defences that they may have vis-à-vis the assured under the policy of insurance (except where damage has resulted from the wilful misconduct of the assured.) Nevertheless, the liability that the insurers have under the certificate is capped at the ship's liability limit even if the shipowner's right to limit has been lost.

Although the CLC Conventions require compulsory pollution liability cover only up to the relevant convention limit, most shipowners will normally insure their ships for higher limits in the event that the ship incurs liability in non-convention countries such as the USA where the risk of pollution liability is greater. However, since liability could in some circumstances reach astronomic levels, the cover provided by the members of the International Group of P&I Clubs is limited to USD 1 billion per incident.<sup>16</sup>

#### 12.4.1.1.1.6 STOPIA and TOPIA

STOPIA and TOPIA are voluntary agreements that have been concluded between the shipowning and oil producing and importing industries. The background to these agreements is that the oil industry believed that it was exposed to significantly greater liability than the shipowning industry in circumstances where:

- there was a spill from a small tanker, which caused significant damage and, therefore, large claims, but where, because of the small tonnage of the vessel involved, the shipowners could limit their liability to a small proportion of the amounts claimed, leaving the balance to be borne by the oil industry or;
- there was a huge spill from a tanker leading to claims significantly in excess of that vessel's limit of liability under CLC, resulting in the fact that the oil industry, through the Fund, was obliged to bear a much larger share of the compensation than the shipowner.

To address this perceived imbalance, a voluntary agreement was concluded between the owners of small tankers that were entered with International Group clubs to introduce the Small Tanker Oil Pollution Indemnification Agreement (STOPIA 2006). Under the terms of STOPIA 2006 the shipowner's liability in respect of incidents involving tankers up to 29,548 GT is increased to SDR 20 million (at the time of writing about USD 33 million). STOPIA 2006 applies to incidents involving participating tankers in all 1992 Fund Member States.

A second agreement known as the Tanker Oil Pollution Indemnification Agreement (TOPIA 2006) provides for the indemnification of the Supplementary Fund for 50 per cent of the amounts paid in compensation by that Fund in respect of incidents involving tankers of any size that are entered in one of the International Group Clubs.

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<sup>16</sup> See Chapter 12.7.1 below.

#### 12.4.1.1.1.7 *The Management and Resolution of Pollution Damage Claims*

If a claim falls within the relevant CLC limits it will normally be negotiated between the claimants, the shipowners and their P&I club. Priority in the handling of claims will usually be given to those claimants who have suffered a significant and provable loss and advance payments may be made to alleviate hardship in appropriate cases. However, difficulties can arise when numerous and sometimes somewhat speculative claims are made. Furthermore, if it looks likely that the total claim will exceed the shipowner's limit of liability, advance payments are normally made on a *pro rata* basis. If the claim does exceed CLC limits then, pursuant to a Memorandum of Understanding dated 2006 between the P&I clubs and the IOPC Fund, the relevant club is obliged to notify the IOPC Fund. Thereafter, the investigation, evaluation and quantification of the damage is generally conducted jointly by the IOPC Fund and P&I club and the allocation of settlement funds is agreed between the Fund and the relevant P&I club.<sup>17</sup>

#### 12.4.1.1.2 *Pollution from Unladen Tankers or from Non-tankers*<sup>18</sup>

The CLC regime applies only to pollution from laden tankers carrying persistent oil as cargo, or tankers in ballast that have remnants of persistent oil as cargo on board. Therefore, claims resulting from spillages of bunker oil from unladen tankers or from non-tankers fall outside the CLC regime. However, this gap in the international convention regime has been plugged by the International Convention on Civil Liability for Bunker Oil Pollution Damage 2001 (The Bunker Convention). The Bunker Convention applies to spillages of 'bunker oil' which is defined as "*any hydrocarbon mineral oil, including lubricating oil, used or intended to be used for the operation or propulsion of the ship, and any residues of such oil.*" The Bunker Convention achieves some of the balance inherent in the CLC regime, but in certain important areas, that balance is lacking.

The Bunker Convention mirrors the CLC regime in that it imposes:

- Strict liability subject to the same limited defences;
- Limitation of that liability; and
- Compulsory liability insurance which is to be certified (except in the case of ships of less than 1,000 GT) by the carriage on board of confirmatory certificates, and which includes the same right of direct action against the liability insurers.

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<sup>17</sup> A copy of the IOPC Fund Claims Manual can be found on the IOPC Fund website: [www.iopcfund.org](http://www.iopcfund.org).

<sup>18</sup> For more detailed commentary see section Chapter 15.5 of the *Gard Handbook on Protection of the Environment* 3rd edition and *Shipping and the Environment* by De la Rue and Anderson, Informa, 2nd edition, 2009.

However, the Bunker Convention differs from the CLC regime in the following ways:

- Liability is imposed not just on the 'shipowner', but also on the "bareboat charterer, manager and operator of the ship" all of whom are jointly and severally liable under the convention.
- There are no provisions channelling liability whether under the Bunker Convention or otherwise to the registered owners of the ship. Consequently, claims may still be brought in appropriate circumstances against charterers other than bareboat charterers or others depending on the law of the country where the pollution took place.
- There is no 'special' or free-standing limit of liability for bunker pollution claims. In the event of such an incident, such claims must share whatever fund that is available under the 1976 Limitation Convention, or the 1996 Protocol thereto, or the 1957 Limitation Convention (that is still in force in some countries) *pari passu* with all other claims which qualify for limitation under those general limitation regimes (e.g. claims for collision damage, cargo damage etc.). An examination must, therefore, be made to see whether any of these conventions are in force in the state in question and if so, whether the claim(s) made are limitable in accordance therewith.
- It is a single-tier regime which is not augmented by 'top-up' conventions such as the FUND Conventions.

Therefore, the Bunker Convention achieves some of the balance inherent in the CLC regime, but in certain important areas, that balance is lacking.

#### 12.4.1.2 Civil Liability for Pollution Caused by Products other than Oil Products<sup>19</sup>

Compensation for loss or damage caused by the carriage of hazardous and noxious substances other than oil is not regulated by either the CLC regime or the Bunker Convention. The International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious substances by Sea 1996 as revised by the Protocol of 2010 (The 2010 HNS Convention) is intended to plug that gap and is modelled on the CLC regime. However, at the time of writing, the 2010 HNS Convention is not yet in force.

The convention applies to various specific types of claims that arise as a result of the carriage of hazardous and noxious substances (HNS). The substances that qualify as HNS are substances that have been previously identified in international conventions and codes such as the IMDG Code and include bulk cargoes (including solids, liquids and gases) and packaged goods.

<sup>19</sup> For more detailed commentary see Chapter 15.4 of the *Gard Handbook on Protection of the Environment*, 3rd edition.

The convention does not apply to claims for 'oil pollution damage' as defined under the CLC regime and Bunker Convention but applies to claims for 'damage' defined as:

- Loss of life or personal injury occurring on board or outside the ship carrying HNS;
- Loss of or damage to property occurring outside the ship carrying HNS;
- Economic losses caused by the contamination of the environment (including the loss of fishing or tourism income);
- The costs of preventative measures and further loss or damage caused by preventative measures;
- The costs of reasonable measures to reinstate the environment.

The convention applies to:

- Any form of 'damage' that occurs in the territory or territorial sea of a state party to the convention;
- Pollution damage that occurs in the exclusive economic zone, or equivalent area, of a state party;
- 'Damage' (other than pollution damage) occurring outside the territory or territorial sea of any state party when caused by the carriage of HNS on ships registered in, or entitled to fly, the flag of a state party.

The HNS Convention mirrors the CLC regime in that the compensation system is based on the inter-linking of the following factors:

- The channeling of all claims to the registered owner of the ship (except in the limited circumstances described below);
- The definition of HNS 'damage' claims;
- The imposition of virtually strict liability with few defences;
- The limitation of the shipowners' liability that is virtually unbreakable;
- The imposition of compulsory insurance for pollution liability;
- 'Top-up' compensation in the form of a HNS Fund funded by cargo interests;
- A dedicated claims management body equivalent to the IOPC Fund.

If the HNS Convention does not apply for any reason regard must be had to the local law of the country where the incident occurred.



### 12.4.1.3 Civil Liability for Pollution Claims under the Law of the USA<sup>20</sup>

The USA is not a party to the CLC regime or the Bunker Convention or the HNS Convention. However, it has its own statutes which regulate liability for pollution damage claims.

US regulations protecting the marine environment have always been very complex. In addition to the very comprehensive federal legal system in this area, there are also individual state and territorial laws and regulations. The principal federal acts governing marine pollution are: The Comprehensive Environmental Response, Compensation and Liability Act, 1980 (CERCLA), the Oil Pollution Act, 1990 (OPA 90) and the Federal Water Pollution Control Act, 1948, as amended (FWPCA), but there are also other federal and state statutes which individually and collectively outlaw the discharge of any type of pollutant into waters under US jurisdiction.<sup>21</sup> For example, the Vessel General Permit program that is administered by the US Environmental Protection Agency under the National Pollutant Discharge Elimination System, regulates the discharge of many types of potential effluents from ships. Therefore, regard must be had to all of these laws and regulations in the event of a spillage.

It is not possible to comment on all of the statutes and laws which may potentially be relevant but comment is made below on the most important statutes.

#### 12.4.1.3.1 *The Oil Pollution Act 1990 (OPA 90)*

OPA 90 is designed to be a comprehensive legal regime that addresses pollution prevention, response/clean-up, damages, compensation, as well as enforcement through civil and criminal penalties. This approach differs significantly from the CLC regimes that focus specifically civil on liability and compensation.

##### 12.4.1.3.1.1 *Scope of Applicability*

The statute applies to any vessel or facility that discharges oil, or poses the substantial threat of a discharge of oil, into or upon the navigable waters of the United States, adjoining shorelines, or the Exclusive Economic Zone extending up to 200 miles from the baseline. Oil is defined broadly to include petroleum, fuel oil, sludge, oil refuse and oily waste, but does not include hazardous substances defined under CERCLA.

<sup>20</sup> For more detailed commentary see Chapter 9 of the *Gard Handbook on Protection of the Environment* and the general provisions of *Shipping and the Environment* by De la Rue and Anderson.

<sup>21</sup> For more detailed commentary see Chapter 22.4.1 (Maritime Regulation and Compliance).

#### 12.4.1.3.1.2 *Responsible Parties*

OPA 90 places liability on 'responsible parties' which includes any parties which own, operate or charter by demise any vessel regardless of type (i.e. tankers as well as non-tankers) and all of these parties are jointly and severally liable for a wide range of recoverable claims. Whilst cargo interests do not appear to fall within the definition of 'responsible parties,' a number of states have, nevertheless, held cargo owners liable for oil pollution damage in addition to or in substitution for shipowners.

#### 12.4.1.3.1.3 *Basis of Liability*

To all intents and purposes there is strict liability unless the 'responsible party' can prove that the spillage and/or consequential damage was caused solely by one or more of the following:

- An act of God;
- An act of war;
- An act or omission of a third party, excluding employees, agents, or those having a contractual relationship with the responsible party. (However, this is not a complete defence since the responsible party is still obliged to clean up the spill and make payments to claimants, but then obtains subrogated rights against such third parties.)

However, these defences are not available if the responsible party failed to report the incident, or failed to provide all reasonable assistance and co-operation requested by responsible officials, or, without sufficient cause, failed to comply with the orders of a government official, given under the FWPCA or the Intervention on the High Seas Act, 1974.

#### 12.4.1.3.1.4 *Recoverable Claims*

The responsible party is liable for:

- All removal costs including the costs of preventing or minimising such an incident;
- All damages to natural resources including the cost of restoring damaged resources, the loss of value of those resources, pending restoration, plus the reasonable cost of damage assessment;
- All damages to real or personal property, including economic loss;
- All loss of subsistence use of natural resources for food, shelter and the necessities of life. Such loss is recoverable by any user of such resources, regardless of ownership;
- Loss of revenue, including taxes;
- Loss of profit and earning capacity. The claimant need not be the owner of the damaged property or resources to recover;
- The additional costs of providing public services during or after the removal activities.

Assessing the damage claimed and attempting to attribute a monetary value to such damage is often a source of much debate. This is particularly true in the case of the assessment and quantification of damages to natural resources, where the US has pioneered the use of computer assisted models to assess the impact that spills have on natural resources, on a broad scale. The claims items that are consequently recoverable from the 'responsible party' include such predictable items as the loss of flora and fauna and habitat restoration, but also such items as lost recreational opportunities for the local populace and transitory tourists, which are calculated by using economic models that are supported by opinion polls and sociological concepts. In major recreational areas this can result in large monetary awards that are collected by government agencies.

The impact on local wildlife can be calculated by not only recording the degree of mortality that is actually observed, but by also adding a 'multiplier factor,' on the basis that wild animals that have been mortally sickened by contact with spilled oil will travel away from the scene and die in hidden or remote locations. This can result in claims that are assessed with reference to many times the number of dead animals that have actually been seen, and can result in much higher monetary assessments of damages to fauna as a result of an oil spill.

#### *12.4.1.3.1.5 Limitation of Liability*

The owners and operators of vessels are entitled to limit their liability under OPA 90, but the right to limit liability can easily be lost if the incident was proximately caused by:

- Gross negligence or wilful misconduct on the part of the responsible party or its agent or employee, or on the part of a person acting pursuant to a contractual relationship with the responsible party;
- The violation of an applicable federal safety, construction, or operating regulation (such as one of the COLREGS);
- The failure or refusal of the responsible party to report the incident or to provide reasonable co-operation and assistance to responsible officials, or to comply with an order issued under the FWPCA or Intervention on the High Seas Act.

The current limits of liability for vessels under OPA 90 are as follows (please note the differential between vessels of double hull and single hull tank vessels):

**a Tank Ships and Tank Barges**

Single hull:

- Ships up to 3,000 gt – USD 3,200 per gt or USD 23,496,000, whichever is greater;
- Ships larger than 3,000 gt – USD 3,200 per gt or USD 6,408,000, whichever is greater.

Double hull:

- Ships up to 3,000 gt – USD 2,000 per gt or USD 17,088,000, whichever is greater;
- Ships larger than 3,000 gt – USD 2,000 per gt or USD 4,272,000, whichever is greater.

**b Non-Tank Vessels**

- Ships up to 300 gt – USD 1,000 per gt or USD 854,400, whichever is greater;
- Ships larger than 300 gt – USD 1,000 per gt or USD 854,400, whichever is greater.

**12.4.1.3.2 *The Comprehensive Environmental Response, Compensation and Liability Act, 1980 (CERCLA)***

CERCLA applies to the release or threat of release from vessels or from onshore or offshore facilities into the territory, navigable waters, the contiguous zone, and the Exclusive Economic Zone, (extending as far as 200 miles from the baseline of US coasts) of any hazardous substance, which is defined broadly but does not include petroleum or natural gas.

CERCLA makes a distinction between:

- liability for clean-up costs; and
- liability for claims brought by third parties for loss or damage.

**12.4.1.3.2.1 *Liability for Clean-up Costs***

The owners and operators of ships and onshore or offshore facilities are strictly liable for clean-up costs subject to the same very narrow statutory defences that apply under OPA 90. However, whilst the owners and operators of onshore and offshore facilities have unlimited liability for clean-up costs, the liability of the owners and operators of vessels carrying such cargo for such costs is limited to a maximum of USD 300 per gross ton, or USD 5 million unless the release of the hazardous substance was proximately caused by conduct similar to that which debars the right to limit under OPA 90.

US courts have generally interpreted CERCLA as imposing joint and several liability, so that any responsible party may be potentially held liable for the entire response costs. However, such a responsible party would then have recourse to contribution rights from any other responsible parties.

#### *12.4.1.3.2.2 Liability for Claims Brought by Third Parties for Loss or Damage*

CERCLA does not limit the liability of responsible parties for loss or damage claims brought by third parties as a result of the discharge of hazardous substances. Such claims would include claims for physical and financial loss and for personal injury and loss of life. Indeed, the potential liability for such claims may be long-lasting if hazardous substances which have been taken ashore for storage, incineration or destruction have leaked into the ground soil or ground water and affected the health of workers, residents or bystanders or the potential development value of the land.

#### *12.4.1.3.3 Certificates of Financial Responsibility (COFR)*

In the same way that the CLC regime requires compulsory evidence that shipowners are insured against liability for pollution claims OPA 90 and CERCLA require the owners and operators of ships of over 300 gross tons to apply for and obtain Certificates of Financial Responsibility (COFR) which evidence the fact that they have sufficient financial resources to meet the maximum limited liabilities under these statutes. However, one COFR satisfies the obligations of the owners and operators of such ships under the two statutes and must be given for the limits imposed by each statute although, in the majority of cases, the OPA 90 limit is likely to be the higher of the two. The COFR system is administered by the National Pollution Funds Centre (NPFCC) which issues the relevant certificate once it has been satisfied with the evidence of financial responsibility that has been produced to it by the relevant guarantor. However, it should be noted that some individual states in the US (e.g. California) also have their own COFR requirements that must be adhered to when calling at ports in such states.

COFR guarantors are entitled to rely on the same defences that are available to the responsible parties under OPA 90 and CERCLA. Furthermore, they are not liable if it is proved that the incident was caused by the wilful misconduct of the responsible party. However, guarantors are subject to direct legal action not only for pollution removal costs, but also for all pollution damage recoverable under the statutes up to the maximum sum guaranteed.

Therefore, since the OPA 90 and CERCLA limits of liability can be broken relatively easily whilst it is unlikely that the limits imposed by the CLC regime can be broken, the potential liability of COFR guarantors is greater than that faced by liability insurers who provide compulsory pollution liability insurance certificates pursuant to the CLC regime. For these reasons, the member clubs of the International Group

of P&I Clubs have declined to provide the guarantees that are necessary to obtain COFRs and the majority of these guarantees are supplied by specialist companies which have been created for this specific purpose such as SIGCo, Shoreline and Arvak.

### 12.4.2 Criminal Liability<sup>22</sup>

In recent years, the number of criminal prosecutions for pollution from ships has increased partly as a result of a growth in the volume of regulations to protect the marine environment and partly as a result of a greater desire on the part of coastal states to take punitive measures against offenders. Countries that have adopted the SOLAS and MARPOL Conventions have undertaken to introduce legislation which imposes criminal liability and disciplinary procedures for violations of those conventions. However, some countries or regions have adopted even stronger measures. For example, Directive 2005/35/EC of the EU<sup>23</sup> states that:

*“Neither the international regime for the civil liability and compensation of oil pollution nor that relating to pollution by other hazardous or noxious substances provides sufficient dissuasive effects to discourage the parties involved in the transport of hazardous cargoes by sea from engaging in substandard practices; the required dissuasive effects can only be achieved through the introduction of penalties applying to any person who causes or contributes to marine pollution; penalties should be applicable not only to the shipowner or the master of the ship, but also the owner of the cargo, the classification society or any other person involved.”<sup>24</sup>*

*Penalties for discharges of polluting substances from ships are not related to the civil liability of the parties concerned and are thus not subject to any rules relating to the limitation or channelling of civil liabilities, nor do they limit the efficient compensation of victims of pollution incidents.”<sup>25</sup>*

However, the law, regulation and practise of states in relation to criminal proceedings for pollution appears to be less uniform than it is in relation to civil liability for pollution from ships and is arguably misused in certain cases where the conduct of the crew has, objectively, not been ‘criminal,’ but the extent of pollution and threatened damage has been significant. Political and social elements often play a part in the decision to detain crew members for investigation and possible criminal proceedings and even though *IMO Guidelines on the Fair Treatment*

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22 For more detailed commentary see Chapters 13 and 14 of the *Gard Handbook on Protection of the Environment*, 3rd edition.

23 See also Chapter 14.4.2.2 below.

24 Paragraph 7 of the preamble to the Directive.

25 Paragraph 9 of the preamble to the Directive.

of Seafarers<sup>26</sup> in the event of a maritime accident exist, these Guidelines are sometimes not followed. Even where international law is the source of the relevant regulation, important aspects of enforcement proceedings and penalties may be left to domestic law and practice. Therefore, in the event of a polluting incident, the criminal law of the relevant country should always be considered as well as the penal provisions of international conventions.

### **12.4.2.1 International Conventions<sup>27</sup>**

#### **12.4.2.1.1 Breaches**

The International Convention for the Prevention of Pollution from Ships (1973/1978) (MARPOL) forbids the deliberate release of oily wastes except in limited circumstances and allows ships to dispose of oily wastes if reception facilities are not available at the ports that it visits only if certain stringent conditions are met. If these restrictions are contravened, contracting states are required to impose penalties which are sufficiently severe to act as a deterrent.

However, if the discharge occurs as a result of damage to the ship or its equipment following a collision, grounding etc., there is a violation of MARPOL only if there has been a failure to act reasonably to minimise damage after discovering the discharge, or if the owner or the master acted either with intent to cause damage, or recklessly and with knowledge that damage would probably result.

#### **12.4.2.1.2 Enforcement**

Coastal states have powers under the provisions of the United Nations Convention on the Law of the Sea 1982 (UNCLOS) to take action to enforce actual and suspected breaches of MARPOL. The action that can be taken will vary depending on the location (whether in the territorial sea, the EEZ or beyond) of the violation, and of the ship when enforcement action is taken. However, in appropriate circumstances the coastal state is allowed to engage in 'hot pursuit' on the high seas beyond its EEZ.

#### **12.4.2.1.3 Penalties**

UNCLOS leaves the question of the appropriate penalty to the forum, and was designed to restrict the ability of states to impose custodial sentences to ships of their own flag. Nevertheless, some states have proceeded on the basis that the convention has wider applicability and have detained and subsequently imposed custodial sentences on personnel serving on foreign flagged ships.

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<sup>26</sup> See Chapter 14.4.2.2 below and IMO Circular Letter No 2711 dated 26 June 2006 which can be accessed via [www.imo.org](http://www.imo.org).

<sup>27</sup> See also Chapters 22.3.2.2 and 22.3.2.3 (Maritime Regulation and Compliance).

#### 12.4.2.2 The Criminal Prosecution of Crew Members

Historically, mariners who caused serious maritime incidents were required to answer for their actions or omissions before a court of enquiry and, if found guilty, would lose their licences resulting in most cases in a loss of their livelihoods. However, such action was not taken unless and until it was proved that the mariner had acted with intent, or recklessly, or with gross negligence. Furthermore, it was only if the mariner could be proved to have acted with criminal intent that he would face more serious criminal charges.

However, in recent years, many legal systems around the world have started to treat maritime accidents routinely as crimes, particularly when environmental damage has taken place. In many cases, prosecutions are brought against individual mariners merely because an incident has taken place and irrespective of whether the mariner was guilty of any criminal intent. Indeed, in some cases, a strong case can be made that the mariner in question had behaved perfectly properly with all the skill of a reasonably prudent mariner and that the negligence, if there was indeed any negligence, was that of a local pilot or even that of a local governmental authority. Nevertheless, a criminal prosecution has been brought. This is particularly true following a major incident resulting in significant oil pollution since emotions run high and decisions may be taken in haste by individuals or authorities whilst under pressure from local people affected by the spill and from the media.

The greater use of the criminal law in this manner has been a controversial development involving a number of contentious issues. However, the United States seems to have adopted such a policy as a result of the EXXON VALDEZ pollution incident in 1989. Therefore, the possibility of criminal liability after a pollution incident is almost 'automatic' under the law of some US states which require no intent element to be proven in order to gain a conviction. Other countries have also followed suit. The European Union published the EU Directive on Criminal Sanctions for Ship-Source Pollution in 2005 which sought to make mariners criminally liable if pollution was caused as a result of 'serious negligence,' a term which has no clear meaning either in the civil or the criminal law of most countries. In 2007 the European Court declared that this Directive was invalid. However, a subsequent proposal of the EU Commission has called for "*effective, proportionate and dissuasive penalties which have to be of a criminal nature for natural persons.*"

There are many reasons for such prosecutions. In some cases, the prosecuting authority considers that an example must be made of the crew member as a form of deterrent. In other cases, it is considered that if there is no possibility to bring a successful prosecution or a civil case for damages against the employer of the mariner (e.g. where a vessel owned by a one-ship company is a total loss), the prosecution of the mariner may encourage the employer to offer some sort of



compensation. The matter is also complicated by the fact that it is a violation of the Universal Declaration of Human Rights to withhold a foreigner's passport without due cause since the Declaration provides that:

*"Everyone has the right to leave any country, including his own, and to return to his country."*

Therefore, some countries have taken the view that they cannot justify detaining a mariner unless he has been charged with an offence which is capable of being punished on conviction by a custodial sentence. Regrettably, other countries have used local law(s) to detain individual crew members and sometimes to bring criminal prosecutions against them, despite the fact that there would appear to be a conflict between such local law(s) and international conventions. For example, if the country in question is a party to the United Nations Convention on the Law of the Sea (UNCLOS), the threat of, or the actual, passing of a custodial sentence in a pollution case may well contravene Article 230 which provides that:

*"2. Monetary penalties only may be imposed with respect to violations of national laws and regulations or applicable international rules and standards for the prevention, reduction and control of pollution of the marine environment, committed by foreign vessels in the territorial sea, except in the case of a wilful and serious act of pollution in the territorial sea.*

*3. In the conduct of proceedings in respect of such violations committed by a foreign vessel which may result in the imposition of penalties, recognized rights of the accused shall be observed."*

Nevertheless, US law can oblige a mariner to be detained in the USA for many months after an incident without being charged with any crime on the basis, simply, that he is a 'material witness.'

These concerns came to the attention of the IMO and led to the adoption in 2006 of the *IMO Guidelines on Fair Treatment of Seafarers*. The objective of the Guidelines is "to ensure that seafarers are treated fairly following a maritime accident and during any investigation and detention by public authorities and that detention is for no longer than necessary." The Guidelines address a number of issues relating not only to the length and conditions of detention, but also to a number of factors concerning the fairness of any criminal proceedings against a foreign mariner. However, the guidelines merely have persuasive force rather than the force of an international convention and therefore, the threat of the criminal prosecution of seafarers cannot be discounted and is arguably now to be expected in many countries, at least when there has been a serious incident.

### 12.4.2.3 The Position in the USA

Violations of OPA 90 involve mandatory civil and criminal penalties and all US coastal states impose a further broad range of fines and penalties in connection with a wide variety of violations. Therefore, as stated in Chapter 12.4.2.2 above, the criminal and civil penalties imposed by these states may be greater than those imposed under OPA 90.

The criminal prosecution of shipowners and seafarers for intentional discharges of pollutants prohibited by the MARPOL Convention raise particular difficulties in claims handling. The US takes the position that UNCLOS does not apply to violations of MARPOL that occur within US jurisdiction and criminal prosecutions are routinely brought against both the corporate owner and individuals which, if successful, can result in high penalties and also jail sentences for the individuals involved.

Corporate owners and operators may be held to be vicariously liable for the acts and omissions of crew even when the relevant act or omission is contrary to company policy and done without the knowledge of the shipowner or operator. The monetary penalties that can be imposed may be for millions of dollars and the investigation and prosecution of the case can severely disrupt the vessel's operations.

It is also a crime to lie to a US official or to destroy or tamper with evidence or to advise any other person to do these things and such conduct may result in the imposition of additional charges for the obstruction of justice.

Finally, government prosecutors in the United States are allowed to designate crew members as 'material witnesses' to a crime thereby enabling them to be kept in the United States until testimony is given at trial. This forcible detention can last for many months, and the cost of maintaining the crew members will often be borne by the shipowner.

## 12.5 Salvage Services<sup>28</sup>

In many instances pollution has occurred as a result of an incident such as a collision or grounding and it will be necessary to engage the services of a salvor to either save the ship and cargo or, if this is not possible, to minimise pollution. Historically, salvors operated on a 'no cure-no pay' basis which means that they would be remunerated only if they succeeded in saving the ship and/or cargo and the amount of remuneration would depend *inter alia* on the value of the property that was saved. Therefore, if the salvor considered that there was little prospect in saving the ship and/or cargo they were reluctant to intervene to minimise pollution. This was clearly unfortunate and with the increasing risk of large pollution incidents, steps were taken to provide salvors with the necessary encouragement to intervene to minimise pollution even when the prospects of saving the ship and/or cargo were small.

Salvors are now entitled to 'Special Compensation' when they have taken steps which have succeeded in preventing or minimising pollution even if the value of the salvaged ship and/or cargo is insufficient to provide for a normal salvage award. Salvors are entitled to compensation for the expenses incurred by them whilst undertaking anti-pollution measures and for a further possible increment of up to 100 per cent of such sum. Guidelines as to the amount of compensation are set out in the Special Compensation P&I Clause (SCOPIC) which has been agreed between salvors, P&I clubs, hull underwriters and other parties.

In the event of an incident which has either caused or is likely to cause pollution, it is vital that prompt action is taken to engage reputable and experienced salvors who are able to intervene with the minimum of delay. Such appointment requires prompt liaison with insurers and other parties and is an important claims management issue.

## 12.6 Liability for the Scrapping of Ships

As ships approach the end of their working lives they are no longer considered to be assets that require further investment in order to keep them profitably operational. Consequently, the ship may be either abandoned at some location<sup>29</sup> or more likely, sold to a breaking yard for dismantling and recycling. In either case, the ship itself or the substances that may be found on board the ship may in various ways prove to be pollutants to the environment. The risk may be to the sea whilst the ship is in transit to the scrapping yard or to the yard itself and its environs once the ship

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<sup>28</sup> More detailed commentary can be found in Chapter 14 (Salvage Claims).

<sup>29</sup> If the ship becomes a wreck liability for wreck removal may be incurred. For more detailed commentary see Chapter 16 (Wreck Removal Claims).

has arrived. The risk is also perceived to be greater due to the fact that most of the large scrapping yards are located in the developing world where health and safety regulations are not advanced.

Currently, a ship that is sent for scrapping may well be considered to be 'hazardous waste' for the purposes of the 1989 Basel Convention on the Control of the Transboundary Movements of Hazardous Wastes and their Disposal (The 1989 Basel Convention)<sup>30</sup> since both the structure of the ship itself and the substances that are likely to be found on board the ship fall within the list of regulated substances itemised in Annex I of the convention. Countries that are parties to the convention are not allowed to send hazardous waste to any other country that is not a party to the convention or to any location if it believes that the waste will not be dealt with there in an environmentally safe and acceptable manner. Applications for the cross-border movement of such waste must be made to, and authorised by, the relevant government authorities and must be covered by compulsory insurance. A failure to comply with any of these requirements means that the movement is considered to be 'illegal traffic' which is deemed to be a criminal offence. Furthermore, pursuant to the 1999 Basel Liability Protocol,<sup>31</sup> a failure to comply may render the relevant party subject to strict liability subject to a limit of liability which is to be imposed by national law depending on the quantity of waste but which cannot be less than SDR 30 million for quantities exceeding 10,000 tonnes.

The potential application of the Basel Convention clearly poses a problem for the commercial recycling of ships and, consequently, the IMO has sought to deal with the problem by sponsoring the Hong Kong International Convention for the Safe and Environmentally Sound Recycling of Ships (SRC) 2009.<sup>32</sup> The convention proceeds on the premise that the recycling of ships in a controlled environment is the best way to decommission ships and lays down regulations relating to the design, construction, operation and preparation of ships so as to facilitate safe and environmentally sound recycling without compromising the safety and operational efficiency of ships; the operation of ship recycling facilities in a safe and environmentally sound manner; and the establishment of an appropriate enforcement mechanism for ship recycling, incorporating certification and reporting requirements. Ships that are to be sent for recycling will be required to carry an inventory of hazardous materials, which will be specific to each ship. An appendix to the convention provides a list of hazardous materials the installation or use of which

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30 See also Chapter 22.3.2.2.5 (Maritime Regulation and Compliance).

31 This Protocol is not yet in force.

32 See also Chapter 22.3.2.3.2 (Maritime Regulation and Compliance). This convention is not yet in force but will enter into force when it has been ratified by 15 or more States that represent at least 40 per cent of the world's merchant shipping tonnage. Details of the status of conventions can be accessed via the IMO website at: <http://www.imo.org/About/Conventions/StatusOfConventions/Pages/Default.aspx>.

is prohibited or restricted in shipyards, ship repair yards, and ships will be required to have an initial survey to verify the inventory of hazardous materials, additional surveys during the life of the ship, and a final survey prior to recycling. Finally, ship recycling yards will be required to provide a 'Ship Recycling Plan,' specifying the manner in which each ship will be recycled, depending on its particulars and its inventory.

Breach of the SRC regulations will oblige the relevant state party pursuant to Article 10.3 to impose criminal sanctions which *"shall be adequate in severity to discourage violations of this Convention wherever they occur"*. However, the SRC does not have any provisions providing for civil liability in the event that loss or damage occurs during the voyage to the recycling yard or during the recycling process. However, civil liability may in the majority of cases be regulated by other conventions such as the CLC, Bunker or HNS Conventions considered above.

## 12.7 Relevant Insurances<sup>33</sup>

A pollution incident will normally cause the loss of a quantity of cargo or bunkers and may necessitate the provision of salvage or pollution prevention services. Furthermore, the polluting vessel may incur substantial civil and/or criminal liability to coastal states and private claimants. Consequently, a pollution incident will normally give rise to claims under the following insurances:

- P&I;
- Hull and Machinery;
- Cargo.

In the event of a pollution incident the relevant assured must notify the relevant insurer as soon as possible since the insurer may wish to be actively involved in any decision-making process particularly if there is the possibility of a direct action against the insurer and, since in any event, the assured has a duty to safeguard any subrogated rights that the insurer may have if a claim is settled under the policy.

### 12.7.1 P&I Insurance<sup>34</sup>

Liabilities in respect of pollution have become one of the most important areas of P&I cover, both in terms of the amounts paid and the coverage that is needed, and, therefore, P&I insurance is normally the most likely insurance that will be relevant in relation to pollution liabilities.

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<sup>33</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>34</sup> See Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 38 (Pollution)).

In the event of a pollution incident the owners of the ship will normally claim under their P&I insurance for:

- Costs and expenses incurred by the member for pollution prevention and/or clean-up costs;
- Liability to authorities for pollution prevention and/or clean-up costs including costs incurred in restoring the natural habitat or natural resources;
- Liability to third parties for physical and financial loss and damage;
- Payment of fines imposed for *accidental* discharge or escape of oil from the ship;
- Special compensation payments made to salvors pursuant to Article 14 of the International Convention on Salvage 1989 or pursuant to the SCOPIC Clause;
- Liabilities, losses, costs and expenses which are not covered by the ship's hull and machinery insurances, e.g. one fourth collision liability, or ship's proportion of general average, salvage or special charges which is not recoverable since the ship's value is in excess of the value insured under the hull and machinery policy.

The normal rule that requires the shipowner to pay the relevant cost or expense, or settle the relevant liability, before he is entitled to be indemnified by the P&I insurer does not apply in relation to some pollution claims since the CLC regime and the Bunker Convention require the insurer to become directly exposed to third party claimants pursuant to the compulsory certificates providing evidence of pollution liability insurance that they must provide.

The level of pollution cover that is available from P&I insurers both individually and through the reinsurance policy of the International Group exceeds the limitation provisions of the various tiers of the CLC regime and Bunker Convention as described above but is subject to an overall limit (currently USD 1 billion per incident).

#### **12.7.1.1 Cover for Tankers Trading to the USA**

Under US law the potential liability that shipowners and their liability insurers face is greater than that which would be faced under the CLC regime and other international pollution conventions. Therefore, the members of the International Group of P&I Clubs will provide cover for any liability, costs or expenses (including fines) in respect of oil pollution or any threat thereof arising as a result of an incident to which OPA 90 is applicable only if certain conditions are met, i.e. the tanker owner must declare in advance how often the ship has traded to the USA and provide details of such voyages and must pay an additional premium (the US Voyage Surcharge).

### 12.7.2 Hull and Machinery Insurance<sup>35</sup>

Standard Hull and Machinery (H&M) insurance policies provide the shipowner with cover for physical damage to, or loss of, the ship but do not provide cover for the liability that the shipowner may have for loss or damage caused to third parties by pollution from the ship, which cover is provided by the ship's P&I insurance. However, H&M insurance may have a limited role to play in the event of pollution. For example, the cost of removing oil from a ship after a collision may be considered to be a measure that is necessary to facilitate repairs to the ship and, therefore, recoverable under the ship's hull and machinery insurance.

### 12.7.3 Cargo Insurance<sup>36</sup>

The polluting event may cause the loss of some cargo and the need to take action to preserve the well-being of the remaining cargo. Such action may involve the salvaging of the ship thereby committing the owners of the cargo to pay their proportion of any future salvage award. Alternatively, the cargo could be transhipped to another vessel or the carrying ship could be towed to a repair yard and the cargo discharged and stored ashore pending the completion of repairs, thereby committing the owners of the cargo to pay cargo's proportion of general average charges in due course. Consequently, the owners of the cargo will normally claim under their cargo policy for:

- The quantity of cargo lost;
- Cargo's proportion of any general average or salvage charges.

The level of cover that is available will depend on the terms of the particular cargo insurance that has been placed for the particular carriage. However, in the majority of cases, cover can be expected to be available and in such circumstances the insurers will normally be subrogated in due course to whatever rights the assured may have against the carrier and any other party who has caused the incident which has given rise to the loss of cargo.<sup>37</sup>

## 12.8 Port Authority Liability for Pollution

A port may be administered by a government department or by a private enterprise depending on local law and circumstances. However, in either case, the port authority has a legal personality and has legal rights and obligations. The legal relationship between the port authority and ships using the port may be governed by whatever charter, constitution or statute that regulates the port authority's activities and may also be subject to more general national laws or the

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35 See Chapter 26.3.1.1 (The Structure of Marine Insurance).

36 See Chapter 26.3.3 (The Structure of Marine Insurance).

37 See Chapter 25.5 (The Fundamental Principles of Marine Insurance).

terms of a contract. However, in each case, the port authority will have duties and responsibilities to those using the port and can be sued or prosecuted if they fail in the execution of those duties.

Since the duties and responsibilities of port authorities can differ quite substantially, it is beyond the scope of this publication to comment in detail on the duties and responsibilities of individual port authorities. However, it can be said in general that port authorities owe a duty of care both to ships that use the port and to privately owned installations in the port to ensure that the port is safe and to take steps to maintain it in such condition. Therefore, if the port authority fails to do so, it may (depending on the terms of usage agreed with the relevant ship or installation under the governing charter, constitution, statute or contract) incur liability to the relevant ship or installation. Such claims are notoriously difficult to substantiate but may be possible in appropriate circumstances.

### Example

On 15 September 1996 the SEA EMPRESS which was laden with 130,000 tonnes of crude oil ran aground at the entrance to Milford Haven in the United Kingdom. About 72,000 tonnes of crude oil and 360 tonnes of heavy fuel oil spilled into the sea. Claims were brought by pollution victims against the shipowners and the IOPC Fund and the Fund brought a recourse claim against the Milford Haven Port Authority (MHPA) alleging that the port authority had been negligent in that it had not taken reasonable care to avoid the risk of laden tankers grounding in the port. The Fund alleged *inter alia* that the MHPA had failed to implement an effective vessel traffic service (VTS), to mark the entrance to the west channel and to provide an effective and properly trained pilot service.<sup>38</sup> The Fund also alleged that the pollution response action taken by the MHPA was improvised and negligent. The MHPA denied all of these allegations and the issue was finally settled by mediation, the MHPA paying the sum of GBP 20 million to the Fund.

A similar claim was made against the MHPA by Texaco which was the terminal operator in Milford Haven and this claim was also settled amicably.

Finally, a criminal prosecution was brought against the MHPA by the UK Environment Agency and the MHPA was found guilty pursuant to section 85 of the UK Water Resources Act 1991 which imposes strict liability (i.e. regardless of negligence) on any person who “causes or knowingly permits any poisonous, noxious or polluting

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38 Port authorities have the power and duty under the Pilotage Act 1987 of the United Kingdom to provide pilotage services where necessary, to set the qualifications for pilots and to authorise and disqualify pilots.



waste matter to enter any controlled waters.” The MHPA pleaded guilty to the charge and a fine of GBP 4 million (reduced on appeal to GBP 750,000) and costs were imposed.

## 12.9 Claims Management

Pollution claims are often high-profile incidents which need calm thinking and an ability to keep many balls in the air at the same time. They require the development of a sensible and workable strategy which necessitates the management of people, authorities and the media. Experience shows that difficult incidents such as these are best managed if the relevant personnel have received adequate training beforehand and therefore, know what needs to be done without unnecessary delay if and when a real incident occurs. The need for such pre-planning and training cannot be overstressed and reference is made again to the comments made in Chapter 12.3.2 above in relation to oil spill response.

In the event of a pollution incident shipowners are advised to instruct the crew to follow the guidelines in Chapters 3.1 (General Response Advice) and 3.12 (Pollution) in the *Gard Guidance to Masters*.

It must also be emphasised that since the ship’s P&I club may incur direct liability to third party claimants for pollution, it is very important that the club should be kept fully informed of all developments and fully involved in all discussions. A failure to do so may well prejudice the right of the member to secure the support of the club.

## 12.10 Case Studies

### Case Study 1<sup>39</sup>

In September 1996 a vessel struck a bridge in Portland, Maine, USA as a result of pilot error. The vessel was holed and spilled an estimated 2,100 barrels of diesel oil from a cargo tank and 2,000 barrels of fuel oil from a bunker tank into the river. There was significant oil pollution to the harbour and adjacent areas and oil spread into nearby marshlands as a result of severe weather conditions. The rocky terrain and the significant tidal action hampered clean-up efforts and the port had to be closed for over a week. However, as a result of intensive clean-up work involving some 600 persons and a number of watercraft, almost 141,000 gallons out of the 180,000 gallons of oil spilt was recovered. In the meantime, lobster and clam fisheries and deep-sea fishing boats had been affected, and because of the closure of the port, the deep-sea fishing boats were either trapped in port or could not deliver their catch. Furthermore, over 700 watercraft and extensive port related shore facilities had to be cleaned.

<sup>39</sup> Reference is also made to the reports which can be found in the periodic IOPC Fund Incidents manual – see footnote 14 above.

The owners of the vessel were designated as the 'responsible party' under OPA 90 and claims were made against the vessel for clean-up costs in the region of USD 47 million. Further claims were also brought by lobster and clam fishermen and property owners and others affected by the closure of the port. Finally, claims were brought for damage to natural resources including sawgrass fields, birds, human quality of life etc. Therefore, federal and state law applied simultaneously to the same incident and some claims were subject to OPA 90 whilst other claims were subject to state law. The vessel's limitation figure under OPA 90 was approximately USD 22 million but under the law of the state of Maine, liability was unlimited. Therefore, it was decided to settle the fishing claims for USD 6 million since they would be governed by state law in Maine and would not therefore benefit from limitation of liability.

When it became clear that the clean-up costs that were subject to OPA 90 would exceed the vessel's OPA 90 limitation fund of USD 22 million, the National Pollution Fund Center (NPFC) was notified that the shipowner would be making a claim on the Oil Spill Liability Trust Fund for any sums expended pursuant to OPA 90 requirements that exceeded the limitation fund. Although there was little reason to believe that the shipowner would ultimately be prevented from limiting his liability under OPA in view of the fact that the incident had been caused by pilot error, a number of complex legal issues arose at this stage, which further delayed and complicated the case. However, in January 1999, the shipowner and his P&I club were advised by the NPFC that the vessel was entitled to limit liability to just over USD 22 million. It was also agreed that the owners would submit the relevant claims documentation to the NPFC which would then determine the recoverable excess claims and make payments from the OSLTF as required.

The shipowners had paid costs and claims of nearly USD 72.5 million in total, of which USD 61 million represented the clean-up costs. Therefore, claims for clean-up costs of just over USD 39 million (i.e. USD 61 million minus the limitation fund amount of USD 22 million) and USD 2.34 million in respect of Natural Resource damage were submitted to the NPFC and it was subsequently agreed that the shipowners would receive reimbursement of USD 38.4 million in respect of clean-up costs and USD 2.31 million in respect of Natural Resource damage. This left a balance of just over USD 11.2 million in dispute and the shipowner was eventually obliged to start legal action against the OSLTF. Negotiations then resumed and a settlement of USD 8.75 million was finally agreed with the NPFC. Therefore, at the end of the day, the shipowner and club recovered a large proportion of their expenditure in excess of the limitation amount.

## Case Study 2

A tanker of 31,500 gt carrying a cargo of heavy fuel oil, ran aground in fog off the coast of Denmark as a result of several errors in navigation on the part of the navigating officers. Two cargo tanks were damaged and holed, causing an estimated loss of some 2,700 tonnes of cargo. The oil drifted in large patches towards the coastline and was drawn into a narrow strait between two islands, resulting in relatively severe pollution in these areas.

The Danish National Authorities mobilised resources to combat the pollution. In all, 15 vessels took part in the 'at sea' response that was organised by the Danish Armed Services. These included several specialised Danish vessels, chartered Danish vessels and specialised Swedish and German vessels that were called upon pursuant to regional marine pollution response agreements and contingency plans. The 'at sea emergency response' was completed some six weeks after the incident, by which time approximately 33 per cent of the released oil (897 tons) was estimated to have been collected at sea.

The onshore emergency response was led by the Danish Civil Defence. Approximately 300 people were mobilised and equipped with both manual and mechanical tools. Due to the high viscosity of the oil, it proved very difficult to pump it, and the removal therefore had to be done mechanically with grabs and similar equipment. Following the emergency response, more detailed and specific on shore cleaning was carried out by the relevant municipalities.

The clean-up operation generated large amounts of oily waste, containing oil, water, sand/mud and other debris. Several thousand tons of waste was collected and incinerated. However, only one facility in Denmark was capable of handling such a large quantity of waste material and, therefore, the waste had to be stored temporarily in barges and in on shore pits.

Numerous claims of the following types were submitted.

- 1 Claims for land damage caused by heavy machinery used for mechanical clean-up work. The total cost of these claims was estimated to be USD 200,000.
- 2 Claims by fishermen. Some nets/equipment and boats were oiled and claims were made for cleaning/replacement and for loss of profits totalling approximately USD 300,000-350,000.
- 3 Claims by aquaculture facilities. Several claims were received from trout farms for the alleged loss of the entire production for that season totalling approximately USD 6 million.

The evidence supporting the nature and quantum of the claims was generally poor, especially in the case of the fishermen's claims. Expert evidence was obtained by claimants and the club in relation to the claims brought by the aquaculture facilities but the experts could not agree on whether the entire production for that season had been lost, and if so, whether this was entirely attributable to this incident, or to extraneous factors that would have occurred in any event.

Following the submission of additional evidence by the claimants, and as a result of meetings between the vessel's club and representatives of all three classes of claimant, the following settlements were achieved:

- 1 USD 100,000;
- 2 USD 250,000;
- 3 USD 3.7 million.

Denmark is a party to the Civil Liability Convention (CLC) 1992. Although it was pointed out that security for claims regulated by CLC 92 had already been provided in the form of the 'blue card' that had been issued by the tanker's P&I club, security was nonetheless demanded by the Danish Authorities and at their request, they were provided with a P&I Club Letter of Undertaking in the amount of USD 15 million. The limitation amount for the vessel under the CLC 92 was approximately USD 24.65 million and consequently, STOPIA did not apply.<sup>40</sup>

About two weeks prior to the three year time bar for pollution claims under CLC 92, a meeting was held between the shipowners, their P&I club and the Danish authorities with the aim of settling the outstanding pollution claims. There was no need for the authorities to prove liability, as this is virtually strict under the convention and none of the very limited exceptions from liability applied. The P&I club had previously settled 75 per cent of the authorities' claim for costs relating to the offshore emergency response on a lump sum basis, pending negotiations. The original claim of USD 9 million made by the authorities had been negotiated down to USD 8.2 million, of which 75 per cent (USD 6.15 million) had been paid 'on account.' Following this meeting, payment of a further USD 1 million was made, leaving USD 1.05 million in dispute.

As the time-bar was rapidly approaching, the authorities were compelled to commence legal proceedings for the disputed amount. Although a time extension had been offered, this was not sufficient since, technically under the CLC convention, a time extension cannot be provided. Settlement negotiations resumed shortly thereafter and the outstanding amount was settled in the sum of USD 800,000. Therefore, the total amount paid in relation to pollution response/

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40 STOPIA does not apply when the ship's limit under CLC 92 exceeds SDR 20 million.

clean-up and pollution damage was USD 12 million, and because this amount fell within the vessel's limit of liability under the CLC 92, it was not necessary for the owners to start proceedings in Denmark to limit their liability.

As a result of the incident some 2,700 m<sup>3</sup> of cargo had been lost. However, the cargo claimants failed to protect the one year time limit within which proceedings would have had to be commenced and failed to ask for a time extension.

Subsequently, cargo claimants tried to avoid the one year time limit by commencing proceedings in several jurisdictions. None of these proceedings was pursued actively and no payment was made to cargo interests. In any event, investigations suggested that the owners would have had a potential defence to this claim, based on the 'negligent navigation' defence in Article IV Rule 2 (a) of the Hague-Visby Rules even if the claim had been pursued.



# 02

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Related Issues

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## Chapter 13

# Safe Ports Claims<sup>1</sup>

### 13.1 Introduction

Throughout their working life ships will visit various ports, berths, anchorages, offshore locations etc. In most cases, a ship may visit and use such places without any danger. However, this is not always the case and ships can suffer damage ranging from scraped paintwork to total loss as a result of some (usually latent or unexpected) dangerous feature of the place visited. Alternatively, they may suffer delay whilst the danger is removed. In such circumstances, shipowners may wish to claim against the port authority or against whoever is their contracting partner under the relevant charterparty or contract of carriage. Whilst it may be possible to make a claim against the port authority, such claims are notoriously difficult to substantiate. Therefore, shipowners are more likely to bring a claim under the governing contract of carriage. Consequently, most contracts of carriage (whether charterparties, bills of lading, sea waybills etc.) have provisions regulating where the vessel is allowed to trade.

### 13.2 Contractual Provisions Relating to Safety

#### 13.2.1 Specific Clauses<sup>2</sup>

In some instances, there may be specific clauses dealing with specific situations. Some clauses may expressly forbid sailing to a certain location where there is a known risk such as a current war, ice or an international embargo. However, danger is not always a permanent feature or cannot always be avoided and therefore, other clauses are designed to establish the rights of the parties if a ship were to encounter danger in such circumstances. For example, most time and voyage charterparties, bills of lading, sea waybills etc., will have clauses regulating the right of the parties

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<sup>1</sup> For more detailed commentary see Chapter 10 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008 and Chapter 5 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007.

<sup>2</sup> For more detailed commentary see paras. 12.22 to 12.24 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007 and Chapter 28 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008.

in relation to areas which are prone to war or ice risks and the use of such clauses can be expected to increase as the instances of particular dangers increase, e.g. the development of the BIMCO Piracy Clauses for time and voyage charters. Such clauses (called Liberty or Caspiana Clauses) tend to be detailed and spell out exactly what can be done in those situations. They usually provide that:

- The ship is allowed to avoid areas affected by such dangers;
- The ship is allowed to proceed to alternative ports;
- The terms of the contract of carriage remain in full force whilst the ship is doing so; and
- The ship is not considered to be deviating.

Even if the contract does not have a Caspiana Clause which deals with the specific risk, Article IV Rule 4 of the Hague-Visby Rules which apply to most contracts either compulsory or by agreement provides that a carrier is entitled to commit a 'reasonable deviation' without incurring liability provided that the deviation is caused by a fortuity, is not caused by a breach of contract or duty on the part of the carrier and is not done purely for the carrier's own benefit.<sup>3</sup>

### 13.2.2 General Provisions

Since parties cannot always predict all the specific kinds of danger that can potentially be encountered, contracts also tend to have more general provisions relating to the use of safe ports, berths, terminals or other locations.

The parties to a voyage charter or bill of lading will normally know where the vessel is to trade before concluding the contract. Therefore, the shipowner is given the opportunity to ensure that the port is safe for his vessel before agreeing to conclude the fixture. However, this is not always the case since the contract may provide for a range of possible ports (e.g. *"1/2 ports East Coast North America range"*) in which case the shipowner will not know the precise port when entering into the contract since the port will not be nominated by the charterers until later. Similarly, the nature of a time charter is such that the shipowner will not normally know when entering into the contract where the vessel will trade in due course since the time charterers are given the right to direct the employment of the ship during the currency of the charter.<sup>4</sup>

The distinction between the two situations is highly relevant. In the case of a contract for a specified port or place the shipowner is normally held to have accepted the risk of proceeding to the port when entering into the contract since he has had the

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3 For more detailed commentary see paras. 85.355 to 85.361 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007 and paras. 10.264 to 10.284 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006.

4 See Chapter 4.5.2 (Charterparty Claims).

opportunity to check the safety of the port for himself. Therefore, he cannot bring a claim against the charterers if the port proves in due course to be unsafe. However, where the contract allows the charterers the right to nominate a port or place in due course, the charterers are normally obliged to nominate a port or place that is safe and are liable for any loss or damage suffered by the shipowner if the port or place proves to be unsafe. This principle normally applies even if the adjective 'safe' has not been added to the designation of the ports or places to be visited (e.g. "1/2 ports East Coast North America range"). However, to add emphasis to this principle, time charters normally provide expressly that the vessel must trade "between **safe** ports" whilst contracts which provide for a range of possible ports normally provide that when the charterers exercise their right to nominate a port, that the port must be a 'safe port' (e.g. "1/2 safe ports East Coast North America range").

The addition of the adjective 'safe' is normally considered to be a promise by the charterer that the particular port will be safe. Consequently, such an addition may alter the rule that normally applies in the case of voyage charters when the port or place has been expressly identified in the contract. Therefore, a voyage charter which provides for "one **safe** port Ventspils" instead of "one port Ventspils" may make the charterers liable if the port is found in fact to be unsafe.

### 13.3 The Nature of Liability

If the charterers are obliged to nominate a safe port but order the vessel to an unsafe port, then they are in breach of contract even though they may not in fact be aware of the dangerous nature of the port. Liability is strict in the same way as it is in relation to dangerous goods.<sup>5</sup> Therefore, if the port is unsafe the charterer may be liable even if they did not know or had no means of knowing that the port was unsafe. For this reason, some charterparties (particularly tanker charters) now provide expressly that the charterers are to be liable only if they have not exercised due diligence to send the vessel to a safe port or berth. For example, Clause 4 of the Shelltime 4 charter provides that:

*"Charterers shall exercise due diligence to ensure that the vessel is only employed between and at safe places (which expression when used in this charter shall include ports, berths, wharves, docks, anchorages, submarine lines, alongside vessels or lighters, and other locations including locations at sea) where she can safely lie always afloat. Notwithstanding anything contained in this or any other clause of this charter, Charterers do not warrant the safety of any place to which they order the vessel and shall be under no liability in respect thereof except for loss or damage caused by their failure to exercise due diligence as aforesaid."*

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<sup>5</sup> See Chapter 7.2.3 (Dangerous Goods Claims).

The aim of such clauses is to soften the strict liability which would otherwise exist. However, it appears that if the charterers are to prove that they have exercised due diligence, they must prove that due diligence has been exercised not only by them personally but also by all their servants and agents. Problems sometimes arise in this regard since enquiry is sometimes made of the operator of a refinery or similar installation which may be acting in a dual capacity – port authority and charterers’ agent. Therefore, if the operator is held to be acting in its commercial capacity as the charterers’ agent when giving the relevant advice, the charterers may be liable if the advice that is given is negligent.

### **13.4 The Meaning of ‘Safe’**

The English High Court gave the following classic definition of what is or is not a safe port in *The Eastern City*:<sup>6</sup>

*“A port will not be safe unless, in the relevant time, the particular ship can reach it, use it and return from it without, in the absence of some abnormal occurrence, being exposed to danger which cannot be avoided by good navigation and seamanship.”*

The following factors are relevant:

#### **13.4.1 “the particular ship”**

The safety of the port is tested in relation to the particular ship since ports may be safe for some ships but not for others. Therefore, factors such as the size, draft, beam, etc., of the ship will be relevant in that regard and the mere fact that many ships have been able to use the port safely is not conclusive since such ships may have different characteristics.

#### **13.4.2 “safe”**

##### **13.4.2.1 Temporary Unsafety**

Unless the charter provides that the port is to be safe at all times, a port will not be considered dangerous if the danger is temporary and is avoidable if the vessel waits for a period of time which is not long enough to frustrate the contract. Nevertheless, if it is the natural characteristic of the port that it is regularly affected by perils which are temporary in duration, then that will not prevent the port from being considered to be dangerous.

For example, if the port is affected by bad weather when a vessel arrives, the vessel is expected to wait until the bad weather is over before berthing. Since the hazard is temporary, the port is not considered to be dangerous. However, if a port is regularly

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<sup>6</sup> [1958] 2 Lloyd’s Rep. 127.

affected by bad weather which, although temporary in nature, is of such ferocity and unpredictability that a ship can be trapped inside the port without adequate protection, the port may be unsafe.

#### **13.4.2.2 Unsafe Infrastructure**

A port may be dangerous if there is no adequate checking or warning system or infrastructure at the port to enable vessels to use it safely. For example, if a ship were to be ordered by charterers to proceed to a port where it sustained serious bottom damage caused by an underwater obstruction in the dredged channel into and out of the port, the port would probably be considered to be unsafe if there was no proper system in place to investigate reports of obstacles in the channel and/or to find and remove such obstacles and/or to warn vessels by the use of buoys and notices to mariners that there was an obstacle in the channel.

#### **13.4.2.3 Political or Legal Unsafety**

A port can be unsafe not simply for physical reasons but also for political or legal reasons, particularly if there is a risk of extended delay, detention, confiscation or 'blacking.' For example, if entry to a port requires governmental permit but, due to an insurrection, the government has refused all permits, the port is probably unsafe since, if the vessel were to proceed there without a permit, she would be susceptible to confiscation by the government.

#### **13.4.3 “can reach it, use it and return from it”**

The promise of safety is not restricted to the port limits but also encompasses the approaches to and from the port. This is particularly relevant in the case of river ports since the only way into and out of the port is by navigating the river. Therefore, if the river passage is unsafe the port is considered to be unsafe. However, the principle is of general application and applies equally to non-river ports. The question is one of fact in each case. Are the approaches to and from the port safe?

#### **13.4.4 “in the relevant time”**

The relevant time is the time that the vessel will be using the port. The charterers promise that the port will be safe for the vessel for the whole of the time that she remains at the port. Therefore, for example, the fact that a port will be unsafe because of hostilities at the date of the charter, or at the date that the vessel is delivered to the charterers, or at the date that the port is nominated, is irrelevant if the hostilities will have ended by the time that the vessel arrives at the port in due course.

### **13.4.5 “in the absence of some abnormal occurrence”**

The charterers merely promise that the usual and normal characteristics of the port make it safe. Therefore, if the danger is the result of an abnormal occurrence at the port (i.e. one which a reasonable person would not normally expect at that port), then even though the port is unsafe in fact, the charterers are not guilty of a breach of contract. Classic examples of abnormal occurrences are the tsunamis which have affected ports in Asia in recent years.

However, occurrences which are considered abnormal at one point in time may be considered normal at another point in time and *vice-versa*. For example, if a vessel were to be ordered to a port at a time of peace but was detained in the port due to the sudden and unexpected outbreak of hostilities, the charterers would probably not be considered to be in breach since hostilities were not a normal characteristic of the port. However, if another vessel were to be subsequently ordered to the same port after the hostilities had continued for some time, then the hostilities might be considered to be a normal characteristic of that port and the charterers might well be considered to be in breach.

### **13.4.6 “without ... being exposed to danger which cannot be avoided by good navigation and seamanship.”**

Whatever be the nature of the danger, the port will not be dangerous if the danger can be avoided by the use of reasonable care and skill on the part of the master and crew. However, if the degree of skill that is required to avoid the danger is greater than that which is normally expected of a reasonably competent mariner, then the port may be unsafe.

## **13.5 Safe Berths**

Sometimes, a contract will specify that the ship is to proceed to a berth rather than simply to a port. In such circumstances, the general principles described above in Chapters 13.2-4 above in relation to safe ports will normally also apply in relation to the berth.

Therefore, if the contract specifies that the vessel is to load at a berth to be nominated by the charterers at a named port without expressly stating that either the port or the berth is to be ‘safe’ (e.g. “*one/two berths Swansea*”) then, so long as the nominated berth has no special characteristics which distinguish it from other berths at that port, the charterers will not normally be held to have promised that the berth that they nominate will be safe.

However, if the charter includes an express term as to the safety of the berth (e.g. "one/two **safe** berths Swansea") then, for the reasons given above in Chapter 13.2.2, the charterers have promised that the berth(s) that they will nominate at Swansea will be safe.

Nevertheless, the situation is often more complicated. For example, if the charterers are to nominate a berth (without specifying whether the *berth* is to be 'safe') at 'a safe port', (e.g. "one/two berths at one **safe** port East Coast North America") then the safety of the port encompasses the whole of the port area including the berth and the charterers will normally be held to have promised that the port and the berth that they nominate will be safe.

However, if the charterers are to nominate 'a safe berth' at a named port (without specifying whether the port is to be 'safe') (e.g. "one/two safe berths Swansea"), the charterers will not normally be held to have promised that the berth that they nominate and its approaches will be free of dangers that affect the port as a whole, but to have promised that the berth will be free of other kinds of danger. For example, a vessel was ordered in one case to proceed to "1/2 safe berths Bandar Abbas, 1/2 safe berths Bandar Bushire, 1/2 safe berths Bandar Khomeini in Charterers' option" during the Iran/Iraq war. The court held that the charterers had not promised that the approach voyage through the Gulf war zone to reach the specified ports would be safe or that the nominated berth would be free of the war perils that affected the port as a whole, but had promised that the berth and its approaches would be free of other *marine* perils.<sup>7</sup>

### 13.6 The Shipowners' Remedies

If a ship is directed by charterers to a port or berth that is unsafe then two different issues arise:

- Can the shipowner be compelled to proceed to that port or berth?; and
- Can the shipowner recover damages for loss or damage incurred as a result of entering such port or berth or reasonably refusing to enter such a port or place?

#### 13.6.1 Can the Shipowners be compelled to proceed to that Port or Berth?

If a specific Liberty or Caspiana clause is applicable then that clause will usually specify exactly what rights the carrier has to avoid the danger.<sup>8</sup> However, the ship may encounter other dangers which are not governed by such clauses and therefore, it is also necessary to consider the rights of the shipowner generally in such circumstances.

<sup>7</sup> *The APJ Priti* [1987] 2 Lloyd's Rep. 37.

<sup>8</sup> See Chapter 13.2.1.

Charterers will normally promise that the port *will* be safe for the vessel when she gets there in due course. Therefore, if a reasonable mariner would conclude at the time that the charterers' order is given that the port will be unsafe for the vessel when she gets there in due course, then the vessel need not normally comply with the order. The reason for this is that, for public policy reasons, the master has an overriding duty to safeguard the interests of the ship and crew. However, if a reasonable prudent mariner would conclude at the time that the charterers' order is given that the port will be safe for the vessel when she gets there in due course then the vessel must comply with the order and proceed to the nominated port. However, if the port subsequently becomes unsafe, the master has the right to refuse to proceed further.

In some instances, it is not completely clear whether the port is or will be safe or unsafe. This is a difficult situation for the master and crew since if the ship were to proceed into an obviously unsafe port with the result that the ship were to suffer damage or loss, the owner would not normally be entitled to any damages since the cause of the loss or liability is not the order of the charterer but the fault or neglect of the owners' own servant or agent in the proper performance of his navigation duties.<sup>9</sup> However, courts and tribunals appreciate that the master and crew may often find themselves 'on the horns of a dilemma' and any decision that they take in such circumstances will normally be supported unless it is clearly a decision that would not have been taken by a reasonably prudent mariner.

If a port is safe when the ship is first ordered to proceed there but becomes unsafe later, the question arises whether the charterers or cargo interest are entitled or obliged to order the vessel to proceed to an alternative port. In the case of time charters, it appears that the charterers are obliged to issue new orders to proceed to an alternative safe port.<sup>10</sup> The position is not so clear in the case of voyage charters or bills of lading. However, such contracts normally provide expressly that the vessel is to proceed to the named or nominated port "*or so near thereto as the vessel can safely get.*" Therefore, if the named or nominated port becomes unsafe, the parties can usually make use of these words to make the contract workable in the changed circumstances.<sup>11</sup>

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9 Such fault or neglect is normally referred to as the '*novus actus interveniens*' (i.e. the intervening act) of the master.

10 See *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition 2008 at para. 10.51.

11 See *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition 2007 at paras. 5.28 to 5.30.



### 13.6.2 Can the Shipowners recover Damages for Loss or Damage incurred as a Result of entering such Port or Berth?

In many instances the vessel has already entered the port or berth before the danger has become manifest and therefore, there has been no opportunity to avoid it.

In such circumstances, the shipowners are normally entitled<sup>12</sup> to claim damages for losses suffered by them as a result. Damages may normally be recoverable for physical damage to the ship, or for the cost of salvaging the ship or removing the wreck, or for the cost of avoidance measures, or for any delay that may be caused to the ship. The shipowners may also incur liability to third parties and may be entitled to claim an indemnity from the charterers or their contracting partner under the relevant contract of carriage for any sums that they have been obliged to pay to such third parties. Such claims may be very large as they were, for example, in the case of the *Aegean Sea*<sup>13</sup> which ran aground whilst proceeding to berth at La Coruna and caused substantial pollution. Consequently, the following claims were brought by third parties against the shipowners:

- Damage to property owned by third parties;
- The cost of clean-up and other preventative measures taken by third parties;
- The loss of use and loss of profits' claims by fishing boat owners, yacht owners, fish and shellfish farm owners, shell fish harvesters, fishing net and fishing pot owners, shop owners, local municipalities, the government of Galicia and the state of Spain.

Damages may also be recovered for losses suffered by the shipowner when the master reasonably refuses to enter a port which is found to be unsafe contrary to the charterers' promise of safety.

### 13.7 Limitation of the Charterers' Liability<sup>14</sup>

The liability of a charterer for sending a vessel to an unsafe port is frequently strict and such liability can result in very substantial damages, e.g. damage to or loss of the ship and/or cargo on board, reimbursement of the shipowners' pollution liabilities etc. Therefore, the charterer will wish to limit his liability for such claims. However, in order to qualify for the right to limit, a person seeking such right must prove that he is a "*person entitled to limit*" and the claim is of the type for which limitation is allowed. Whilst a charterer is a "*person entitled to limit liability*" under the 1957 and 1976 Limitation Conventions (and the 1996 Protocol thereto), the English court has concluded in the leading case of the *CMA Djakarta*<sup>15</sup> that charterers are not entitled to limit their liability for damage caused to the vessel itself

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<sup>12</sup> Subject to any *novus actus interveniens* on the part of the master. See footnote 9.

<sup>13</sup> (1998) 2 Lloyd's Rep.39.

<sup>14</sup> For more detailed commentary see Chapter 21 (Limitation of Liability).

<sup>15</sup> [2004] 1 Lloyd's Rep. 460.

since such a claim is not a claim which is “*subject to limitation*” under Article 2 of the 1976 Convention or, probably, the 1957 Convention. However, it appears that a charterer would be entitled to limit his liability for the value of other property that may be lost or damaged (e.g. containers or bunkers) or for loss or damage to shore based property or for any indemnity claim that may be brought by the shipowners for payments made by them to third parties for such claims or for pollution claims.<sup>16</sup>

## **13.8 Insurances<sup>17</sup>**

### **13.8.1 Hull and Machinery Insurance**

Claims for physical damage to the ship caused by entering an unsafe port or berth will normally be covered by the shipowner’s Hull and Machinery insurers unless loss or damage has been caused by “*derelect mines torpedoes bombs or other derelect weapons of war*” in which case it is the War Risk insurers that will cover the risk.<sup>18</sup> However, Hull and Machinery insurers will not cover losses caused by delay in either avoiding unsafe ports or berths or as a result of entering such places.

Hull and Machinery insurers will normally have the subrogated right to take over whatever rights the shipowner may have to claim an indemnity from any other party who may be liable for sending the ship to a dangerous port or berth. Should Hull and Machinery insurers decide to pursue claims against other parties either in their own name or in the name of the shipowner, the Hull and Machinery insurers are normally responsible for costs which are incurred by the shipowner in that respect. For that reason, such costs are normally excluded from the Defence cover that may be provided by the shipowners’ P&I insurers.

### **13.8.2 P&I Insurance<sup>19</sup>**

In the event that pollution is caused as a result of sending the vessel to an unsafe port or place the vessel’s P&I club may have direct liability for pollution claims pursuant to the certificates (Blue Cards) which the International Group clubs normally issue under the provisions of the CLC and Bunker Conventions. In such circumstances, it is the club that has the subrogated right to take over whatever rights the shipowner may have to claim an indemnity from any other party who may be liable for sending the ship to a dangerous port or place.

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<sup>16</sup> For further commentary see Chapter 21.3.3.2 (Limitation of Liability) and pages 17 to 21 of *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, Informa, 4th edition, 2005.

<sup>17</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>18</sup> See for example, Clause 23.3 of the International Time Clauses Hulls 1/10/83.

<sup>19</sup> For further commentary see Chapter 12.7.1 (Pollution Claims), Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 38 (Pollution)).

### 13.8.3 Cargo Insurance<sup>20</sup>

The incident that causes damage to the ship may also cause damage to or the loss of the goods themselves. On the face of it, the standard cargo insurance terms ICC provide cover for at least some of the likely claims since the ICC A terms insure the goods against 'all risks' whereas ICC B and C insure the goods against "vessel or craft being stranded grounded sunk or capsized" or "collision or contact of vessel craft or conveyance with any external object other than water." However, such clauses normally exclude cover when loss or damage has been caused by "derelict mines torpedoes bombs or other derelict weapons of war." Furthermore, cargo insurers will not cover losses caused by delay in either avoiding unsafe ports or berths or as a result of entering such places.

### 13.8.4 Charterers' Liability Insurance<sup>21</sup>

Charterers can insure their liabilities to third parties as a result of sending the ship to an unsafe port or berth under two separate forms of insurance:

- Liability to shipowners for damage caused to the ship (Charterers' liability for Hull (CLH) or Damage to Hull (DTH)) cover; and
- Liability to other parties such as the owners of cargo on board, i.e. P&I cover.

Such insurances are normally provided on a fixed premium basis by P&I clubs or by other market insurers. For example, Gard's Comprehensive Charterers' Liability Cover provides cover for the liability of charterers for, *inter alia*:

- Damage to or loss of the ship;
- Salvage of the ship or wreck removal;
- Pollution;
- Shipowners' claims for consequential losses such as demurrage, detention, loss of hire or loss of use, or for an indemnity for any liability that shipowners may have to third parties.

Although this cover is entitled 'Comprehensive Charterers' Liability' it can also be extended by agreement to provide cover for a charterer or affiliate that is held liable in its capacity as owner of cargo rather than as charterer.

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<sup>20</sup> For further commentary see Chapter 26.3.3 (The Structure of Marine Insurance).

<sup>21</sup> For further commentary see Chapter 26.3.2 (The Structure of Marine Insurance).

### 13.9 Claims Management

Irrespective of whether it is the shipowners or charterers or cargo interests that have the contractual responsibility to provide a safe port or berth, the reality of life is that it is the shipowner who is likely to suffer in the first instance if these duties are not complied with. However, the shipowners may have the right to be indemnified by the charterers or cargo interests who will not have the benefit of limiting their liability for damage to the ship.

Therefore, it is very important that shipowners and charterers should exercise care to double-check the suitability of any port or berth that may be named or nominated. Substantial assistance may be gained in that respect from local agencies at the relevant port (e.g. the vessel's local agent, P&I correspondents, Lloyds' Agents etc.) and from the detailed guidance in reference books such as the Pilot Book, Ports of the World, The Guide to Port Entry etc. Furthermore, any failure by the shipowner to exercise such care may not only prejudice his rights to an indemnity from the shippers but also his rights under the relevant insurances.

If the ship enters an unsafe port and is damaged or delayed as a result, or if the master refuses to enter a port or berth which he considers unsafe, or takes steps to avoid danger en route, it is very important that a detailed record is kept of the relevant circumstances and of the steps taken by the ship. Prompt action should also be taken by the ship to report problems to shore based management. Detailed guidance in this respect can be found in Chapter 2.13 of the *Gard Guidance to Masters*.

### 13.10 Case Study

The vessel is time chartered with a safe port warranty, voyage chartered with a safe port warranty and sub-voyage chartered with a safe port warranty that names the port. Gard's insured is the voyage charterer who is covered under Gard's Comprehensive Charterers' Cover including cover for Charterers' Liability to Hull (DTH). The vessel grounds at the port and owners claim against the time charterer under the safe berth warranty and time charterer claims against the voyage charterer who claims against the sub-charterer. All claims are submitted to arbitration. The arbitration award finds that the port is unsafe, that the time charterer is liable to the owner and that the voyage charterer insured with Gard is liable to the time charterer for 100 per cent of the USD 3 million claim. The arbitration award finds that the sub-voyage charterer is not liable to Gard's voyage charterer because the sub-voyage charter named the port. The final arbitration award plus costs and the costs of defence are covered by the Comprehensive Charterers Cover.

Further example of relevant case studies can be found in Gard's brochure for its Comprehensive Charterers' Liability Cover which can be found at <http://www.gard.no/ikbViewer/Content/67630/SCC%20Brochure.pdf>.

## Chapter 14

# Salvage Claims<sup>1</sup>

### 14.1 Introduction

When ships get into difficulties it is often the case that specialist assistance is needed urgently in order to prevent the ship and her cargo from being damaged or lost. It has been the public policy of most maritime states for centuries to encourage seafarers to go to the aid of others who may be in danger on the seas and this policy is now enshrined in Chapter V, Regulations 33.1 of the Safety of Life at Sea (SOLAS) Convention.<sup>2</sup>

*“The master of a ship at sea which is in a position to provide assistance, on receiving information from any source that persons are in distress at sea, is bound to proceed with all speed to their assistance, if possible, informing them or the search and rescue service that the ship is doing so.”*

Salvage services can be rendered by ordinary commercial vessels but in the majority of cases, such services are rendered by professional salvors who have invested in specialist ships and equipment and who provide their services on a professional basis. This form of assistance (salvage) should be distinguished from the ordinary day-to-day towage assistance that ships may require, e.g. when entering or leaving the berth or port. Such assistance is planned in advance and is not necessitated by any unexpected peril whilst salvage services are normally required only after the ship has got into difficulties and needs assistance. Therefore, the nature of the services is very different. In the former case the parties will normally negotiate a towage contract, normally on standard terms, in advance in which the nature of the services and the remuneration will be agreed. It may also be possible to negotiate terms

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<sup>1</sup> For more detailed commentary see Chapter 10 of the *Gard Handbook on P&I Insurance*, 5th edition, Brice: *The Maritime Law of Salvage* by Reeder, Sweet & Maxwell, 5th edition, 2012 and the website of the International Salvage Union: [www.marine-salvage.com](http://www.marine-salvage.com).

<sup>2</sup> See also Chapter 22.3 (Maritime Regulation and Compliance).

after the ship has suffered an incident and requires assistance but that will only be if the ship and/or cargo are not in immediate danger, e.g. when there is an engine breakdown on the high seas in good weather conditions well away from any source of peril.<sup>3</sup>

Salvage rights and obligations are now governed predominantly by the International Convention on Salvage 1989 which applies to *“any act or activity undertaken to assist a vessel or any other property in danger in navigable waters or in any other waters whatsoever.”* However, if the vessel and/or cargo is in imminent danger, there will often be no time to negotiate terms and the ship may be obliged to engage the services of a professional salvor under a standard form of salvage contract, the best known being the Lloyd’s Open Form of Salvage Agreement (LOF).<sup>4</sup> The LOF form has been periodically revised over the years, the most recent being in 2000 and 2011 but all the forms provide that the salvor is to use its best endeavours to save the property at risk and take it to a place of safety as agreed. Remuneration under LOF and similar contracts is based on the principle of ‘no cure-no pay’ which means that the salvor is rewarded only if it succeeds in saving the ship and/or cargo and receives no reward if it fails in that respect. However, it is the public policy of most maritime nations to encourage salvors and therefore, the quantum of the reward is determined by a specialist system of arbitration and is determined by an evaluation of the following factors:

- The degree of danger to human life and to the salvaged property;
- The value of the life or property saved;
- The degree of skill demonstrated by the salvor;
- The degree to which the salvors have invested in equipment, personnel and training;
- The risks faced by the salvor;
- The cost to the salvor of performing the salvage services.

LOF provides for disputes to be resolved by arbitration in London in accordance with English law. There is a small panel of highly experienced salvage arbitrators, one of whom will be appointed as the arbitrator by Lloyd’s Salvage Arbitration Branch at the request of the parties, and any appeal therefrom will be heard by the appeal arbitrator (of whom there is only one). Where the salvaged fund is small or where the facts are uncomplicated or no point of law arises, the arbitrator may order

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<sup>3</sup> See also Chapter 15.1.1 (Towage Claims).

<sup>4</sup> Copies of LOF contracts and all other associated documents and rules may be accessed at <http://www.lloyds.com> (follow the links to the Lloyd’s Agency Department and Salvage Arbitration Branch).

that the claim be determined on documents alone in accordance with the Fixed Cost Arbitration Procedure (FCAP), in which case, the overall costs and the recoverable costs are fixed at a maximum sum.<sup>5</sup>

As from 2011 records of the awards that have been made by the Lloyd's Salvage Arbitrators in London are publicly available and these records, whilst in no way binding or conclusive in any future arbitrations will, nevertheless, be a useful guideline to the likely award in any future similar salvage arbitration.

However, there is one important exception to the principle of 'no cure-no pay.' Salvors are entitled to 'Special Compensation' when they have taken steps which have succeeded in preventing or minimising pollution even if the value of the salvaged ship and/or cargo is insufficient to provide for a normal salvage award. Salvors are entitled to compensation for the expenses incurred by them whilst undertaking anti-pollution measures enhanced by a percentage of such expenses. Remuneration is normally based on the pre-agreed tariff rates set out in the Special Compensation P&I Clause (SCOPIIC) which has been agreed between salvors, P&I clubs, hull underwriters and other parties. The SCOPIIC Clause may be incorporated into LOF and if so incorporated, may be invoked by the salvors at any time of their choosing.<sup>6</sup>

## 14.2 Contributing Interests

In the event of peril the following interests are normally at risk:

- Human life;
- The ship;
- The cargo;
- Bunkers;
- Containers;
- Freight.

In general terms, the master is considered to have authority as an agent of necessity to enter into a salvage contract on behalf of all such interests and therefore, to bind each interest to pay their proportion of any subsequent salvage award. This authority is now enshrined in Article 6.2 of the International Convention on Salvage 1989 which states that:

*"The master of a ship in distress has authority to bind the owners of property on board the ship to a salvage contract."*

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<sup>5</sup> Full details of the service provided by Lloyd's Salvage Arbitration Branch and copies of the Lloyd's Standard Salvage and Arbitration (LSSA) Clauses and Procedural Rules can be found on <http://www.lloyds.com> (see footnote 4).

<sup>6</sup> See Chapter 14.9 Case Study.

If such interests are saved as a result of the salvage services, the salvage award is payable by each interest according to the proportion that the post-salvage value of each interest bears to the total value saved. However, there is one exception to this rule. Since it is difficult if not impossible to value human life in financial terms, Article 16 of the International Convention on Salvage 1989 makes it clear that persons who are saved are not expected to contribute to the salvage award. If the salvors succeed in saving human life and property, the salvage award is consequently increased and the enhanced award is shared proportionally between the other salvaged interests. However, in the unusual case that the salvors save human life but no property, there is generally no right on the part of the salvors to recover from the persons saved. Nevertheless, the public policy of some countries (e.g. the UK) requires the government to make some payment to the salvors in such circumstances (i.e. to pay for life salvage).

The salvor generally has a maritime lien on physical salvaged property such as the ship, the cargo, containers or bunkers and may arrest that property unless he receives adequate security for that property's proportion of any subsequent salvage award.<sup>7</sup> The salvor will normally require separate security from each of the salvaged interests and where LOF has been signed, such security must be provided within 14 days of the completion of the salvage services, failing which the salvor is entitled to arrest that property. Where the property at risk is insured such security is normally provided by insurers acting for each interest<sup>8</sup> and usually in a form published either by the International Salvage Union (ISU) or by the Council of Lloyd's.<sup>9</sup> However, where the property at risk is uninsured, the onus is on the owners of that property to provide security in a form acceptable to the salvor.

If the vessel is time chartered at the time of the salvage services it is likely that the bunkers will be the property of the time charterers and will consequently be at their risk. Therefore, liability for that proportion of the salvage award which is payable in respect of the value of bunkers saved will be borne by the time charterers and their insurers. On the other hand, if the vessel is voyage chartered, the bunkers will normally be owned by the shipowner and that proportion of the salvage award which is payable in respect of the value of bunkers saved will be borne by the shipowners and their insurers.

Similarly, the containers (whether full or empty) which are being carried on a vessel at the time of the salvage services may not be owned by the owner of that vessel or, in the case of cargo-carrying containers, by the owners of that cargo. The nature

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<sup>7</sup> For more detailed commentary on maritime liens see Chapter 24.4 (Security Enforcement Measures).

<sup>8</sup> See Chapter 14.5 below.

<sup>9</sup> Copies can be accessed at the website of the International Salvage Union: [www.marine-salvage.com](http://www.marine-salvage.com).



of multimodal transport is such that containers owned by one multimodal operator are often carried on vessels owned by another multimodal operator pursuant to complex slot charters or space-sharing arrangements. Therefore, such containers will often be at the risk of a multimodal operator other than the owner of the salvaged ship and that proportion of the salvage award which is payable in respect of the value of the containers saved will be borne by such multimodal operator and its insurers.<sup>10</sup>

That proportion of the salvage award which is payable in respect of the value of the freight at risk will be borne either by the shipowners and their insurers or by the cargo owners and their insurers depending on whether it is payable on completion of the voyage or after loading. If freight is payable on completion of the voyage it will be at the risk of the shipowners and their insurers whereas, if it is payable in advance after loading and non-returnable (ship and/or cargo lost or not lost), it will be at the risk of the cargo owners and their insurers. In the latter event, the value of the freight will be included in the value of the cargo and freight will not contribute separately.

### 14.3 Special Compensation (Environmental Salvage)<sup>11</sup>

Article 8 of the International Convention on Salvage 1989 obliges a salvor when performing salvage services to “*exercise due care to prevent or minimise damage to the environment.*” The salvor may incur substantial expenditure in doing so and runs the risk that if salvage efforts are unsuccessful, he may receive no compensation for such expenditure. In order to protect the salvor in such circumstances Article 14 of the International Convention on Salvage 1989 provides that a salvor who has prevented or minimised damage to the environment may be paid special compensation.

The provisions of Article 14 are normally incorporated into LOF contracts and state that if efforts to salvage property which poses a threat to the environment are unsuccessful or only partially successful, the salvor is, nevertheless, entitled to receive his reasonable expenses from the owner of the vessel and an increment of 30 per cent (rising in exceptional circumstances to 100 per cent) of such expenses, but only if, and to the extent that, such expenses, together with the increment, are greater than any amount otherwise recoverable under the traditional ‘no cure-no pay’ basis.

Because of the various technical difficulties which are inherent in assessing remuneration under Article 14 of the convention, it has become more common for claims to be assessed under the Special Compensation P&I Clause (SCOPIC) which

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<sup>10</sup> For more detailed commentary on multimodal carriage see Chapter 3.2.9.6 (Cargo Claims).

<sup>11</sup> For more detailed commentary see Chapter 11.6.3.2 of the *Gard Handbook on Protection of the Environment*, 3rd edition, Chapter 10.3.3 of the *Gard Handbook on P&I Insurance*, 5th edition.

is included as an option in LOF salvage contracts.<sup>12</sup> Salvors will normally wish to claim traditional salvage remuneration on a 'no cure-no pay' basis but are given the option to invoke the SCOPIC clause should they consider that the measures that are necessary to protect the environment will not be adequately remunerated under the 'no cure-no pay' principle. Should the salvor invoke the SCOPIC clause then:

- Salvage services shall continue to be assessed on a 'no cure-no pay' basis but SCOPIC remuneration shall also commence to be assessed as from the time that SCOPIC was invoked;
- The shipowners shall, within two working days, provide security for SCOPIC remuneration in the form of a bank guarantee or a P&I letter of undertaking in a form reasonably satisfactory to the salvor;
- The SCOPIC remuneration shall be assessed on the basis of the tariff rates set out in the SCOPIC clause enhanced by a standard bonus of 25 per cent which may be increased in special circumstances;
- The SCOPIC remuneration will be payable (if at all) solely by the shipowners and their insurers;
- SCOPIC remuneration is payable only if it exceeds the salvage award that is payable on a 'no cure-no pay' basis by all salvaged interests including cargo, bunkers etc.

The SCOPIC scheme is supported by a non-binding Code of Practice between the International Salvage Union (ISU) and the International Group of P&I Clubs (IG) relating to the provision of SCOPIC security and by another similar non-binding Code of Practice between the ISU and the International Group and property insurers regulating the payment of costs incurred by a Special Casualty Representative (SCR) who is appointed by representatives of the International Group, the ISU, the International Union of Marine Insurance (IUMI) and the International Chamber of Shipping (ICS) (collectively known as the SCOPIC Committee) and has the responsibility to use his best endeavours to liaise with the salvor in order to minimise damage to the environment and to achieve a proper delineation between 'no cure-no pay' services and SCOPIC services. The salvage master remains in overall charge of the operation. However, the SCR is to be kept informed by, and to consult with, the salvage master on a daily basis throughout the salvage and is obliged to communicate any difference of opinion to the salvage master and the other interested parties. On completion of the salvage services the SCR must issue a final salvage report commenting on:

- The facts and circumstances of the casualty and the salvage operation insofar as they are known to him;
- The tugs, personnel and equipment employed by the salvor; and
- A calculation of the SCOPIC remuneration to which the salvor may be entitled.

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<sup>12</sup> Copies of the relevant SCOPIC documents and associated guarantee can be accessed at the website of the International Salvage Union: [marine-salvage.com](http://marine-salvage.com).

Whilst these provisions encourage salvors to take measures that are necessary to protect the environment, they face a potential penalty if SCOPIC is invoked in inappropriate circumstances. If it is assessed in due course that the traditional 'no cure-no pay' salvage award is greater than the SCOPIC remuneration, the 'no cure-no pay' award will be discounted by 25 per cent of the difference between the 'no cure-no pay' award and the amount of SCOPIC remuneration that would have been assessed had the SCOPIC remuneration provisions been invoked on the first day of the salvage services.<sup>13</sup>

#### 14.4 General Average<sup>14</sup>

The event which gives rise to salvage may also cause the various interests at risk to incur other expenditure, e.g. the cost of jettisoned cargo or containers or post-salvage cargo storage costs, and therefore, these expenditures and the salvage payments made by the various interests have historically been allowed in general average and re-adjusted between the various parties pursuant to the York-Antwerp Rules (YAR) 1974 and 1994. However, under the York-Antwerp Rules 2004 (YAR 2004), salvage payments made by the various interests at risk are to lie where they fall and are not to be re-adjusted in general average, unless one party to the salvage has paid all or any of the proportion of salvage due from another party. The York-Antwerp Rules are not mandatory and only apply on a contractual basis. Therefore, it is important to ascertain whether general average is to be adjusted in accordance with YAR 1974, YAR 1994 or YAR 2004.

Special Compensation payments for environmental salvage, whether under SCOPIC or Article 14 of the 1989 Salvage Convention, are not adjusted in general average since such payments are purely the responsibility of shipowners and their insurers.

#### 14.5 Insurances

##### 14.5.1 Cargo Insurers<sup>15</sup>

Cargo's proportion of any salvage award is normally covered by standard cargo policies such as the ICC clauses and cargo insurers are normally prepared to put up security for such claims when demanded by salvors. If the event which has necessitated the salvage services can be attributed to a breach by the shipowners of the contract of carriage, cargo insurers will normally have to pay cargo's proportion of the award to salvors but may then wish to use their rights in subrogation to claim

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<sup>13</sup> See Chapter 14.9 below (Case Study.)

<sup>14</sup> For more detailed commentary see Chapter 10 (General Average Claims) and *A guide to General Average* by Richard Cornah which can be accessed at the website of Richards Hogg Lindley Ltd: [www.rhlg.com/pdfs/GAGuide.pdf](http://www.rhlg.com/pdfs/GAGuide.pdf).

<sup>15</sup> See Chapter 26.3.3 (The Structure of Marine Insurance).

an indemnity from the shipowners in the form of a cargo claim.<sup>16</sup> If such claims are successful, the shipowners' liability to provide indemnification is normally covered by P&I insurers.<sup>17</sup>

### 14.5.2 Hull and Machinery Insurers<sup>18</sup>

Ship's proportion of any salvage award is normally covered by standard hull and machinery policies and hull and machinery insurers are normally prepared to put up security for such claims when demanded by salvors. If the event which has necessitated the salvage services can be attributed to the negligence of cargo owners (e.g. as a result of the shipment of dangerous goods<sup>19</sup> or the sending of the vessel to an unsafe port<sup>20</sup>), hull and machinery insurers will normally have to pay ship's proportion of the award to salvors and the ship's proportion of General Average but may well wish to use their rights in subrogation to claim an indemnity from the cargo interests. If such claims are successful, the cargo owners' liability to provide indemnification is not covered by cargo insurers but may possibly be covered by charterers' liability insurers.

### 14.5.3 P&I Insurers<sup>21</sup>

P&I insurers will normally provide cover for the following claims:

- Special compensation for environmental salvage claims under LOF and/or SCOPIC;
- Salvage charges which the shipowners have been compelled to pay despite the fact that they should have been paid by cargo interests and which are not recoverable from cargo interests because of the shipowner's breach of the contract of carriage;
- The shipowner's liability to reimburse cargo interests for their proportion of any salvage award which has been caused by the shipowners' breach of the contract of carriage;
- The shipowner's liability to pay that proportion of the ship's contribution to salvage which is not recoverable from Hull and Machinery insurers because the valuation of the ship for the purposes of the salvage award is deemed to be higher than the sum insured under the Hull and Machinery policy;
- Life salvage to the extent that this is legally payable by the shipowners and not recoverable under any other policy.

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16 For more detailed commentary on subrogation see Chapter 25.5 (The Fundamental Principles of Marine Insurance).

17 See Chapter 14.5.3 below.

18 See Chapter 26.3.1.1 (The Structure of Marine Insurance).

19 For more detailed commentary see Chapter 7 (Dangerous Goods Claims).

20 For more detailed commentary see Chapter 13 (Safe Ports Claims).

21 For more detailed commentary see Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guide to Rule 42 (Salvage)).

#### 14.5.4 Marine Container Insurers

There are various specialist insurers who provide cover for the liability of container owners to pay salvage remuneration pursuant to standard clauses such as the Institute Containers Clauses-Time 1/1/87 or the Institute Container Clauses – Time Total Loss, General Average, Salvage, Salvage Charges, Sue and Labour 1/1/87.

#### 14.6 Salvor Negligence<sup>22</sup>

Salvors are expected to perform their services with reasonable skill and care depending on the particular circumstances of the case. Therefore, salvors may be liable for any negligence on their part whilst performing salvage services.<sup>23</sup> The salvage award or special compensation payment may be reduced to reflect the degree of damage caused by such negligence and should the degree of damage exceed the sum which would otherwise be awarded to the salvor, the salvor will be liable to the shipowner for the difference.

In the event that large claims are made against them, salvors are entitled to limit their liability under the 1976 Limitation Convention but not under the preceding 1957 Limitation Convention which is still in force in some parts of the world. The relevant limit under the 1976 Convention depends on whether the salvor is or is not conducting salvage services from a salvage vessel. If the salvor is conducting services from a salvage vessel then the limit will depend on the tonnage of that ship. However, if the salvor is either not operating from a vessel or is operating solely on the ship which he is trying to save, then the salvor is deemed to have a limitation tonnage of 1,500 tonnes. The right to limit only applies to claims *against* the salvor. Therefore, salvaged interests cannot claim the benefit of limitation to reduce a claim for salvage reward brought by a salvor.<sup>24</sup>

#### 14.7 Coastal State Intervention

Article 9 of the International Convention on Salvage 1989 maintains the right of coastal states to intervene in salvage operations pursuant to rights given under other international conventions such as the United Nations Convention on the Law of the Sea (UNCLOS), the Intervention Convention 1969<sup>25</sup> or other regional agreements, and give directions in order to protect its coastline from the threat of

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22 For more detailed commentary see Chapter 10.1 of the *Gard Handbook on P&I Insurance*, 5th edition and Chapter 7 of *Brice: The Maritime Law of Salvage* by Reeder, 5th edition, 2012.

23 For more detailed commentary generally on negligence see Chapter 14 of the *Gard Handbook on P&I Insurance*, 5th edition.

24 See also Chapter 21.3.3.2 (Limitation of Liability), Chapters 28.6.2 of the *Gard Handbook on P&I Insurance*, 5th edition and page 12 of *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, Informa, 4th edition, 2005.

25 See Chapter 22.3.2 (Maritime Regulation and Compliance).

pollution. Therefore, coastal states can be expected to exercise such rights and may sometimes do so merely to remove the problem from their coastline to a neighbouring coastline.

Traditionally, coastal states have been encouraged to provide safe havens for ships that are in distress but the increasing risk of pollution has resulted in unfortunate cases in which ships have been refused entry which has consequently, made the prospect of a successful salvage that much more difficult. Industry concern has resulted in the IMO adopting *the Guidelines on Places of Refuge*<sup>26</sup> which sets out the following balanced test:

*“When permission to access a place of refuge is requested, there is no obligation for the coastal state to grant it, but the coastal state should weigh all the factors and risks in a balanced manner and give shelter whenever reasonably possible.”*

These Guidelines do not have the force of law. However, each member state of the European Union is obliged to designate appropriate ports of refuge in its territory,<sup>27</sup> whilst in the United Kingdom, the Secretary of State’s Representative (SOSREP) has wide powers to oversee, control and direct salvage operations within UK waters in appropriate places and in an appropriate manner.<sup>28</sup>

In the United States, the US Coastguard has the responsibility under the Ports and Waterways Safety Act (33 USC 1221 *et seq.*) and other federal statutes to decide whether to allow a damaged vessel to enter a port area in response to a Place of Refuge request. In deciding this issue the Coast Guard must comply with detailed guidelines which require the Coast Guard to consider a number of factors such as weather and environmental conditions, salvage equipment and personnel availability, security, and physical attributes of the port.<sup>29</sup>

## 14.8 Claims Management

Salvage incidents require quick decisions and a cool head since major decisions need to be taken with the minimum of delay at a time when the ship and its crew and cargo may be in danger. Owners’ leading Hull and Machinery insurers will normally wish to be involved in such discussions and decisions and may wish to conduct negotiations with the salvors themselves. The decisions that are taken will also affect a number

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26 Further details can be accessed via the IMO website at: <http://www.imo.org/ourwork/safety/navigation/pages/placesofrefuge.aspx>.

27 See Directive 2002/59/EC of the European Parliament and Council.

28 Further details can be accessed via the website of the UK Department for Trade at: <http://www.dft.gov.uk/mca/lrgtxt/sosrep.pdf>.

29 The USCG Commandant Instruction 16541.9 dated 17 July 2007 in response to the IMO’s Guidelines on Places of Refuge for Ships in Need of Assistance, IMO Assembly Resolution A.949(23), adopted 5 December 2003.

of different interests and their insurers and require the co-operation of people and authorities. Experience shows that difficult incidents such as these are best managed if the relevant personnel have received adequate training beforehand and therefore, know what needs to be done without unnecessary delay if and when a real incident occurs. The need for such pre-planning and training cannot be over-stressed.

Steps should also be taken to ensure that the ship's crew is instructed to follow the guidance recommended in Chapter 3.9.3 of the *Gard Guidance to Masters*.

## 14.9 Case Study

### Casualty

Ship A, a fully laden container vessel of 9,567 gt, suffered a main engine breakdown in the Atlantic Ocean, approximately 50 nautical miles SW of Madeira. Weather conditions at the time were favourable but the attempts that were made by the crew to rectify the problem were unsuccessful and the vessel drifted slowly towards Madeira. Therefore, the master of the vessel immediately alerted the shipowners.

### Salvage Negotiations

The vessel was insured on ITCH 83 terms with H&M insurers principally in the London market and was entered with a P&I club that is a member of the International Group. The shipowners immediately notified the lead H&M underwriter who quickly investigated which salvage companies had resources in the area. The H&M insurers then confirmed that they were ready to conclude a contract on daily hire terms with salvage company X that had tugs and equipment available some two days steaming time away from the reported position of the ship A. However, the shipowners notified the H&M insurers that they had already concluded a contract with another salvage company, Y, on Lloyd's Open Form (LOF) terms which incorporated the SCOPIC clause. Salvor Y did not in fact have tugs in the vicinity of the drifting vessel, but had subcontracted the work to another salvage company that, reportedly, did have available crew and tugs. However, in reality, the nearest available tug needed four days of steaming time to reach the reported position of ship A.

### SCOPIC

One day after the tug sub-contracted by Y commenced its voyage to ship A, the weather deteriorated. Ship A continued to drift towards Madeira and it was estimated that she would run aground in approximately 30 hours if help did not arrive. Since salvor Y did not wish to take the risk that ship A would run aground and become a total loss before the sub-contracted tug could arrive, it immediately invoked the SCOPIC Clause. By this time, salvage company X's tug was approximately 30 hours steaming time away from ship A and had the best chance of reaching ship A before she was expected to run aground. Therefore, salvor Y

concluded a sub-contract with salvage company X to enable it to use the services of X's tug to prevent the grounding of ship A prior to the arrival of the tug that had been previously sub-contracted by Y.

As the weather conditions continued to worsen, ship A continued to drift towards the island and on day three, shortly before the arrival of salvage company X's tug, she grounded on a shore consisting of sand and rocks. Cracks were discovered in several of the ballast tanks, but the bunker tanks remained intact and no fuel was lost. The local authorities initially instructed salvor Y to remove the bunkers before attempting to refloat the vessel, but Y was able to persuade them that there was minimal risk of damage to the bunker tanks and that removing the bunkers would delay the refloating plan. After 18 days, salvor Y finally managed to refloat the vessel with the bunkers still inside and towed it to a nearby yard for repairs.

### Salvage award

Since salvor Y had successfully salvaged ship A and her cargo a Lloyd's Arbitration Panel subsequently awarded Y the sum of USD 4,150,000 pursuant to Article 13 of the Salvage Convention based on an estimated salvaged value of all the property at risk (i.e. ship, cargo, bunkers and containers) of USD 42 million. However, since the Article 13 award was higher than the total SCOPIC costs which were assessed at USD 3,320,000, a deduction was made from the Article 13 award of 25 per cent of the difference between the awards in accordance with the provisions of the LOF contract.<sup>30</sup> Consequently, the property insurers were obliged to indemnify the owners of ship A for a salvage award totaling USD 3,942,500, the majority of which was payable by cargo insurers based on cargo's proportion of the total value at risk. Furthermore, salvor Y received USD 207,500 less than they would have done had they not invoked SCOPIC.

It is also important in circumstances such as this that, where time permits, all interested parties should liaise before taking important decisions such as appointing salvors. The decision of the shipowners to engage salvors on LOF terms independently before securing the agreement of their insurers could in some instances have had serious results and/or resulted in a much higher Article 13 or SCOPIC award, as well as causing operational difficulties.

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<sup>30</sup> See Chapter 14.3 above



## Chapter 15

# Towage Claims<sup>1</sup>

### 15.1 Introduction

Ships may need towage assistance in various circumstances. However, the most common circumstances are the following:

- i Deep sea towage: Ships are often towed long distances to repair yards and large structures such as floating docks, power plants and oil rigs are often towed from one part of the world to the other. Such services are provided by large ocean-going tugs which are capable of spending long periods at sea, with a significant fuel range and a very large towing power. These vessels are also sometimes used in providing salvage services and are often stationed near important navigational routes. A number of these vessels provide multi-purpose services such as towage, salvage, oil-rig supply and services.
- ii Coastal and river towage: The tugs that are involved in this activity are generally smaller versions of ocean-going tugs and are primarily used to tow or push barges loaded with cargo and other materials along coastlines, major navigable rivers, and across short ocean passages. Such tugs are occasionally also used in order to provide salvage services.
- iii Harbour towage: Ships will often require tug assistance in berthing, docking or undocking in confined port areas and, in many instances, such assistance will be mandatory as a condition of port entry. This operation may require the use of more than one tug but may not involve actual attachment to the towed vessel since in many cases, pushing will be sufficient. The tugs that are involved in this form of activity are often highly manoeuvrable, with very sophisticated steering and/or propulsion systems.

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<sup>1</sup> For more detailed commentary see Chapter 13 of the *Gard Handbook on P&I Insurance*, 5th edition and *The Law of Tug and Tow and Offshore Contracts* by Simon Rainey QC, Informa, 3rd edition, 2011.

Towage is normally provided by specialist towage companies pursuant to a formal towage contract that has been negotiated well in advance between shipowners and towing companies. In some instances (particularly in the case of coastal, river or harbour towage) such contracts are period contracts which relate to the provision of towage as and when needed at particular locations within a specified period. However, even if no formal agreement is negotiated, completed or signed, a towage contract may be deemed to exist by implication especially where the shipowner or the master has consistently accepted such terms on previous and similar occasions. Furthermore, should the need for towage arise at short notice, the master of a vessel has implied authority to engage towage services that are reasonably necessary for the safe and proper performance of the voyage.

### 15.1.1 The Distinction between Towage and Salvage<sup>2</sup>

However, an important distinction should be drawn between a towage contract and a salvage contract. A towage contract was described as long ago as 1848 as:

*“... the employment of one vessel to expedite the voyage of another when nothing more is required than the accelerating of her progress.”*

Therefore, a towage contract is normally negotiated at a time when the ship that is to be towed is not facing imminent peril and remuneration is negotiated and agreed in advance, usually on a fixed fee basis. However, a salvage contract (normally a standard form of salvage contract such as the Lloyd’s Open Form of Salvage Agreement (LOF)) is agreed when the ship that is to be assisted is facing imminent peril and remuneration is assessed after the completion of the salvage services by a specialist system of arbitration based on a number of factors including the degree of danger to the salvaged property, the value of the property at risk, the degree of skill demonstrated by the salvor and the cost to the salvor of performing the services. Furthermore, the remuneration that is normally payable under a towage contract is payable regardless of the success of the operation whereas a salvage contract is based on the principle of ‘no cure-no pay’ which means that the salvor is rewarded only if he succeeds in saving the ship and/or cargo and receives no reward if he fails to do so. Therefore, since the public policy of most countries is to encourage salvage for the common good, a salvage claim normally qualifies as a maritime lien whereas a claim under a towage contract does not do so.<sup>3</sup>

However, the demarcation between towage and salvage may become blurred. For example, a ship which may be proceeding perfectly normally without tug assistance may suffer a problem such as an engine breakdown which does not

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2 For further commentary on salvage see Chapter 14 (Salvage Claims).

3 For more detailed commentary see Chapter 24.4 (Security Enforcement Measures).

place the ship in imminent peril but which nevertheless, requires the attendance of a tug to tow the vessel to a port where she can be repaired. Disputes can then arise as to whether the services provided by the tug should be considered to be salvage and remunerable on the usual 'no cure no pay' basis, or towage services for which remuneration should be in the form of a lump sum. Therefore, it is important whenever time allows that the owners of the ship which requires assistance should involve those other parties who may have to contribute to such remuneration in due course (e.g. his hull and machinery and P&I insurers, and cargo insurers) in such discussions to avoid future disagreements between the interested parties.

Alternatively, if it is known that the ship will need tug assistance to perform a voyage and the shipowners enter into a towage contract in advance for that purpose they will normally envisage that the tow may encounter some difficulties en route and conclude terms that will govern their relationship in circumstances which are reasonably foreseeable and anticipated. In particular, the tug will normally be obliged to use its best endeavours to protect the tow in such circumstances. Therefore, if an event that was anticipated occurs during the towage and the tug is obliged to take steps to preserve the safety of the tow such services will normally be considered to be an integral part of the towage contract and the tug is not entitled to any additional remuneration. However, if the safety of the tow is imperiled by an event or danger that was not within the reasonable contemplation of the parties, such services may be considered to be salvage services, notwithstanding the existence of the towage contract, and the tug may be entitled to claim additional salvage remuneration if it succeeds in saving the towed ship.

Article 17 of the Salvage Convention states that a salvage reward is payable only where "... the services rendered exceed what can be reasonably considered as due performance of a contract entered into before the danger arose." Therefore, to convert a towage contract into a salvage it has been held that the tug must prove (a) that the services that it performed were of such an extraordinary nature that they could not have been within the reasonable contemplation of the parties to the original towage contract, and that (b) the services that had in fact been performed and the risks in fact run would not have been reasonably remunerated by the contractual remuneration that had been agreed in the towage contract.<sup>4</sup>

Each case will depend on its particular facts. However, it is possible for a towage contract to expressly exclude the right to salvage if a clause to that effect is included in the towage contract.

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<sup>4</sup> *The Homewood*, [1928] 31 Lloyd's Rep. 336. For the facts of the case see Chapter 15.6 (Case Study 1) below.

## 15.2 Towing Vessels

Although a towing vessel need not necessarily be a purpose-built vessel such services will normally be provided by specialist vessels called tugs. Whereas most ships are powered solely for their own propulsion, a tug is a vessel that is built specifically to provide auxiliary propulsion for another vessel and the efficiency of a tug is measured by the percentage of power that the tug can transmit through a tow-rope or other attachment to the towed vessel, i.e. the tug's bollard pull.

Whilst there is nothing in principle to prevent a non-tug from providing towage services it is unlikely that such services will normally be provided unless towage is urgently required and the non-tug is the only available option. In most circumstances, such services will be provided as salvage services since the vessel that is to be towed will be in peril. Therefore, the right of the non-tug to provide towage will normally be justified for public policy reasons by the law of most countries and by international conventions such as the SOLAS Convention and Article IV Rule 4 of the Hague and Hague-Visby Rules even if the non-tug is engaged on another cargo carrying voyage at the time. However, it is extremely unlikely that a non-tug will be justified in interrupting such service in order to tow a vessel which is not facing the sort of peril that would justify salvage. Such action might well be deemed to constitute a deviation<sup>5</sup> and the owner of the non-tug may well prejudice its insurance cover.<sup>6</sup>

## 15.3 Liability

Liability may arise either in tort or in contract depending on whether claims arise between:

- the tug/tow combination and third parties; and
- the tug and tow *inter se*.

### 15.3.1 Liability Between the Tug/Tow Combination and Third Parties

When damage is caused to third parties with whom the tug/tow has no contractual relationship the question arises whether liability in tort<sup>7</sup> is to be borne by the tug or by the tow or by both. The issue can have substantial financial impact since tugs tend to be smaller than the towed vessel and, consequently, have smaller limitation funds.<sup>8</sup> Normally, the issue is decided on negligence principles and it is a question of fact in each case whether the damage can be attributed to the negligence of the tug or the tow or both. The tug owners are not expected to perform the towage satisfactorily in all circumstances and despite all hazards. However, the

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<sup>5</sup> See also Chapter 4.4.3.2.2 (Charterparty claims).

<sup>6</sup> See Chapter 15.4 below.

<sup>7</sup> For further commentary on tort and negligence see Chapter 14 of the *Gard Handbook on P&I Insurance*, 5th edition.

<sup>8</sup> For more detailed commentary see Chapter 21.3 (Limitation of liability).

tug is normally obliged to use reasonable care and skill in its service, and since physical control of the operation is normally presumed to lie with the tug, the latter is normally the party liable unless there is evidence of independent fault by the tow that has contributed to the accident. In the majority of cases tugs have been held to be negligent on the basis that:

- The tug was unseaworthy or unfit to perform the service; or
- The towline was of an improper length; or
- The tug master was unprepared for, or ignorant of, the conditions to be encountered; or
- The tug master did not plan or perform the service with sufficient care.

However, the tow may be held to be negligent if:

- It is not equipped with the necessary anchors, lights, lines, steering equipment etc.; or
- It is not in a fit structural state of repair to withstand the intended towage: or
- Its crew is not properly trained for the planned towage; or
- It does not follow the tug's instructions.

### 15.3.2 Liability between the Tug and Tow *inter se*

It has not proved possible to conclude any international conventions regulating the liabilities of parties to towage agreements since the law of many countries enforces the principle of freedom of contract which allows parties to include clauses in contracts to exclude liability that would otherwise be imposed on one of the parties to the contract. Consequently, such clauses have traditionally been found in most towage contracts and have the effect of allowing tug owners to mitigate, or even escape from, liabilities incurred during the towage service. The precise extent of such exclusion depends on the particular form of towage contract that has been agreed.

### 15.3.3 National Terms

Most national towing conditions have three main elements:

- The master and crew of the tug are deemed to be the servants of the tow and are to be under the control of the tow;
- The tug owner is exempted from liability for loss or damage however caused, including negligence;
- The tow owner is to indemnify the tug owner against and in respect of any claims for loss or damage made against it by third parties.

The most commonly used national terms are the United Kingdom Standard Conditions for Towage and other Services (The UKSTC revised 1986) which are used both in the UK and in many other countries. These terms provide the widest form of protection for the tug. Unless a loss, damage or liability arises as a result

of “the personal failure of the person or person having the ultimate control and chief management of the Tugowner’s business to exercise reasonable care to make the tug or tender seaworthy for navigation at the commencement of the towing or other service,” the tug is not liable for, and will be indemnified by the tow against, any damage arising out of the towage service either to the tow or to the tug or to any other third party property “even if the same arises from or is caused by the negligence of the tug-owner his servants or agents.” However, liability for personal injury or death caused by the negligence of any of the tug’s officers or employees is not excluded.

Under the common law towage was considered to commence when the towline was passed to the tug or *vice versa* and the responsibilities of the parties under the contract attached at that moment. However, under the UKSTC, towage is deemed to commence earlier when the tug is in a position to receive orders directly from the tow “to commence holding, pushing, pulling, moving, escorting, guiding or standing by”.

The same appears to be the case under the Scandinavian conditions which apply when damage is caused “in connection with” the services. Therefore, such conditions may give protection in the event, for example, that a collision occurs between the tug and tow when the tug is manoeuvring in close proximity to the tow in order to pass the tow line.

However, the Australian court has held that the wide protection that is given to the tug under the UKSTC is rendered void in relation to harbour towage by the Australian Trade Practices Act 1974 since such a towage contract is not a contract for, or in relation to, the transportation of goods. Consequently, it has been suggested that tug owners should consider including a clause such as the following in towage contracts that incorporate the UKSTC and which apply Australian law:

*“The Tugowner shall be subject to any implied condition or warranty provided by the Trade Practices Act 1974 (Cth) (the Act) if and to the extent that the Act applies, in which circumstances the Tugowner limits its liability for breach of such implied condition or warranty to supplying the service again or the payment of the cost of having the service supplied again, as determined by the Tugowner.”*

The Japanese Nippontow conditions, the Shipping Federation of Canada Standard Towing Conditions, the Scandinavian Tugowners Standard Conditions (as revised in 1985) and the Netherlands Standard Towage Conditions 1951 all follow the United Kingdom model, although the wording in these various contracts may differ and there are also some substantive differences. The Japanese and Canadian terms apply the same wide exemption for tug liability for almost all damage, including that

due to unseaworthiness and negligence and require the tow owner to indemnify the tug owner against any claims that may be brought by third parties. However, under the Netherlands conditions, the towed vessel is not liable for damage to the tug caused by the fault of the tug or for damages to third party property resulting from collision with the tug which was not caused by, or was only partially caused by, the towed vessel.

Towage in Scandinavia has traditionally been performed subject to the Scandinavian Tugowners Standard Conditions 1959 as amended in 1974 and 1985 which exempt the tug owner from liability for damage caused to the tow unless the damage has been caused by the fault or neglect of the tug owner's manager acting in that capacity. Therefore, the tug owner is not liable if the damage has been caused by the fault or negligence of the crew or by a member of the tug owner's management when acting in their capacity as master of the tug or as a member of its crew. In any event, the liability of the tug owner is limited to NOK 100,000 (SEK 100,000 under the Swedish version of the conditions and DEK 100,000 under the Danish version) unless the loss or damage has been caused by the wilful intent or gross negligence of the tug owner. Furthermore, the tow owner is required to indemnify the tug owner for any damage caused to the tug owner in connection with the services, unless the tow owner proves that the damage was not caused, either partly or wholly, by the fault or neglect of the tow owner or of someone for whom the tow owner is responsible, such as the master of the tow or a member of its crew. The tow owner is also required to indemnify the tug owner for any liability that the tug owner may incur to third parties in connection with the services, unless it is proved that the tug owner would have been liable to the tow owner if the damage had in fact been suffered by the tow owner.

### **15.3.3.1 Towage in the USA**

There are significant differences between the rules that apply under the national forms of towage contracts described above and those that apply in the United States. Under US law the towing vessel is not permitted to rely on any term that attempts to exclude liability for negligence unless the owner of the tow is the US government. Consequently, where the towage is to be performed within US territorial waters, most towage contracts give protection to the tug in another way. The towage contract normally provides that the tow (and its cargo) must obtain insurance in order to protect the tug against liability. Such insurance is normally an integral part of the insurance that is taken by the tow and names the towing vessel as an additional vessel and includes a waiver of subrogation on the part of the insurers, i.e. the insurers waive their rights to bring claims against the towing vessel if the loss or damage can be attributed to default on the part of the towing vessel. If the owner of the towed vessel fails to obtain the insurance that is required under the towage contract, he will have to bear the loss that would otherwise have been

covered by such a policy, and will be unable to recover any shortfall from the owner of the towing vessel. However, such a provision will only protect the towing vessel against liability that is covered by whatever insurance that is required under the towage contract. Therefore, the towing vessel may still be liable for loss or damage negligently caused by it that falls within any deductible or that is otherwise not covered under the policy.

However, where the service is considered to be fully international, and the towage terms are agreed at arm's length and not imposed by the towing vessel, US courts may be prepared to accept foreign towage conditions.

#### **15.3.3.2 International Terms**

The TOWCON and TOWHIRE contracts were introduced by BIMCO in 1985 and updated in 2008.<sup>9</sup> These contracts are now used more widely than the UKSTC or any other national towage contracts and are rarely amended in day to day usage. The TOWCON contract provides that the towing vessel is to be reimbursed on a lump sum basis (as in the case of a voyage charter) for the towage services whereas, under the TOWHIRE contract, the tug is paid on a daily hire basis (as in the case of a time charter). However, whereas the national terms described in Chapter 15.3.3 above place all or most of the risks of the towage service on the tow, the risk under TOWCON and TOWHIRE contracts is allocated on a knock-for-knock basis between the tow and tug so that each party, irrespective of blame and without the right of recourse against the other contracting party, bears any loss or damage that is incurred by its own property, including the death or personal injury of its own servants or agents, and responsibility for any other claims that may be brought against it by third parties.

### **15.4 Insurance**

In general, the risks and liabilities associated with towage operations (regardless of whether the entered vessel is the tow or the towing vessel) are far greater than those associated with normal shipping operations. Towage involves, by necessity, two vessels operating in close proximity. As a result, there is a greater danger of collision and other related accidents.

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<sup>9</sup> Copies of these contracts can be accessed at the website of the International Salvage Union: [www.marine-salvage.com](http://www.marine-salvage.com).



### 15.4.1 Hull and Machinery Insurance<sup>10</sup>

The terms of most standard hull and machinery policies recognise the increased risk and place restrictions on the cover that is normally available. In general terms, risks that are imposed by towage operations but which would not ordinarily be faced by a ship when engaged in the ordinary course of trading are excluded whether the insured ship is the towing ship or the towed ship. For example, Clause 1 of the Institute Time Clauses Hulls (1/11/95) provides that:

*"1.1 The Vessel is covered subject to the provisions of this insurance at all times and has leave to sail or navigate with or without pilots, to go trial trips and to assist and tow vessels or craft in distress, but it is warranted that the Vessel shall not be towed, except as is customary or to the first safe port or place when in need of assistance, or undertake towage or salvage services under a contract previously arranged by the Assured and/or Owners and/or Managers and/or Charterers. This Clause 1.1. shall not exclude customary towage in connection with loading and discharging.*

*1.2 This insurance shall not be prejudiced by reason of the Assured entering into a contract ... for customary towage which limits or exempts the liability of ... tugs and/or towboats and/or their owners when the Assured or their agents accept or are compelled to accept such contracts in accordance with established local law or practice."*

In such circumstances, Clause 3 provides as follows:

*"Held covered in case of any breach of warranty as to ..., towage, ... provided notice be given to the Underwriters immediately after receipt of advices and any amended terms of cover and any additional premium required by them be agreed."*

Similar provisions can also be found in The Institute Time Clauses Hulls 1/10/83 and 1/11/03. However, shipowners often approach their H&M insurers to request cover for any particular non-customary towage that is envisaged and insurers may agree to cover such risk on such amended terms and/or premium that they deem appropriate.

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<sup>10</sup> For more detailed commentary see Chapter 26.3.1.1 (The Structure of Marine Insurance).

### 15.4.2 P&I Insurance<sup>11</sup>

P&I cover also reflects the additional risks and dangers that may be encountered in towage operations. However, cover is normally available for liabilities, costs and expenses arising from towage operations provided firstly, that the particular liabilities, costs and expenses are within the standard heads of cover that are generally available to other members and provided secondly, that certain conditions are satisfied.

Cover is normally available whether the entered ship is the towing ship or the towed ship but a distinction is normally drawn between the cover that is available for:

- A ship that is being towed; and
- A ship that is towing.

#### 15.4.2.1 A Ship that is Being Towed

Such a vessel will normally not be covered unless:

- The towage contract is entered into for the purpose of entering or leaving port, or manoeuvring within a port in the normal course of trading; or
- The towage contract is for the towage of such ships from place to place in accordance with the custom of that trade; or
- The towage contract has been approved by the P&I club.

The risks involved in towage into, within and out of a port, or in accordance with the custom of the trade are mutual risks which are borne by the majority of P&I club members and therefore, towage contracts entered into for such purposes do not normally require formal approval by the P&I club. However, where the towage contract is concluded for other reasons (e.g. for the deep sea towage of a vessel to a repair yard) the risks that are being assumed are greater than those that are normally borne by the majority of club members and therefore, require formal approval by the P&I club. In such circumstances, the TOWCON or TOWHIRE contracts are more likely to be approved than the UK, Netherlands, Scandinavian or similar standard towing conditions for the reasons explained in Chapter 15.3.3 above. Furthermore, if the towed vessel is carrying cargo, the carrier may also be required to ensure that the relevant contract of affreightment contains a clause such as a Himalaya clause in order to prevent the cargo owner from bringing a claim in tort against the tug owner who might then be able to seek an indemnity from the member under the towage contract.

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<sup>11</sup> For further commentary see Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 43 (Towage)).

#### 15.4.2.2 A Ship that is Towing

Towage requires specialist skills and often requires specialised equipment. A ship which is not a fully fitted tug is unlikely to have either the equipment or the crew which will be necessary to conduct safe towage operations and errors of judgment or failures of equipment can lead to the loss of the tow and her cargo and expose the member to large claims, not only from their owners, but also from the authorities which may require the removal of the wreckage.<sup>12</sup> Such liabilities are not normally considered to be liabilities which should be shared by the P&I membership as a whole in the context of mutuality. Consequently, cover is not usually available for liability, costs and expenses incurred as a result of the loss of or damage to the tow unless:

- The towage is carried out for the purpose of saving life at sea; or
- The entered vessel is a tug or a vessel that normally engages in towage operations and has been insured in that capacity on approved terms; or
- The terms of cover have been specifically agreed prior to the commencement of the towage.

### 15.5 Claims Management

Long-distance towage is a highly technical operation and should not be entered into lightly. It is normally good policy to engage the services of an experienced marine surveyor specialising in towage operations to carry out a detailed 'Tug, Tow & Towage' survey prior to commencement of the towage and to issue a 'towage approval certificate' when satisfied with all aspects. Such a surveyor could then be asked to subsequently monitor and report on the progress of the tow

Secondly, parties are strongly urged to consult their P&I insurers prior to concluding towage contracts (even coastal or harbour towage contracts) to ensure that the terms of such contracts do not impose unusually onerous terms which might thereby prejudice their insurance cover.

In the event that problems occur during the towage transit, shipowners should ensure that their masters are familiar with and adopt the recommendations made in the *Gard Guidance to Masters*.<sup>13</sup>

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<sup>12</sup> For further commentary on wreck removal see Chapter 16 (Wreck removal claims).

<sup>13</sup> See, for example, Chapters 3.9 and 3.17 of the *Gard Guidance to Masters*.

## 15.6 Case Studies

### Case Study 1

The owners of the HOMEWOOD entered into a contract for the towage of the vessel from Workington to Glasgow for a fixed price. The HOMEWOOD had no propulsion power and was manned by only five crew members. The tow rope parted in very bad weather and fouled the tug's propeller. Therefore, the HOMEWOOD was forced to anchor in a place of refuge and the crew left the vessel pending the return of the tug. Subsequently, the tug returned to the HOMEWOOD and, despite the absence of the HOMEWOOD crew, cut her anchor chains, re-attached the tow and towed the vessel to Glasgow.

The owner of the tug claimed a salvage award for the service rendered in assisting the HOMEWOOD after the parting of the tow rope. The court held that the parting of the tow rope during the course of towing a vessel devoid of propulsion power in November was within the reasonably contemplated scope of the towage contract. However, the contract did not contemplate, *inter alia*, that her crew would have to be evacuated, that the vessel would have to be left at anchor with no one on board nor that the tow would continue without the assistance of the HOMEWOOD's anchors or crew. Therefore, there was an unexpected and unanticipated element of danger. Nevertheless, the original towage contract envisaged that the towage would be performed with the assistance of the HOMEWOOD's crew and anchors and since the tug decided of its own volition, and without reasonable justification, to forego that assistance, they were entitled merely to the remuneration agreed in the towage contract and could not claim salvage.

**NB!** If the tug had been entitled to claim a salvage award that award would have been paid solely by the shipowners and their Hull and Machinery insurers since no other interest was at risk. The sum payable under the towage contract would be payable solely by the owners of the HOMEWOOD but the costs of defending the claim may have been recoverable under their Defence cover.

### Case Study 2

The tug MIGHTY DELIVERER was contracted to tow the A TURTLE drilling rig from Brazil to the Asia on the TOWCON 1985 form which obliges the tug owners to use their "*best endeavours to perform their towage*" and to exercise due diligence to "*tender the tug at the place of departure in a seaworthy condition and in all respects ready to perform the towage.*" However, the contract also has a 'knock for knock' term which provides that each party to the contract agrees to bear the responsibility for its own people and property "*howsoever caused*" and "*whether or not the same is due to breach of contract, negligence or any fault*". The contract also provides that neither contracting party has the right of recourse against the other contracting party.

During the transit, the tug began to run out of fuel and the drilling rig was intentionally released from the tow since, if the tow had not been released, both tug and tow would have been at risk of loss at sea. After refuelling, the tug returned to search for the rig. However, after being adrift for several weeks, the rig finally ran aground on the island of Tristan da Cunha in the Atlantic. The owners of the rig brought a claim against the owners of the tug for the loss of the rig and the wreck removal costs and the owners of the tug brought a claim against the owners of the rig for the 95 per cent of freight that was *“due and payable on arrival of the tug and tow at the place of destination.”*

The English court held that the owners of the tug had not exercised due diligence to *“tender the tug at the place of departure in a seaworthy condition and in all respects ready to perform the towage”* since it was insufficiently fuelled for the transit despite the fact that surveyors appointed by the rig had surveyed the tug before concluding the towage contract and had issued a ‘fitness to tow’ certificate. The court also held that the tug was in breach of its continuing duty during the transit to use its *“best endeavours to perform the towage”*. However, despite these findings, the court held that the owners of the tug were not liable for the claims brought by the rig since they were protected by the ‘knock for knock’ provisions of the TOWCON charter. It also held that the tug owners were entitled to retain the 5 per cent freight that had been paid in advance but were not entitled to payment of the balance of 95 per cent since the precondition for payment (i.e. delivery at the agreed place of destination) had not been satisfied.

The hull of the rig was insured with Hull and Machinery insurers on special terms which included wreck removal cover up to a limit of 25 per cent of the insured value. The balance of the wreck removal costs was borne by P&I insurers.



## Chapter 16

# Wreck Removal Claims<sup>1</sup>

### 16.1 Introduction

A wreck is normally defined as a ship which has sunk or grounded, or has been beached, for example as a result of a collision, error in navigation, capsizing, fire, explosion or severe weather conditions, in circumstances where the costs of removal and/or repairs are considered to exceed the value of the ship after removal. Consequently, salvage is not deemed a viable commercial proposition and there is little commercial reason for the owners of the ship to incur the costs of removal.

Over the past few decades, there has been increased focus on the protection of the marine environment, local interests and safety issues. Many coastal states have therefore implemented regulations to mitigate as far as possible the hazards that arise as a result of shipwrecks and/or wrecked cargoes and/or other pollutants that may be on board. Consequently, it is now the rule rather than the exception that a wreck removal order will be issued when there is a wreck within the territorial or inland waters of a state, and that the shipowner will be required to bear other liabilities that may arise as a result of the presence from the wreck.

Depending on the size, type, condition and location of the wreck, the liabilities, costs and expenses that may be incurred in order to remove it can be very substantial. Wreck removal operations may be technically complex requiring advanced equipment, technology and skills that may be in limited supply. Furthermore, the shipowners may not be entitled under the local law to limit liability or may be subject to especially high limits. It is therefore of the utmost importance that any casualty that may render the shipowner liable for wreck removal is promptly reported to the relevant insurers and that any advice and recommendations that may be provided by the insurers and any specialist lawyers and other experts that may be appointed are followed.

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<sup>1</sup> More detailed commentary can be found in Chapter 11 of the *Gard Handbook on P&I Insurance*, 5th edition and in Chapter 11.7 of the *Gard Handbook on Protection of the Environment*, 3rd edition.

## 16.2 Liability for Wreck Removal Costs

### 16.2.1 General Aspects

The legal obligation that a shipowner may have to mark, light, raise, remove or destroy a wreck may be derived from a statute, local port/harbour regulations or contractual terms relating, for example, to the use of an oil or gas terminal or for provision of offshore services. A wreck removal order may therefore either be issued by a public authority based on a statutory or regulatory obligation, or it may be imposed by a private enterprise pursuant to a contractual obligation. The precise legal basis for the order may influence the rights of insurance recovery for wreck removal liabilities, costs and expenses.<sup>2</sup>

The removal of the wreck is usually required by law if it is located within the jurisdiction of a coastal state and poses a threat to navigation and/or is considered a hazard to the marine environment (especially if there is a risk that oil contaminants or toxic substances may escape) and/or represents an obstruction to commercial or public activities such as fishing or oil and gas exploration. Furthermore, the wreck may be considered to be aesthetically unsightly. For these and other reasons there will often be pressure on local authorities either to order removal of the wreck, or to take action themselves.

The type of measures that need to be taken depends on the type of order that is issued by the relevant authorities and may vary widely from case to case depending on the risks that the wreck is deemed to present. In some instances, the wreck of a grounded ship may only require additional lights pending further consideration, whereas a wreck which is partly submerged may also need to be marked with buoys or radar beacons. However, in both cases, wrecks that are deemed to pose a risk of damage either to the environment or to other vessels will often have to be removed in whole or in part. In some cases, the local authorities may be prepared to accept that the grounded wreck can be destroyed on site or that a submerged wreck can be partially removed by reducing the height of the wreck so that it no longer poses a threat to navigation.

If the wrecked ship is owned by a one-ship company that has, consequently, lost its only viable asset, its owners may, in a minority of cases, not be ready to co-operate, and it may not be possible to bring pressure on that company to raise the wreck. In such circumstances, there may be little choice for the owners of the waterway or the local governmental authorities but to remove the wreck themselves at their own cost and, thereafter, to try to recover those costs from the owners of the wreck or their insurers. Similar issues may arise where the sunken property is not the ship itself but parts of the ship or cargo or containers etc., that have fallen off the ship.

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<sup>2</sup> See Chapter 16.4 below.



The owners of the wreck may also incur liability to third parties for loss or damage incurred by them as a result of the presence of the wreck. Common examples include claims brought by the owners of another vessel that has been damaged as a result of contact with the wreck. Claims may also be brought by commercial or public interests alleging that they have incurred financial loss due to the fact that the wreck has caused an obstruction to, for example, a subsea pipeline, a power or telecommunications cable, or a seawater inlet to a waterfront industrial site. Alternatively, claims may be brought by fishermen, hotel owners or terminal owners whose business has been interrupted by the presence of the wreck.

In the event that the shipowners are liable for the costs of wreck removal and/or for claims brought by third parties, they may wish to recover such costs from other parties that may be responsible for the incident. The merits of such a claim will depend either on the terms of the relevant charterparty or contract of carriage (e.g. if the ship has become a wreck as a result of the carriage of dangerous goods or the nomination by the charterers of an unsafe port)<sup>3</sup> or on the tortious liability of any other third party, e.g. the owners of a colliding vessel.<sup>4</sup>

### 16.2.2 Law and Jurisdiction

Pending implementation of the Wreck Removal Convention 2007,<sup>5</sup> there is currently no international convention in force to regulate responsibility for wreck removal. Therefore, the obligation to remove a wreck and any related liability is governed by the local laws of the country where the wreck is located.

Countries have full jurisdiction in their territorial seas and internal waters but have more limited legislative and enforcement rights in the exclusive economic zone (EEZ) and on the continental shelf. Countries may only order the removal of wrecks from the EEZ and on the continental shelf if there is a specific legal basis for doing so under international conventions such as the International Convention relating to Intervention on the High Seas in Cases of Oil Pollution Casualties 1969, as amended in 1973 (The Intervention Convention).<sup>6</sup> The Intervention Convention provides that coastal states may take such measures outside their territorial seas that are necessary to prevent, mitigate or eliminate 'grave and imminent' danger to their coastline or related interests from pollution or threat of pollution. The action that may be taken by the relevant coastal state must be proportionate to the hazard, but in a worst case scenario the coastal state is entitled to remove and destroy the vessel. However, the Intervention Convention is not applicable where the wreck

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<sup>3</sup> For more detailed commentary see Chapter 13 (Safe Ports Claims).

<sup>4</sup> For more detailed commentary see Chapter 6 (Collision Claims).

<sup>5</sup> See Chapter 16.2.4 below.

<sup>6</sup> See also Chapter 22.3.2.2 (Maritime Regulation and Compliance) and Chapter 11.3 of the *Gard Handbook on Protection of the Marine Environment*, 3rd edition.

does not constitute serious pollution or a serious threat of pollution, but is simply a danger to safe navigation. Furthermore, countries only have limited powers to claim compensation for costs that are related to the removal of wrecks in the EEZ and on the continental shelf.

The laws of most local jurisdictions normally make the shipowner responsible for the removal of any property that is considered to be a threat to the territorial waters of that country and give the local authorities the right to intervene to do so themselves if necessary and to recover such costs from the shipowners. The basic rules of most countries can be summarised as follows:

- The owners of the vessel involved in a marine casualty must notify the coastal authorities promptly to enable rescue operations and anti-pollution measures to be taken promptly;
- The owners of the wreck must mark the position of the wreck promptly;
- The owners of the wreck will be required by the local authorities to remove or raise the wreck at its cost if it poses a danger to navigation and/or the environment and/or otherwise represents an obstruction;
- If the owners of the wreck do not do so, the local authorities will normally have the statutory power to do so themselves and to claim the costs from the owners of the wreck;
- The shipowners may be entitled to limit their liability in relation to the wreck removal costs, but in several countries, no such limit applies, or a higher limit applies;
- If the wreck has any residual value after it is raised, it can be sold and the proceeds used to defray the cost of the wreck removal;
- The owners of the wreck are responsible for third party claims caused by the presence of the wreck and any failure to take appropriate action to safeguard innocent third party interests.

The authorities of a country that has a claim against the shipowners for the costs of wreck removal will normally be able to sue the shipowners in the courts of that country and will subsequently seek to enforce any judgment in their favour against assets belonging to the shipowners in one or more jurisdictions where the judgments of that country are recognised and enforceable. Therefore, shipowners should be aware that the authorities in the country where the ship has become a wreck are likely to investigate whether the shipowners have any other assets in that country, and are also likely to keep a close eye on the trading pattern of any sister ships or other ships in the same management in order to obtain security, or to put pressure on the shipowners to remove the wreck, or to reimburse the authorities for any wreck removal expenses that they may have been obliged to incur themselves.

### 16.2.3 Limitation of Liability for Wreck Removal Claims

The cost of wreck removal can be very high and may exceed whatever the ship's global limitation fund may be under the relevant international limitation convention or limitation statute. Therefore, if the shipowners are obliged to incur such costs either directly or by way of indemnity for the costs incurred by the owners of the waterway or the local governmental authorities, they may wish to limit their liability for such costs.<sup>7</sup> Article 2.1 paragraph (d) of the 1976 Limitation Convention allows shipowners to limit their liability for "*claims in respect of the raising, removal, destruction or the rendering harmless of a ship which is sunk, wrecked, stranded or abandoned, including anything that is or has been on board such ship*" and similar rights can be found in the 1996 Protocol to the 1976 Convention and in the 1957 Limitation Convention. However, many of the countries that have ratified the 1976 Limitation Convention and its 1996 Protocol, have exercised the right that is granted by the convention<sup>8</sup> to exclude the right to limit liability for wreck removal. For example, the United Kingdom has done so that liability for such claims is unlimited in the United Kingdom. There is also case law in the United States which suggests that the Limitation of Liability Act, 46 U.S.C. 30501, et seq. does not apply to claims for wreck removal that must be carried out pursuant to federal law. Other countries have combined this right to 'opt-out' of the convention with the implementation of higher, special limits of liability for wreck removal claims, and, in some instances, other related claims such as pollution clean-up expenses.<sup>9</sup>

Therefore, it is important that shipowners should obtain prompt advice about the specific limitation rules that apply in the country where the issue of limitation is to be decided.

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7 More detailed commentary on limitation issues can be found in Chapter 21 (Limitation of Liability), in Chapters 27-30 of the *Gard Handbook on P&I Insurance*, 5th edition and in *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, Informa, 4th edition, 2005.

8 Article 18.1 of the 1976 Limitation Convention provides, *inter alia*, that: "*Any State may, at the time of signature, ratification, acceptance, approval or accession, reserve the right to exclude the application of Article 2 paragraph 1 (d) and (e).*"

9 This is the position in Norway. See the Norwegian Maritime Act, articles 172(a), 175(a) and 178(a). The latter provision regulates the legal effects of the constitution of a special limitation fund in respect of the types of claim to which the higher, special limits of liability apply.

### **16.2.4 The Nairobi International Convention on the Removal of Wrecks 2007 (The Wreck Removal Convention)**

The Nairobi International Convention on the Removal of Wrecks 2007 (Wreck Removal Convention) has been adopted by the IMO, but is not yet in force.<sup>10</sup> When implemented, it will fill the gap in the existing legal framework by providing the first set of uniform international rules that regulate wreck removal.

#### **16.2.4.1 Scope of Application**

The geographical area of application of the convention is the EEZ of any state party. The convention will therefore provide a firm legal basis for states to order the removal of wrecks and to claim compensation. There is an opt-in solution where contracting states may declare that the application of the convention shall extend to their territorial seas, where the states have full jurisdiction.<sup>11</sup>

#### **16.2.4.2 Reporting, Locating, Marking and Removing Wrecks**

The convention imposes a duty on the master and the operator of the ship to report without delay when a ship has been involved in a maritime casualty resulting in a wreck. The state is obliged to locate the wreck and determine whether the wreck poses a hazard to navigation or the marine environment.

If the wreck is determined to be a hazard, the state shall ensure that all reasonable steps are taken to mark the wreck by using the international system of buoys and publish the location of the wreck through notices to seafarers.

The registered owner will be under an obligation to remove the wreck if it poses a hazard to navigation or the marine environment. If the owner does not remove the wreck within a deadline set by the state, or the owner cannot be contacted, or the circumstances require immediate action, the state may remove the wreck by the most practical and expeditious means available and make a claim against the shipowners or their insurers for reimbursement of its costs.

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<sup>10</sup> The Convention will enter into force twelve months following the date on which ten States have either signed it without reservation as to ratification, acceptance or approval or have deposited instruments of ratification, acceptance, approval or accession. As at 31 October 2012 the following States had deposited such instruments: Bulgaria, India, Iran (Islamic Republic of), Nigeria and Palau. Another six States were signatories, but all subject to ratification or approval: Denmark, Estonia, France, Germany, Italy, Netherlands.

<sup>11</sup> In the negotiations of the convention, Norway argued that the state territories should be part of the geographical area of application since most wrecks are located within the territorial seas. It is therefore expected that Norway will be among the states that will exercise the right to extend the application of the convention to its territorial seas.

### 16.2.4.3 Liability of the Owner

The convention imposes strict liability (without regard to fault) on the registered owner of the ship for the costs of locating, marking and removing the wreck, provided that these costs are reasonable and in proportion to the hazard. Liability is subject to the customary defenses that are found in the IMO liability and compensation conventions, i.e. that the maritime casualty that caused the wreck (1) resulted from an act of war, hostilities, civil war etc.; (2) was wholly caused by an act or omission done with the intent to cause damage by a third party; or (3) was wholly caused by the negligence or other wrongful act of any government or authority responsible for the maintenance of lights or other navigational aids in the exercise of that function.

### 16.2.4.4 Limitation of Liability

The convention itself contains no right to limit liability in any specific way. Instead, unlike the CLC but similar to the Bunker Convention,<sup>12</sup> it merely provides that shipowners are entitled to exercise whatever rights they may have to limit their liability under the relevant general limitation conventions or statutes.<sup>13</sup>

### 16.2.4.5 Compulsory Insurance and Direct Action<sup>14</sup>

The convention requires the owner of a ship of 300 gross tons and above to maintain insurance to cover its liability under the convention, provided that the ship is flying the flag of a state party or is entering or leaving a port in its territory, or arriving at or leaving from an offshore facility in its territorial waters. Such insurance must be for no less than the limits of liability under the relevant national or international limitation regime but need not exceed the limits under the 1996 Protocol and each ship must carry an insurance certificate in an approved format, similar to that required by the 1992 CLC Convention,<sup>15</sup> the 2001 Bunker Convention<sup>16</sup> and the 2002 Athens Convention.<sup>17</sup> In similar fashion, the convention allows claims to be brought directly against the insurer.

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<sup>12</sup> For more detailed commentary see Chapter 12.4.1.1.2 (Pollution Claims).

<sup>13</sup> See Chapter 16.2.3 above.

<sup>14</sup> See also Chapter 16.4.1 below.

<sup>15</sup> For more detailed commentary see Chapter 12.4.1.1.1.5 (Pollution Claims).

<sup>16</sup> For more detailed commentary see Chapter 12.4.1.1.2 (Pollution Claims).

<sup>17</sup> For more detailed commentary see Chapter 11.3.2.4 (People Claims).

### 16.3 Wreck Removal Contracts

Depending on the size of the wreck removal operation, several international contractors are often requested to bid for the work through a tender process. Most of the potential contractors are professional salvage companies that have the necessary vessels, equipment and skills to remove wrecks sufficiently expeditiously and in a safe and environmentally friendly manner. However, for the most complex and demanding operations, potential contractors may decide to combine their overall resources in the form of joint ventures and bid for the work in such a capacity.

An Invitation to Tender (ITT) will be normally prepared by the technical experts that are advising the shipowners and insurers and will outline the details of the casualty and the scope of work required. The bid will normally cover three items: price, time and method of removal and a time limit within which all bids must be submitted will be established. The contractors to whom the ITT has been sent will then decide whether to bid or not and once all bids have been received, they will be evaluated by the shipowners and insurers together with their legal and technical advisers, and a decision will be taken, sometimes to award the contract immediately, and sometimes to continue negotiations with one or more of the contractors that have made the most attractive bids.

The wreck removal is normally conducted pursuant to the terms of one of the BIMCO standard contract forms such as Wreckhire 2010 (which provides for remuneration by way of a daily hire), Wreckstage 2010 (which provides for remuneration by way of a lump sum split into several stage payments) and the somewhat less used Wreckfixed 2010 (which provides for remuneration on a fixed price – no cure, no pay basis). The use of the BIMCO forms enables the parties to avoid the lengthy negotiations that would otherwise be necessary, although the BIMCO standard documents often need to be adjusted and supplemented by special provisions relating to the operation in question.

Contractors normally agree to lump sum contracts when the wreck removal operation is relatively predictable and straight forward but in unpredictable or especially challenging circumstances, a daily rate contract, or a hybrid is often used. In the Wreckhire 2010 contract, the daily rate basis has been modified somewhat compared to the 1999 version. A bonus incentive scheme has been introduced, which is designed for operations that are likely to last for an extended period of time. The contractor is entitled to an agreed bonus if removal is completed before a specific date, but the bonus may be reduced on a sliding scale if the date is missed. A reduction in the daily rate of hire has also been introduced if the services are not completed within an agreed time.

## 16.4 Insurance

### 16.4.1 P&I Insurance<sup>18</sup>

The costs of wreck removal are normally covered by P&I insurance. Such insurance will normally cover the costs of the marking, raising, removal and destruction of the ship or any part of the ship, or of any cargo, containers or any other property that has fallen from the ship. However, such cover is normally available only if:

- These items have been lost as a result of a maritime casualty;<sup>19</sup> and
- The shipowners are legally obliged by international convention or local law to take the relevant remedial action; or the costs and expenses incurred by any third party in taking such remedial action is legally recoverable from the shipowners; and
- The hull and machinery insurers have not assumed ownership of the wreck; and
- The shipowners have not transferred their interest in the wreck to some other party.

Should the shipowner incur liability for wreck removal by virtue of the terms of a contract for the use of a terminal, berth or offshore site, cover is available only if the P&I insurer has given its prior approval to those (or materially similar) terms.<sup>20</sup>

Cover is also normally available for liabilities that may be incurred by the shipowners as a consequence of the wreck causing an obstruction, including, for example, liability for demurrage and delay incurred by other ships, as well as for liabilities resulting from the fact that another ship has collided with the wreck.<sup>21</sup>

In all cases, the relevant P&I insurers must be kept closely involved in order to ensure that the shipowners' legal rights, including any right to limit their liability, are fully protected. If the shipowners fail to do so and incur wreck removal costs that exceed the amount to which they could have limited their liability had prudent action been taken, cover may not be available. Furthermore, since the P&I insurers are entitled to be credited with the residual value of the wreck, (i.e. the net proceeds of any sale) if they provide cover for the wreck removal cost, the shipowners are obliged to offer all necessary assistance to the P&I insurers in order to maximise the realised value of the wreck.

<sup>18</sup> For further commentary see Chapter 26.3.1.5 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 40 (Liability for obstruction and wreck removal)).

<sup>19</sup> In this context, a casualty is an event caused by a maritime accident such as a grounding, fire, collision or contact with a fixed or floating object. Therefore, cover is not available, e.g. in the case of a ship which has become a wreck as a result of lack of maintenance or abandonment on the part of the assured.

<sup>20</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 55 (Terms of Contract)).

<sup>21</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 40 (Liability for obstruction and wreck removal)).

It has already been stated above that if the Wreck Removal Convention comes into force, shipowners will be required to provide certificates evidencing the fact that ships have the insurance cover that is required by that convention.<sup>22</sup> However, it is not yet certain whether, or to what extent, P&I insurers will be prepared to provide such certificates in view of the fact that some of the liabilities that are regulated by the convention fall outside the scope of the standard P&I cover (such as, for example, liabilities caused by terrorism, or by a bio-chem, nuclear or cyber attacks).

#### **16.4.2 Hull and Machinery Insurance<sup>23</sup>**

Hull and machinery insurers do not normally provide cover for the cost of wreck removal. If the cost of removing a ship exceeds her value after recovery the ship is normally considered to be a total loss and the insurers will agree to pay the shipowners the agreed insured value under the policy. In the event of a total loss, the assured will normally tender notice of abandonment of the ship to the hull and machinery insurers who are entitled in principle under the doctrine of subrogation to take over all rights that the assured had in the ship. However, there is no obligation to do so and hull and machinery insurers are normally unlikely to do so if the ship has become a wreck since if the local coastal authorities were to demand the removal of the wreck, they would thereby become responsible for doing so as the owners of the wreck.

#### **16.4.3 Indirect Cover under Hull and Machinery or P&I Insurance**

The hull and machinery insurance will often provide cover for collision liability. If the wreck removal is the result of the tortious liability of another ship (e.g. as a result of a collision) and the shipowners recover an indemnity from the owners of the other ship in respect of liabilities or losses incurred by them as a result, the owners of the other ship may be covered for any liability that they have in such circumstances either in full or in part by their hull and machinery insurers. If such hull and machinery insurers only cover three fourths collision liability, the remaining one-fourth liability will normally be covered by that ship's P&I insurers.<sup>24</sup>

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<sup>22</sup> See Chapter 16.2.4.5 above.

<sup>23</sup> For more detailed commentary see Chapter 26.3.1.1 (The Structure of Marine Insurance).

<sup>24</sup> For more detailed commentary see Chapter 6.8 (Collision Claims) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 36 (Collision with other Ships)).



#### 16.4.4 Charterers' Liability Insurance<sup>25</sup>

If the wreck removal is the result of a breach by charterers of the terms of the relevant charterparty or contract of carriage and the shipowners recover an indemnity from charterers in respect of liabilities or losses incurred by them as a result, the charterers may be covered for any liability that they have to the shipowners in such circumstances by charterers' liability insurance.

#### 16.4.5 Cargo Insurance<sup>26</sup>

Normally, there is no cover under standard cargo insurance clauses such as the ICC clauses for the costs of recovering cargo which has fallen from a ship where the costs of recovery are greater than the insured value of the cargo.

#### 16.4.6 Marine Container Insurance

Normally, there is no cover under standard marine container insurance clauses such as the Institute Containers Clauses-Time 1/1/87 or the Institute Container Clauses – Time Total Loss, General Average, Salvage, Salvage Charges, Sue and Labour 1/1/87 for the costs of recovering containers which have fallen from a ship where the costs of recovery are greater than the value after recovery. In such circumstances, it is likely that cover may be provided either by charterers liability insurers or under owners' P&I insurance since most P&I insurers provide cover for *"costs and expenses relating to the raising, removal, destruction, lighting and marking of the Ship or the wreck of the Ship or parts thereof or of its cargo lost as a result of a casualty"* when such costs are legally recoverable from the insured member.

### 16.5 Claims Management

Wreck removal claims are often complex, time consuming and expensive. They may occur in locations which give rise to political, legal and environmental challenges and may be subject to the added pressures of high media coverage and public outcry. Shipowners must promptly report such serious incidents to the relevant authorities, flag state, classification society and their insurers, and take immediate action to minimise the danger of pollution and threats to navigation. However, the removal of pollutants and the wreck itself should be conducted by professional contractors.

For all these reasons, the P&I insurer must be promptly notified and kept closely advised and involved. The best remedial strategy requires close liaison. The process of engaging a wreck removal contractor and the follow-up during the wreck removal

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<sup>25</sup> For more detailed commentary see Chapter 26.3.2 (The Structure of Marine Insurance) and the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 52 (Limitations for charterers and Consortium Vessels)).

<sup>26</sup> For further commentary see Chapter 26.3.3 (The Structure of Marine Insurance).

operation may require extensive administration and assistance from technical experts, lawyers and the P&I insurer. It is also important that the general response advice outlined in Chapter 3.1 of the *Gard Guidance to Masters* should be followed to ensure that the legal and political impact of the incident can be controlled from the outset.

It is often in the best interest of the shipowner and P&I insurer to assume and retain control over the wreck removal process where this is permitted by the authorities, and not leave it to the local authorities or other third parties. A proactive and professional attitude is likely to lead to better control of the factors that affect costs overall.

### **16.6 Case Study**

At 0215 hours local time on 14 December 2002 a vehicle carrier loaded with 2,871 new luxury cars plus some other cargo bound for the United States, collided with a general cargo vessel in the French EEZ of the English Channel whilst on a crossing passage from Zeebrugge, Belgium to Southampton, England. Prior to the incident, both vessels were sailing on similar courses in the traffic separation lane in order to enter the southwest-bound traffic lane. The vehicle carrier was slowly overtaking the other vessel on her starboard side when the latter suddenly and unexpectedly altered course strongly to starboard, causing her bow to heavily strike the port side of the vehicle carrier amidships. The vehicle carrier immediately suffered ingress of water and sank in less than half an hour, fortunately with no loss of life, in a water depth of about 27 metres. The hull was overturned sideways with the starboard side facing up, partly visible in low water.

French authorities having responsibility for the safety of shipping and the environment for the relevant area, issued a notice to the owners of the vehicle carrier requiring them to immediately take steps to eliminate the threat of pollution from the vessel and a professional salvage company was contracted to remove and dispose of the bunkers and other oil on board.

The vessel had sunk in a very busy part of the traffic separation scheme, and represented a hazard to navigation given its exposed position, particularly since the hull would be submerged on high tide. The French authorities therefore marked the vessel initially with one wreck buoy and deployed a naval patrol vessel to guard the area and provide warnings to other ships. In addition, the French, Belgian and English authorities gave warnings about the vessel to other ships in transit in the area. However, in spite of these efforts, two days after the incident a general cargo vessel collided with the sunken vehicle carrier causing hull damage.

After this incident the French authorities decided to enhance the safety measures by deploying five cardinal buoys around the sunken vessel by a distance of 600 metres, one of which was equipped with a radar beacon and a naval patrol vessel remained on site at all times.

On 23 December 2002, the hull and machinery insurers of the vehicle carrier confirmed their acceptance of the fact that the vehicle carrier was a total loss and they abandoned their interest in the vessel. Various orders were issued by the French authorities for the removal of oil on board as well as the wreck itself pursuant to the Intervention Convention 1969 in view of the threat of environmental damage that the wreck represented in its exposed location.

The process of preparing an Invitation to Tender (ITT) for the removal and disposal of the wreck and the cargo of vehicles on board was started with close involvement of the P&I insurer. At the same time, and in spite of the enhanced safety measures on site, yet another vessel, this time a combination carrier with heavy oil cargo on board, collided with the wreck. The vessel sustained substantial hull damage and both cargo and fuel oil escaped, causing marine pollution.

The ITT was submitted to a selection of salvage companies on 17 January 2003 and technical experts were appointed to assist in the review of bids. On 11 April 2003 a wreck removal contract on an amended Bimco Wreckstage 1999 Form was signed with a consortium consisting of four salvage companies. The contract provided, *inter alia*, for payment to be made in stages upon reaching defined milestones, and for the payment of extra remuneration if the removal operation was completed by a certain date.

The removal operation was complex and required the use of special crane barges, other equipment, skills and creativity. The wreck was cut into nine sections from the seabed upwards by a specially designed diamond cutting wire system operated by a vessel on each side of the wreck. Each wreck section, with the cargo of vehicles inside, was lifted by means of large sheer-leg cranes working in tandem onto a transport pontoon for carriage ashore, where the cargo was separated and disposed of according to EU regulations. The engine section weighed more than 3,000 tons and represented the heaviest submerged item ever lifted by cranes operating at sea.

Due to adverse weather conditions and other challenges, the removal work was not completed according to the original plan and, therefore, the contractor earned no bonus. The work was resumed in May 2004 and formally completed in October of that year after the French authorities had inspected the casualty site and seabed and lifted the removal order. However, the cargo and wreck disposal operations ashore took some more time to complete.

Whilst these events were happening, various legal actions were commenced by the different parties that were affected by the casualty in, *inter alia*, Belgium, The Netherlands, France, the UK, and the USA. Limitation funds were constituted both in Belgium and The Netherlands and the relevant P&I insurers exchanged letters of undertaking on a reciprocal basis, and agreed that Belgian jurisdiction and law should apply to the inter-ship claims.

The case illustrates the complexity and longevity of some large casualties. More than ten years after the incident litigation is still on-going. One of several legal issues pending is whether, according to Belgian law, the owners of the surviving vessel may limit their liability for the wreck removal claim that has been brought by the owner of the vehicle carrier as part of the overall collision claim.

## Chapter 17

# Claims Resolution Systems

### 17.1 Introduction

It is generally preferable from a cost, time and customer relations standpoint to settle claims whenever possible. However, this is not possible in all circumstances for various reasons and, therefore, parties will need to refer the dispute to a neutral third party for resolution. The classic neutral third party is a judge and the constitution of practically all countries enables parties to refer disputes to such a judge as a matter of right. Furthermore, courts and judges have become increasingly more sophisticated with the passage of time and many countries now have specialised courts to hear specialised disputes. This is particularly true of maritime countries many of which have admiralty courts or specialised commercial courts which have developed particular expertise in resolving the claims and disputes that arise as a result of maritime activity. However, for a variety of reasons, parties often consider resolving their disputes outside court and have turned to other claims resolution systems such as arbitration, mediation etc. The reality of the situation is that different types of dispute require different types of claims resolution systems and it is not possible to say dogmatically that any one system is inherently better than any other.

### 17.2 Court Proceedings

The reader will probably be more familiar with court proceedings than other forms of dispute resolution systems since this is the system that most people encounter in day-to-day life. However, court systems do differ between countries and it is not possible to comment in detail on such differences. Nevertheless, it can be said that court proceedings normally have the following advantages:

- The judge has wide powers to ensure that all relevant evidence and witnesses are made available and can, if needs be, call on the power of the state to ensure that this is done. A failure by any party to comply with a court order can constitute contempt of court and can attract substantial penalties including fines and even imprisonment in extreme cases;

- Court proceedings follow established rules and timetables which ensure that the litigation progresses in an orderly fashion without inordinate delay;
- The court can require security to be provided and can enforce provision of security by attachment of assets, arrest of a ship etc.;
- The judge can interpret the law accurately and any failure by him to do so can be rectified by a higher court of appeal;
- The judgement of the court (or court of appeal if there is an appeal) is final and the judgement can be enforced by the power of the state;
- The judgement can create a precedent which will be binding in subsequent cases before the same court in relation to the issue in dispute and may therefore, avoid future litigation on the same point either with the same party or with other parties.

However, court proceedings can also suffer from the following disadvantages:

- Proceedings can be complicated and expensive;
- There can be lengthy delays if a case is complicated and the court diary is congested;
- The process can be very formal and inflexible. Whilst judges are generally prepared to be flexible, their efforts may be restricted by rigid court rules;
- The process is public in nature. Court proceedings are normally open to the public and the judgement of the court is a public document which can be inspected by anyone. Therefore, it is difficult to maintain privacy of information;
- A judge may not have any particular knowledge of the particular trade or industry. Judges are experts in the process of dispute resolution but they may not have much personal knowledge of the subject matter of a dispute;
- Questions may arise in some countries as to whether a foreign litigant benefits from a fair process when the competing litigant is a local party.

### **17.3 Arbitration<sup>1</sup>**

It has been the public policy of most countries for many years to support arbitration if that is the means by which parties wish to resolve their disputes. This policy is summed up in Section 1 (b) of the Arbitration Act 1996 of the United Kingdom which provides that:

*“The parties should be free to agree how their disputes are resolved subject only to such safeguards as are necessary in the public interest.”*

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<sup>1</sup> For more detailed commentary see Chapter 29 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008, paras. 2.72 to 2.87 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition, 2007 and paras. 14.35 to 14.39 of *Bills of Lading* by Aikens, Lord and Bools, 2006, Informa.

This policy is given further impetus by The New York Convention on the Recognition and Enforcement of Arbitral Awards 1958 which obliges the courts of countries that are parties to the convention to stay any proceedings which have been commenced in their courts if the parties have agreed in writing that the relevant dispute should be resolved by arbitration and an application for a stay is made by one of those parties. The New York Convention also provides that the courts of countries that are parties to it must enforce any arbitration award that has been made in any other convention country unless such enforcement is contrary to the public policy of that country. This convention has been ratified by a very substantial number of countries and consequently, arbitration has traditionally played a big part in relation to the resolution of maritime claims. Many contracts of carriage, particularly charterparties, include clauses which provide that disputes are to be resolved by arbitration in one of the major arbitration centres around the world.

One of the main reasons for the popularity of arbitration is the fact that, whilst court proceedings are normally open to the public pursuant to the constitution of most countries, arbitration is private. Therefore, whilst a court judgement is a public document which can be disclosed to anyone, an arbitration award cannot normally be disclosed to any party other than the parties to the arbitration unless both of the latter parties agree to the disclosure. Furthermore, many disputes require expert knowledge which can only be acquired by intimate experience of the particular trade. Therefore, such knowledge is more likely to be had by arbitrators than judges. Each major arbitration centre around the world tends to have its own arbitration rules and it is important to make sure that the rules of any particular arbitration centre are clearly understood before agreeing to arbitrate there. For example, it is often said that whilst London arbitrators are bound to ensure that their awards are made in accordance with legal precedent, New York arbitrators have more freedom to disregard legal precedent if they believe that the interests of justice require this to be done in the particular case.<sup>2</sup> This has led to the belief that London arbitration awards are more predictable whilst New York awards are more likely to avoid unfairness. Neither comment is completely true but they are indicative of the relatively different approaches that are adopted by the two arbitration centres.

It is not possible to comment in detail on variations between the rules of the various arbitration centres. However, it can be said that arbitration proceedings normally have the following advantages:

- The constitution of the arbitration tribunal or panel can be decided by the parties themselves. There can be a sole arbitrator or a tribunal of any odd number (3, 5, 7, etc.) or a tribunal of two and an umpire;

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<sup>2</sup> See, for example, the decision of the US Supreme Court in *Hall St Assocs.LLC v Mattel Inc*, 2008 US Lexis 2911.

- The arbitrators can be chosen either by the parties themselves or by trade organisations such as the London Maritime Arbitrators Association (LMAA), the New York Society of Maritime Arbitrators (SMA), the Hamburg Chamber of Commerce or the Singapore Chamber of Maritime Arbitrators (SCMA) amongst others;
- The parties can choose the form of the arbitration. For example, it can be very informal and proceed by exchange of written submissions or formal involving pleadings and an oral hearing. Most arbitration centres now provide a simplified arbitration system which proceeds on the basis of documents alone and which restricts the exposure of the losing party to costs up to a reasonable limit;
- The arbitrators can order discovery of documents or samples or other physical evidence and can require the attendance of witnesses. In most countries, court orders to this effect can be obtained if necessary;
- The New York Convention on the Recognition and Enforcement of Arbitral Awards 1958 provides that the courts of countries that are parties to the convention must enforce any arbitration award that has been made in any other convention country unless such enforcement is contrary to the public policy of that country. This convention has been ratified by a significantly large number of countries around the world including countries that have not ratified other international or bilateral conventions providing for the enforcement of court judgements. Therefore, arbitration awards can often be enforced in countries which are not obliged to enforce court judgements made in the country of arbitration.

However, arbitration proceedings can also suffer from the following disadvantages:

- The uncertainty of the result. Arbitrators are not necessarily legally trained and may not always reach conclusions which can be supported by legal principle. In some countries such as the United Kingdom parties are entitled to appeal to the courts on issues of law (but not on findings of fact) if they believe that the tribunal has erred in law. However, the right to appeal is restricted in that the error must appear on the face of the award and must normally be either obviously wrong or have some general importance to the world at large not just to the parties to the dispute. In other countries, the tribunal may not be bound to follow legal principle and may reach their decision based on purely equitable principles. Such decisions are difficult to predict and to overturn since they are based on the tribunal's subjective assessment of what is fair in the particular case;
- Arbitrators are not able to grant remedies such as injunctions which require the power of the state to enforce;
- Whilst arbitrators normally have the right to order production of documents, witnesses, samples, etc., and to draw adverse conclusions if such evidence is not produced, they cannot normally enforce such production without the assistance of the court;



- The delay in obtaining a hearing in complex cases. If the arbitration is complex and requires a tribunal of three or more arbitrators it may be difficult to secure dates which can accommodate the diaries of all the parties and arbitrators that are involved with the result that the proceedings can be substantially delayed;
- Arbitration awards are not binding on any party other than the parties to the arbitration. Therefore, awards have no public value as binding precedent. Even when arbitration awards are published with the consent of the parties (as is the case with SMA awards in New York) those awards have persuasive rather than binding authority.

#### **17.4 Alternative Dispute Resolution (ADR) Systems**

It has become more common in recent years for parties to wish to resolve disputes by the use of innovative ADR systems which are considered to avoid the cost and delays which have increasingly come to plague traditional resolution systems such as arbitration and court litigation. It is also recognised that there is always a 'litigation risk' when claims are brought before a court or arbitration tribunal and that the adversarial nature of litigation can ruin a commercial relationship.

The main difference between litigation or arbitration on the one hand, and ADR on the other hand, is that whilst litigation and arbitration result in a binding award or declaration, ADR does not do so unless the parties wish it to do so. Therefore, whilst the mediator can suggest a possible solution after the parties have aired their differences before him, the parties are not bound to accept it. Furthermore, the mediator does not normally give his views on the merits of each party's case unless the parties wish him to do so as his function is merely to facilitate a meeting of hearts and minds. He may seek to achieve this result in whatever way the parties require and the discussion can range far and wide regardless of the subject matter of the original dispute. For example, the parties may finally agree a compromise which is not based on a compromise of the original dispute but on agreeing a new contract for a completely different venture.

If the parties agree to settle after engaging in the ADR process the agreement is normally recorded in a settlement agreement which is signed by both parties. Thereafter, if the agreement is not honoured by one of the parties, the other party can apply to the court to enforce the agreement. Such a procedure is the equivalent of an application to enforce any other kind of contract or agreement and does not necessitate any re-opening of the underlying dispute or claim.

However, if the ADR process has not succeeded in achieving compromise, the parties may still proceed to resolve the original dispute by more traditional dispute resolution systems such as litigation or arbitration. In that event, the mediator cannot

normally play any further part in the litigation or arbitration process and neither party is entitled to make any reference in the subsequent litigation or arbitration to anything which has been said or done in the preceding ADR process.

It is reported that ADR has a success rate of approximately 80 per cent and many maritime organisations have recognised the benefits that ADR may bring in appropriate circumstances. Indeed, organisations such as BIMCO and the London Maritime Solicitors Group have produced standard clauses which enable the parties either to arbitrate or to use ADR as the circumstances require without prejudice to their wider rights. Furthermore, many of the leading arbitration centres around the world provide ADR services instead of, or as well as, arbitration services if this is required by the parties. However, ADR is of little practical benefit if one or more of the parties has no interest in settlement and is determined to litigate or arbitrate at all costs, or when one or both parties wish to create a binding precedent. It can also be used irresponsibly when a guilty party has no real defence to a claim but wishes merely to delay resolution for as long as possible.

There are various ADR systems which are currently employed, such as:

- Mediation. A mediation is a settlement negotiation meeting which takes place between two or more parties to a dispute in the presence of a specially trained facilitator whose function is to try to broker a settlement of the dispute;
- Conciliation. Conciliation is similar to mediation except that the conciliator tends to play a more active role and may offer suggestions and opinions in an effort to encourage the parties to reach a settlement;
- Early Neutral Evaluation (ENE). This is where a trusted third party is asked by the parties to the dispute to consider and pronounce his views on the likely merits of the claim or on one or more aspects of the claim at an early stage before full evidence is available and before full argument has been made; and
- Med-Arb. This is a process whereby the parties agree that if the mediation does not result in a settlement the mediator converts into an arbitrator and makes a binding award.

Courts are increasingly ready to encourage parties to use ADR systems in appropriate cases and have often ordered court proceedings to be stayed for say, one month, to enable the parties to try ADR solutions. Such orders can be made either on the application of one or more of the parties or by the court of its own volition. If such an order is made then any party which is seen not to be co-operating may suffer costs penalties in due course even if that party were to win the subsequent litigation since courts usually have a discretion when awarding costs.

## 17.5 Costs

All claims resolution systems will involve parties incurring legal and other costs and a decision to engage in any such processes will require consideration of the following issues:

- How much will the process cost?
- Will the successful party be entitled to recover those costs from the losing party?

It is not possible to comment on the cost of the various processes since so much depends on the nature and complexity of the particular dispute, the location of the claims resolution process and the seniority and expertise of the legal and other assistance that may be required. However, it is vital that all parties engaged in a dispute should ask for realistic quotes of the likely cost from the various people who will be involved in pursuing or defending the matter before embarking on the process. Parties can be assisted in this regard by their P&I insurers or Defence insurers who will have up-to-date information on these issues. However, if parties do not involve their liability insurers in these enquiries at an early stage their right to claim reimbursement for such costs in due course may be prejudiced.<sup>3</sup>

The question of whether costs can be recovered from the losing party arises only in the case of adversarial processes such as court litigation or arbitration. If the parties engage in non-adversarial ADR processes then the costs are usually shared equally and neither side is entitled to recover any proportion of those costs from the other side. However, there is nothing in principle to prevent the parties agreeing a different cost-sharing ratio in any settlement agreement which may result from the ADR process.

The question of whether costs can be recovered from the losing party in adversarial processes normally depends on the country where that process takes place. The laws of the majority of countries give the court a discretion whether to allow the winning party to recover costs from the losing party and if so, what proportion of those costs. In the majority of cases the court will allow the winning party to recover the bulk of the costs that it has incurred unless there are equitable reasons to the contrary, e.g. where the winning party has conducted the litigation in a reprehensible way. However, there are important exceptions to this rule. For example, US courts tend to require parties to bear their own legal costs, including lawyers' fees (with some exceptions for specific items designated under applicable court rules). However, it is important to understand that this general rule may not be applied if there is a contractual or statutory provision to the contrary or the law governing

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<sup>3</sup> See Chapter 17.6 below.

the underlying dispute permits or requires legal costs to be awarded. Arbitrators in the US will award legal costs if permitted by the rules governing the arbitration, by agreement of the parties, or by the law of the applicable contract.

### **17.6 Insurance Issues<sup>4</sup>**

When insurers of any type are involved in a particular claim or dispute, it is important that those insurers are involved in any discussions relating to appropriate claims resolution procedures. The assured has a duty to safeguard any rights to which the insurer may become entitled by way of subrogation in due course and his right to be indemnified by the insurer may be prejudiced if the assured adopts a claims resolution strategy which does not have the approval of the insurer.

If the claim is one that is covered by any of the standard insurances that shipowners normally take out (i.e. hull and machinery, P&I, war risks etc.) it will be those insurers that need to be consulted. However, if the claim does not involve any such insurances, the assured may wish to secure the support of his Defence cover insurers to finance the litigation. An important feature of the Defence cover (which is normally placed as a separate class of cover with the assured's P&I club) is that it enables the club officials to provide advisory and financial support to a member who may be involved in a large and/or complicated case including the member's potential liability to pay for legal and other costs that may be incurred by the member's opponent should the member lose the case. However, such financial and other support is not given unquestionably or without limit. The rules relating to Defence cover normally give the club officials the right to control and direct the handling of any case and to withdraw cover at any stage if they believe that the manner in which the member is pursuing or defending the claim is considered to be contrary to the best interests of the membership as a whole. Therefore, it is very important that a claimant or defendant should seek the view of his Defence club officials before embarking on any particular claims resolution strategy.<sup>5</sup>

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<sup>4</sup> For more detailed commentary see Chapter 26.3 (The Structure of Marine Insurance).

## Chapter 18

# Frustration<sup>1</sup>

### 18.1 Introduction

In some instances, a contract can be terminated automatically at law when an unexpected event occurs without any default on the part of either party to the contract. Such a principle exists under most legal systems under different names but the term that is used most often is that which is used in common law systems, i.e. frustration of the contract. The classic definition of frustration was given by the High Court of England and Wales in the case of *Davis Contractors v Fareham UDC* in 1956:

*“Frustration occurs whenever the law recognises that without default of either party, a contractual obligation has become incapable of being performed because the circumstances in which performance is called for would render it a thing radically different from that which was undertaken by the contract. Non haec in foedera veni. It was not this that I promised to do.”*

In the majority of cases a contract is declared to be frustrated because one of the parties to the contract alleges that this is the case and applies to a court or tribunal for a declaration to this effect. However, frustration occurs automatically at law. Therefore, if a court is satisfied that the facts constitute frustration, then the contract is treated as terminated even though neither of the parties to the contract may have asked the court to make a declaration to this effect. The parties can, of course, continue to deal with each other on the same terms and conditions should they so wish and often do so in practice. However, in legal terms, they are then operating under a new contract which happens to be on the same terms as the one that has been terminated by frustration.

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<sup>1</sup> For more detailed commentary see Chapter 22 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition, 2007 and Chapter 26 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Indoema, 6th edition, 2008.

## 18.2 The Effect of Frustration

Should the contract be frustrated then, under the common law, the parties are released as from the moment of frustration from any future duties or obligations under the contract, but any rights which have accrued due before the frustration remain binding and enforceable. For example, if freight is earned and payable on delivery of the cargo but the contract of carriage is frustrated before the end of the voyage, no freight is payable as the payment of freight is a future (post frustration) obligation. However, if freight is earned on shipment and is payable before the frustrating event (i.e. advance freight), then it remains payable (or non-returnable if it has already been paid before the frustrating event) despite the fact that the charter has subsequently been frustrated before the end of the voyage.

The freight in the last example was earned on shipment and therefore, the shipowner had done that which was necessary to earn the freight before the frustrating event. However, in some instances, payments are made in advance for services which will not be earned until later. For example, time charter hire is normally payable in advance (e.g. every 30 days in advance) but the payment relates to services which will be earned progressively during the next 30 days. Therefore, if the contract is frustrated before the expiry of those 30 days, payment will have been made for services which have not yet been performed and therefore, the full payment will not yet have been earned when the frustrating event occurs. In such circumstances, sums which have been paid but not earned before the occurrence of the frustrating event are normally repayable. For example, if the time charter is frustrated on the 20th day, the shipowner would normally be entitled to retain only 20 days hire out of the full 30 days hire that had been paid in advance.

## 18.3 What Constitutes Frustration?

### 18.3.1 There must be more than mere Extra Cost, Difficulty or Delay

When considering whether or not there is frustration, the tribunal considers the impact of the event in the light of the terms of the contract and the obligations of the parties. However, the fact that performance has become more expensive, difficult or time-consuming, even substantially more expensive, difficult or time-consuming, is not in itself sufficient to frustrate the contract. The tribunal must be satisfied that the event has rendered performance of the contract either impossible or so radically different from that originally contemplated by the parties that it would be unjust to hold the parties to the contract in the changed circumstances. For example, if the customary route for a contemplated voyage is blocked by an unforeseen event which means that the vessel has to proceed by an alternative route at substantially increased cost and delay, the contract is probably not frustrated since

the fact that there is an alternative route means that the contract, although now more expensive to perform, is not impossible to perform. The English court held in *The Eugenia*<sup>2</sup> that:

*“The fact that it has become more onerous or more expensive for one party than he thought is not sufficient to bring about a frustration. It must be more than merely more onerous or more expensive. It must be positively unjust to hold the parties bound.”*<sup>3</sup>

However, if the contemplated routing was the only possible routing then the contract may be frustrated since the intention of the parties will then have been rendered impossible by the frustrating event.

Common law courts have been prepared in some cases to conclude that impossibility is not restricted to physical impossibility but includes commercial impossibility. Logically, that means that additional cost or delay can sometimes result in frustration. However, each case turns on its own facts and whilst it is not possible to give concrete guidance as to what will constitute commercial frustration in all cases, it can be said as a general rule that the additional cost or delay must be extreme in the same way that marine insurance considers a constructive total loss (CTL) to be the equivalent of an actual total loss.

The question of whether or not there is frustration depends on the impact that the frustrating event has in relation to the particular contract. Therefore, if a vessel is time chartered for two years, the fact that the vessel is obliged to go into a repair yard for three months may not be sufficient to frustrate the contract as the delay does not radically undermine the value of the contract for the charterers. However, by way of contrast, if the vessel is voyage chartered to carry perishable goods on a voyage which should normally take three weeks, then the fact that the vessel is obliged to go into a repair yard for three months may be sufficient to frustrate the contract.<sup>4</sup>

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2 [1963] 2 Lloyd's Rep. 381.

3 See the Case Study in Chapter 18.8 below.

4 See Chapter 18.5.3 below.

### 18.3.2 The Event must be Unexpected

Traditionally, frustration has been considered to be an unexpected event which has radically changed the contemplated mode of performance of the contract. Therefore, if the particular event is either one which has been contemplated by the parties or, even more importantly, if the parties themselves have made provision for such an eventuality in the contract by the inclusion of a specific clause, then frustration may not be possible since, in such circumstances, the event must have been foreseeable and not unexpected.

Therefore, it appears that a specific clause of this nature will normally exclude the possibility of frustration only if:

- it contemplates the specific event; and also
- provides clearly and unambiguously exactly what remedy is available to the parties in that event; and
- makes “*full and complete provision for all of the effects of the supervening (frustration)*”.

Unless all three separate criteria are satisfied the possibility of frustration may not be excluded.

For example, in the case of *The Florida*,<sup>5</sup> the English court was asked to consider whether a contract was frustrated when the Nigerian government unexpectedly declared an embargo on future imports of vegetable oil. The charterers argued that the contract was frustrated and that consequently, they were under no obligation to find an alternative cargo. The shipowners disagreed and argued that since the contract included a detailed clause which laid down various alternative means of performance in such circumstances, the contract was not frustrated since the parties had themselves made provision for this eventuality. The court held that the contract was frustrated since the clause provided alternative means of performance only in the event that the embargo was declared *after* the cargo was shipped, whereas, in this case, the embargo was declared *before* the cargo was shipped and that, consequently, the possibility of frustration was not excluded.

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5 [2007] 1 Lloyd's Rep. 1.



### 18.3.3 Human Intervention on the Part of One or More of the Parties to the Contract

There can be no frustration where the relevant event has been caused by the deliberate act or omission of one of the parties to the contract or where such act or omission has contributed to the occurrence. Such conduct, which is often described as 'self-induced frustration', normally excludes the possibility of frustration.

For example, in the case of *Ocean Trawlers Ltd v Maritime National Fish*,<sup>6</sup> the English court was asked to consider whether a charter for a fishing vessel called the ST CUTHBERT was frustrated when it became illegal in the United Kingdom for fishing vessels to use otter trawls without a licence. The ST CUTHBERT did originally have such a licence but the charterers were subsequently able to obtain only three licences for the vessels that they chartered. They chose not to allocate one of these licences to the ST CUTHBERT and argued that the charter was frustrated by subsequent illegality. It was held that the frustration was self-induced and that the charterers could not rely on their own election not to allocate one of the licences to the ST CUTHBERT as justification for their failure to operate the charterparty.

However, where the relevant event is not the result of a deliberate act or omission on the part of one of the parties to the contract but is the result of the negligence of one or more of them, it is not so clear whether there can be frustration. However, it appears that so long as one or more of the parties is in a position to avoid the event but fails to do so, whether deliberately or negligently, this may be sufficient to exclude the possibility of frustration.

### 18.4 When is it Decided whether or not there is Frustration?

The question of whether or not there is frustration is decided as soon as practicable after the consequences of the event are capable of assessment. Therefore, if a reasonable person would conclude following a casualty and an assessment of the likely consequences that the vessel is likely to have to spend six months in dry dock for repairs then (depending on the duration of the contract) a court may conclude that the contract is frustrated. The fact that, subsequently, the vessel is able to leave the dry dock and resume service within three months is irrelevant. The contract has been frustrated in the meantime. The assessment must be made when the facts and the likely consequences are known and that assessment is not subsequently affected with the benefit of hindsight.

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<sup>6</sup> [1935] 51 Lloyd's Rep. 299.

## 18.5 Types of Frustration

A contract is normally held to be frustrated when further performance is considered to be:

- Impossible; or
- Illegal; or
- Substantially delayed.

### 18.5.1 Impossible Performance

A contract is not frustrated if it has merely become more difficult or even very difficult to perform. Impossibility means that it is not possible to perform and, if one party wishes to allege that there is frustration, that party must prove that it has taken all reasonable steps to avoid the frustrating event and its consequences and that, despite such efforts, it is still not possible to perform.

The classic example of impossibility of performance is where the chartered ship has become a total loss or a constructive total loss. However, if the intended cargo is destroyed before shipment, there is usually no frustration since it is normally possible for the charterer to obtain a substitute cargo of the same type. The charterer is under an absolute duty to procure for shipment a cargo of the agreed description and is not absolved from that duty even if the contemplated cargo has become unavailable as a result of factors that are outside his control. However, there may be frustration if the contract provides for the shipment of a specific cargo, not merely a cargo of a particular type (i.e. *this* cargo of chemical and not simply a cargo of chemical of this type) and the specific cargo has become unavailable through no fault of the charterer.

### 18.5.2 Supervening Illegality

It is an implied term of all contracts that they are to be performed in a legal manner. Therefore, if, after the contract has been agreed, there is a change in the law which renders performance of the contract illegal, there is usually frustration since thereafter *“the thing undertaken would, if performed, be a different thing from that contracted for.”*<sup>7</sup>

A contract can be frustrated if the supervening illegality arises under the law which governs the contract or under the law of the place or places of performance. For example, if war breaks out between the country of the flag of the vessel and the country to where the cargo is to be delivered, or which results in the owners or charterers of the vessel becoming enemy aliens, there would normally be frustration. Similarly, if the charter provides for the carriage of a cargo to a particular country but that country is subsequently made the subject of a UN enforced embargo

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<sup>7</sup> Per Lord Radcliffe in *Davis Contractors v Fareham*, [1956] AC 696 at 729.

recognised by the country of the vessel's flag or the country where the owners are domiciled, there would normally be frustration. Finally, a contract may be frustrated if the specified exporting or importing country declares without prior warning that it is reducing the annual export or import quota of the specified cargo.

### 18.5.3 Delay in Performance

To amount to frustration, the delay must be of very substantial duration in relation to the purpose of the charter, the overall contemplated period, and the remaining period of the charter. Therefore, the delay necessary to frustrate a time charter of long duration is likely to be greater than the delay which would be necessary to frustrate a short-term charter or a voyage charter, unless there were special circumstances. For example, if a vessel suffers a breakdown and needs to go into drydock for repairs which are likely to take three months to complete, then:

- In the context of a time charter for four months or a short voyage charter, the period of delay may well be sufficient to constitute frustration;
- In the context of a time charter for two years which still has 15 months to run, the delay is probably not sufficient to constitute frustration;
- However, in the context of a time charter for a special and urgent trade which still has 15 months to run, the delay may be sufficient to constitute frustration.

### 18.6 Insurance<sup>8</sup>

In many cases, one party to a contract may wish to allege that the contract is frustrated whilst the opposing party will wish to argue that the contract remains in full force. Therefore, an allegation of frustration will often give rise to dispute and potential litigation. The costs of such litigation may be recoverable by each party pursuant to its Defence cover provided that the relevant party has notified its Defence insurers at an early stage of the dispute and has complied with any directions that may be made from time to time by such insurers.<sup>9</sup>

### 18.7 Claims Management

Frustration is a notoriously difficult concept. Much depends on the facts and on an assessment of the impact that the particular event is likely to have on the performance of the contract. It is also notoriously difficult to make an objective assessment of the relevant issues. Therefore, such a combination of difficulties can prove to be extremely dangerous since a wrong decision can have dramatic repercussions. For example, if a party decides that a contract is frustrated and that, consequently, it is not going to perform the contract any further, it runs the risk that a court or tribunal may disagree in due course with the result that that party may be

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<sup>8</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>9</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV Rule 65 (Defence Cover)).

held to have repudiated the contract and become liable for substantial damages for which there may be no insurance cover. Therefore, it is very important that legal advice is taken before a contract is treated as frustrated and that full enquiry is made at an early stage of the impact that the particular event is likely to have on the continued viability of the contract.<sup>10</sup>

### **18.8 Case Study**

The CAPTAIN GEORGE K<sup>11</sup> was voyage chartered to carry a cargo from Mexico to India. The contemplation of the parties was that the ship would proceed via the Suez Canal which was open at the time that the fixture was negotiated and there was no suggestion at that time that it might be subsequently closed. However, by the time that the ship arrived at the Northern entrance to the Canal the master was informed that the Canal had been closed following the recent outbreak of war between Israel and Egypt. Therefore, the shipowners notified the charterers that the charter had been frustrated and that, if the ship was to proceed to India, it would have to sail back through the Mediterranean and around the Cape of Good Hope resulting in an increased sailing distance of 18,400 miles for which the shipowners claimed additional freight of approximately USD 68,000. The charterers did not accept that the charter was frustrated and argued that the shipowners were obliged to proceed on the longer route in order to earn the freight that was agreed in the charter.

The dispute was initially referred to arbitration and the umpire held that *“no man of commercial sense would say that the voyage the vessel performed after she anchored off Port Said was comparable with what her owners had contracted she should perform when she left Mexico.”* However, the award was appealed to the English court and the judge held that although he personally had come to the view that the voyage actually performed was fundamentally different from that which the parties had originally contemplated in the charter with the result that the charter would appear to have been frustrated, he was bound by the decision of the Court of Appeal in *The Eugenia*<sup>12</sup> and must find that the charter was not frustrated merely because of the delay and extra cost.

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<sup>10</sup> See Chapter 18.6 above.

<sup>11</sup> [1970] 2 Lloyd's Rep. 21.

<sup>12</sup> See footnote 2 above.

## Chapter 19

# Law and Jurisdiction

### 19.1 Introduction

The shipping industry is perhaps the most international of all industries. However, the industry needs to be regulated and the major problem which the world has always faced is that there is no one system of law which is binding on all countries and on all people who are engaged in international trade. For many centuries the shipping community has had to make do with a patchwork of legal rules which differ according to the country or the court in which the particular issue is determined. Therefore, it was difficult traditionally to draw up contracts since an agreement drawn up in one country might be construed completely differently in another country. Furthermore, insurers have found it difficult to rate the premium which should be charged for a voyage since the liability for incidents occurring en route may differ depending on the jurisdiction where the liability for the incident is determined. Lastly, even when one party has a perfectly good claim, it may be difficult for that party to recover its losses since the defendant might be resident in another state which does not recognise the jurisdiction of the court which is adjudging the claim and which will not enforce its judgement in due course. The result of all this is confusion and higher costs to the detriment of all concerned.

The question is further complicated by the fact that a distinction needs to be drawn between the jurisdiction where the claim is to be determined and the law that should be applied in adjudicating the claim. It does not follow automatically if a claim is determined by a court or arbitration tribunal in country A that the law of country A will necessarily be the law that governs the dispute. The law of most countries requires its courts or tribunals to consider whether the claim should be determined by a foreign law and if necessary to apply that law. Therefore, a dispute may be heard by the courts of country A but that court may apply the law of country B. A classic example may be

where the courts of country A are asked to resolve a dispute arising out of a contract which is subject to the law of country B. This requirement to consider the possible application of foreign law is normally referred to as the conflicts of law issue.<sup>1</sup>

Therefore, the twin issues of jurisdiction and the applicable law constitute a fundamental problem and all subsequent attempts to improve the situation have had to tackle the various difficulties which are inherent to international trade. Consequently, even today, it is necessary whenever a claim arises to consider a patchwork of:

- 1 International conventions;
- 2 Regional conventions;
- 3 National laws; and
- 4 Local laws.

Whilst international conventions have played a major part in the regulation of international shipping, large numbers of countries have either not ratified some of these conventions or not adopted the conventions into their domestic law, and there are large areas of commercial activity which are not subject to the conventions for a number of reasons. Therefore, it is still necessary in most situations to have regard to the domestic law of the particular country where a dispute is being determined. This is particularly so in the case of the United States since it has traditionally been the policy of the USA not to ratify or accede to international trade or shipping conventions but to implement its own national and state laws. For example, whilst the Carriage of Goods by Sea Act 1936 (COGSA 1936) of the USA adopts many of the provisions of the Hague Rules into US law, it does so subject to some important amendments. Similarly, the United States has not adopted any of the CLC, Bunker or HNS pollution conventions but has implemented its own very different Oil Pollution Act (OPA 90) as well as the Comprehensive Environmental Response, Competition and Liability Act (CERCLA) 1980 in relation to HNS cargoes.<sup>2</sup>

## 19.2 Forum Shopping

The choice of law and jurisdiction can have a major impact on the merits of a claim particularly since certain aspects of a dispute may be heard in one jurisdiction whilst other aspects must be heard in another jurisdiction. For example, the merits of a claim may be determined in country A whilst the shipowner's right to limit his liability in respect of any judgement which may be given in country A may be determined in country B. Limitation rights around the world are far from uniform.<sup>3</sup> Most countries have now adopted the 1976 Limitation Convention, and many of those countries have subsequently adopted the 1996 Protocol to the 1976 Convention which

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1 See Chapter 19.10 below.

2 For more detailed commentary see Chapter 12.4.1.3 (Pollution Claims).

3 For more detailed commentary see Chapter 21 (Limitation of Liability).

increases the limitation amounts substantially.<sup>4</sup> However, there are still substantial parts of the world where neither the 1996 Protocol nor the 1976 Limitation Convention have been adopted. As a result, some countries still give effect to the lower limits of the 1957 Limitation Convention, whilst other countries are not parties to any international convention whatsoever and give effect to their own national legislation, which may or may not provide for limitation.<sup>5</sup>

Although there are many bi-lateral and multi-lateral treaties that purport to regulate jurisdiction for claims, there is no universal agreement. Consequently, countries are often free to decide for themselves whether or not they will accept jurisdiction for a particular claim. This lack of uniformity may result in a claimant attempting to proceed in a country that gives him the maximum advantage whereas a defendant will prefer to proceed in a country that provides the claimant with the least advantage. In many instances, a party derives a tactical advantage by being the first to establish jurisdiction in the country of his choice and he may therefore, rush to establish his claim there as soon as possible. This process is called 'forum shopping'.

For example, a party who fears that he may face a claim in due course but wishes to ensure that the claim is brought in a jurisdiction that is favourable to him, may prefer not to wait until the claimants commence proceedings in the jurisdiction of their choice in due course but to take the initiative and commence proceedings in the jurisdiction of his choice in order to apply for a declaration of non-liability. Alternatively, a claimant may decide to commence *in rem* proceedings against a vessel that is present in the territorial waters of a country.<sup>6</sup> Once jurisdiction has been established in this fashion, the courts of that country will have to decide whether or not to retain jurisdiction or relinquish it in favour of some other foreign court. This question is, however, complicated by many factors and the court in question will have to weigh up all the circumstances in order to decide whether or not to retain or reject the proceedings. In many circumstances, the court will be obliged to reject the proceedings (e.g. where the claim is subject to arbitration)<sup>7</sup> but where the court has a discretion, it must consider all the facts in order to decide whether the case should remain in that jurisdiction or whether the interests of justice dictate that it should be heard in another jurisdiction. This issue is considered further in Chapter 19.7 below.

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4 A list of which countries have adopted which convention can be accessed on the IMO website at: <http://www.imo.org/About/Conventions/StatusOfConventions/Pages/Default.aspx>.

5 For commentary on limitation rights in the United States see Chapter 29.2 of the *Gard Handbook on P&I Insurance*, 5th edition and Part B Chapter 42 of *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, Informa, 4th edition, 2005.

6 See Chapter 19.4 below.

7 For more detailed commentary on arbitration see Chapter 17.2 (Claims Resolution Systems).

### 19.3 Jurisdiction for Interim Security Applications

A claimant will normally wish to be sure that if his claim succeeds in due course he will be able to enforce his judgement or award. However, a claim can take many years to be finalised and in the meantime, the defendant may have gone out of business or become bankrupt or his only asset (the ship) may have been lost. Therefore, a claimant will wish at an early stage to ensure that he has security for the claim.

The laws of most countries allow applications to be made in the courts of that country for the provision of security even though the merits of the claim must clearly be adjudicated in another jurisdiction. This right is also recognised by Article 7.2 of the International Convention for the Unification of Certain Rules Relating to the Arrest of Sea-Going Ships 1952 (The 1952 Arrest Convention) and Article 2.3 of the International Convention on the Arrest of Ships 1999 (The 1999 Arrest Convention). Where the claim lies against a ship or its owners claimants are normally given the right, once they have satisfied the court that they have a 'good arguable case' against the ship, to arrest the ship whilst it is within the territorial limits of that country to obtain security to satisfy any judgement which may be made in due course either by that court or a foreign court or, if this is not provided, to sell the ship by order of the court and to utilise the proceeds to satisfy the claim.<sup>8</sup> Alternatively, if the claim lies against someone other than the shipowners, the courts of most countries are prepared to issue an interlocutory (i.e. interim) injunction preventing the defendant from removing its assets from that country until satisfactory security has been provided. This form of injunction is normally referred to as a Mareva injunction or a freezing injunction.<sup>9</sup>

In both cases, the court granting the arrest or interim injunction will normally stay further proceedings once security has been provided but may keep the proceedings in abeyance in case it becomes necessary in due course to resurrect the proceedings in order to enforce any security that has been given to the claimant.

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8 For more detailed commentary see Chapter 24.6.1 (Security Enforcement Measures).

9 For more detailed commentary see Chapter 24.6.2 (Security Enforcement Measures).



### 19.4 *In Rem* Jurisdiction

Generally, the defendant in any litigation is either the individual or the corporation that has caused the loss. Both of these are considered to be 'persons' in law and the claim against them is accordingly, called a claim *in personam*. Traditionally, this was also the position in the case of maritime law. However, this caused a problem since the 'person' who caused the loss or damage (e.g. the carrier or shipowner) was often either not present within the jurisdiction of the court at all, or was present within the jurisdiction for only a limited time, and would be beyond the jurisdiction of the court as soon as the ship sailed outside the territorial waters of that country. Therefore, claimants found that by the time they discovered their claim, they had no satisfactory means of pursuing that claim since the defendant had escaped.

Therefore, the courts of most maritime countries are given the right to bring proceedings against the ship itself and to attach or arrest the ship whilst it is within its territorial waters. This form of proceeding is called an action *in rem* since it is an action against 'a thing' (i.e. the ship) not the person. *In rem* jurisdiction can be brought against either the ship that is responsible for the incident or against any of her sisterships. A sistership is one which is in the same ownership as the ship against which the claim is brought. However, different countries take different views as to what is meant by 'the same ownership'. In most countries there must be a commonality of shareholding, i.e. 100 per cent of the shareholding in each ship must be the same. However, other countries (an important example being South Africa because of its geographical location) take a more liberal view and consider that ships are sisterships if the owning companies are subject to common accounting or operational or management arrangements. Indeed, the South African court is prepared in many instances to investigate the shareholding of companies in order to ascertain whether there is indeed any evidence of such control.

Once *in rem* proceedings have been issued they remain in full force until the vessel or any of her sisterships enter the territorial waters of the country in which the proceedings have been commenced. In other words, they create a statutory lien which 'follows the ship' and remain in force despite any subsequent sale or transfer of that property.<sup>10</sup> Where common control is found to exist the vessels will be deemed 'associated' ships and so open to arrest for the debts or liabilities of the other despite being owned by different companies. Australia offers a similar regime with its concept of 'surrogate' ships.

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<sup>10</sup> For more detailed commentary see Chapter 24.5 (Security Enforcement Measures).

## 19.5 Jurisdiction by Agreement

Traditionally, parties to international agreements have preferred wherever possible to agree on the jurisdiction to which any dispute between them is to be referred. Therefore, international contracts including contracts such as charterparties, bills of lading etc., will normally include law and jurisdiction or arbitration clauses which specify where a dispute is to be resolved and the law that is to govern the dispute. In some cases the clause will say that a particular court or arbitration tribunal will have exclusive jurisdiction whereas other types of clauses will provide options depending on the nature of the dispute. There is obviously much good sense in this approach and in general, the approach adopted by the international community has been to support and enforce the parties' wishes unless it is considered necessary to do otherwise on the basis of public policy or a particular convention.<sup>11</sup> Therefore, the parties may not have freedom of choice in all circumstances.

### 19.5.1 Arbitration<sup>12</sup>

It has been the public policy of most countries for many years to support arbitration if that is the means by which parties wish to resolve their disputes. This policy is given further impetus by The New York Convention on the Recognition and Enforcement of Arbitral Awards 1958 which obliges the courts of countries that are parties to the convention to stay any proceedings which have been commenced in their courts if the parties have agreed in writing that the relevant dispute should be resolved by arbitration and an application for a stay is made by one of those parties. The New York Convention also provides that the courts of countries that are parties to it must enforce any arbitration award that has been made in any other convention country unless such enforcement is contrary to the public policy of that country.

### 19.5.2 Alternative Dispute Resolution (ADR) Systems<sup>13</sup>

It has become more common in recent years for parties to wish to resolve disputes by the use of innovative ADR systems which are considered to avoid the cost and delays which have increasingly come to plague traditional resolution systems such as arbitration and court litigation. Therefore, organisations such as BIMCO and the London Maritime Solicitors Group have produced standard clauses which enable the parties either to arbitrate or to use ADR as the circumstances require without prejudice to their wider rights. It is also the public policy of most countries to support such systems if that is the means by which parties wish to resolve their disputes.

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11 For example, a choice of jurisdiction clause may not be conclusive if the Hamburg Rules are applicable. For further commentary see Chapter 3.2.9 (Cargo Claims).

12 For more detailed commentary see Chapter 17.2 (Claims Resolution Systems).

13 For more detailed commentary see Chapter 17.3 (Claims Resolution Systems).

## 19.6 International Conventions

However, if a claim relates to a non-contractual issue (e.g. collisions, wreck removal, pollution etc.) contractually agreed law and jurisdictional clauses will be inapplicable. The most effective method of regulating jurisdiction in such cases is by international convention. However, for international conventions to come into force the draft convention must be ratified (or acceded to) by the required number of countries specified in the convention and, even then, the convention is binding only as between those countries that have ratified them or acceded to them.

The act of ratification or accession is in reality a promise by the country doing so that it will make the convention part of the domestic law of that country. Therefore, each country must then introduce its own domestic statute to make the convention binding as part of its domestic law.<sup>14</sup> Thereafter, whilst various international bodies may subsequently administer the mechanics of the convention, enforcement is left to the courts and law enforcement officers of that country.

### 19.6.1 International Conventions which Regulate Jurisdiction

Article 92 of the United Nations Convention on the Law of the Sea (UNCLOS) provides that the country of the ship's flag shall have jurisdiction in relation to events which occur on the high seas (i.e. in international waters) unless the particular event is regulated by an international convention or agreement which seeks to regulate jurisdiction in specific situations.<sup>15</sup> However, in the majority of cases jurisdiction is in fact governed by such specific conventions or agreements. There are two types of conventions or agreements which are normally relevant in this regard:

- Regional conventions which regulate jurisdiction generally; and
- International conventions which regulate jurisdiction in particular cases.

#### 19.6.1.1 Regional Conventions which Regulate Jurisdiction generally

The most relevant convention for those carrying on business in Europe is the European Regulation (EC) 44/2001 of 22 December 2000 on Jurisdiction and Enforcement of Judgements in Civil and Commercial Matters (The EU Regulation). This convention is binding between the countries of the European Union whilst issues between the countries of the European Union and the EFTA countries (i.e. Iceland, Norway and Switzerland) are regulated by the EFTA Convention on Jurisdiction and Enforcement of Judgements in Civil and Commercial Matters (commonly known as the Lugano Convention). Both conventions are very similar and provide that, subject to certain exceptions, a claim for a civil or commercial matter must be brought in the court of the state where the defendant is domiciled.

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14 For example, the Hague-Visby Rules have become part of the law of the United Kingdom by means of the Carriage of Goods by Sea Act 1971 (COGSA 1971) of the UK.

15 See Chapter 22.3.1 (Maritime Regulation and Compliance).

However, Article 71 of the regulation provides that the regulation will not override the provisions of other international conventions to which the member states are parties and which govern jurisdiction in specific situations.<sup>16</sup>

Furthermore, the claimant is given the option in certain cases to bring the claim in a jurisdiction other than the one in which the defendant is domiciled. For example, a claim in tort may be brought in the courts of the state where the damage occurred and a claim in contract may be brought in the state where performance was to take place. Lastly, in certain circumstances, the parties may be held to be bound by a jurisdiction clause in a contract specifying that the courts of a particular country will have exclusive jurisdiction.

The provisions of the conventions apply to court proceedings whether they are *in personam* or *in rem* but do not apply to arbitration. However, the precise scope of the arbitration exclusion is a matter of some doubt. For example, the European Court has held in the controversial case of the *Front Comor*<sup>17</sup> that EU Regulation 44/2001 is applicable when a party ignores an arbitration clause and pursues the claim before a court in another EU country, thereby entitling that court to rule on whether the arbitration clause is binding on the parties and forbidding a court in any other EU country from interfering with such process by the grant of an anti-suit injunction.<sup>18</sup> However, the English court has subsequently held by two separate judgements in the same case that, notwithstanding the court proceedings in the other EU country, arbitrators in London are not debarred by the EU Regulation from firstly, making an award declaring that the other party to the arbitration agreement is not liable to the party that has commenced the court action in the other EU country,<sup>19</sup> and secondly, from making an award holding that party liable in damages for breach of the agreement to arbitrate.<sup>20</sup>

### **19.6.1.2 International Conventions which Regulate Jurisdiction in Particular Cases**

There are a number of international conventions that regulate jurisdiction for particular kinds of maritime disputes as between the countries that have ratified those conventions. It is not possible to list them all but the most significant are:

- The International Convention on Certain Rules Concerning Civil Jurisdiction in Matters of Collision 1952 (The 1952 Collision Jurisdiction Convention) which regulates jurisdiction in relation to collisions;

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<sup>16</sup> The most likely conventions are the 1952 and 1999 Arrest Conventions, the 1952 Collision Jurisdiction Convention and the Hamburg Rules. See Chapter 19.6.1.2 below.

<sup>17</sup> Case C-185/07. The facts are described in Chapter 19.12 Case Study.

<sup>18</sup> See Chapter 19.8 below.

<sup>19</sup> [2012] 1 Lloyd's Rep. 398.

<sup>20</sup> [2012] 2 Lloyd's Rep. 103.

- The International Convention for the Unification of Certain Rules relating to the Arrest of Sea-Going Ships 1952 (The 1952 Arrest Convention) which regulates jurisdiction in relation to the arrest of ships;
- The Convention on the Recognition and Enforcement of Arbitral Awards, New York, 10 June 1958 which regulates jurisdiction in relation to arbitration;
- The United Nations Convention on the Carriage of Goods by Sea 1978 (The Hamburg Rules) which regulate jurisdiction in relation to international carriage of goods by sea;
- The Athens Convention on the Carriage of Passengers and their Luggage by Sea 1974 (The Athens Convention) which regulates jurisdiction relating to the carriage of passengers.

In some cases there would appear to be a conflict between the provisions of two or more conventions which may apply in a particular situation. It is not possible to consider each and every possible conflict which may occur but in general terms, the more general convention normally gives way to the more specific convention.

For example, Article 71 of the EU Regulation provides that:

*“This Convention shall not affect any conventions to which the Contracting States are parties and which, in relation to particular matters, governs jurisdiction or the recognition or enforcement of judgment.”*

### **19.7 ‘Threshold’ and Final Jurisdiction**

The *in rem* jurisdiction of a country normally gives its court jurisdiction over a ship once that ship enters the territorial waters of that country. This form of ‘initial’ jurisdiction is normally called ‘threshold jurisdiction’. There may also be ‘threshold jurisdiction’ when a claimant succeeds in bringing *in personam* proceedings against a person who is within the territory of that particular country. In both cases, that court is considered to be the court that is first seized of the claim. That court may consider its jurisdiction to be either final, in which case it will then proceed to determine the merits of the case, or merely provisional, in which case the court may direct that the merits should be heard by another tribunal or by another court in another country. However, in the latter event, the court will normally maintain the provisional proceedings and any arrest until satisfactory security has been provided for any award or judgement that may be given in due course by the other tribunal or court. The question of whether or not there is jurisdiction (whether ‘threshold’ or final) depends largely in practise on the view that is taken by the court which is first seized of the claim. The courts of some countries are more ready than others to assume final jurisdiction.

When deciding whether or not it has final jurisdiction the court first seized of the claim will consider firstly whether it has the right to deal with the claim on a provisional basis. If it decides that it does not have jurisdiction even on a provisional basis then the proceedings go no further and they are dismissed. However, if the court decides on a provisional basis that it has jurisdiction, then it must go on to consider whether there is any other rule which either obliges it to stay the proceedings or which gives it a discretion to do so. Lastly, if it decides that it should dismiss or stay the proceedings, it must consider whether the dismissal or stay is final and unconditional or alternatively, temporary or conditional in order to protect any rights which have accrued as a result of the proceedings, e.g. the preservation of any relevant time limit. In deciding these various issues the court will consider the provisions of any international conventions or treaties which are binding on it and also the provisions of its own private international (conflicts) law.

In some instances the court first seized of the claim will consider that it has no option but to stay proceedings whereas, in other circumstances, it may conclude that it has a discretion whether to stay or maintain jurisdiction.

### **19.7.1 Obligatory Stay of Proceedings**

If the country of the court which is first seized of the claim has ratified a convention which provides for a form of mandatory jurisdiction, the court has no alternative but to stay its own proceedings if they are brought contrary to the provisions of the particular convention.

In some instances, the court must stay the proceedings of its own volition regardless of whether any of the parties make an application to that effect. For example, if the EU Regulation applies, then the court of an EU country must normally stay the proceedings in favour of any other jurisdiction specified by the regulation of its own volition. However, in other instances, the court cannot act on its own volition but must stay the proceedings only if an application is made by one of the parties. For example, if the parties have agreed to refer a dispute to arbitration under an agreement in writing which is subject to the New York Convention on the Recognition and Enforcement of Arbitral Awards 1958, then the court must normally stay its own proceedings and refer the dispute to arbitration if an application is made to it to do so by one of the parties to the arbitration agreement.

## 19.7.2 Discretionary Stay of Proceedings

It is necessary to consider two different situations in this regard:

- where there is an agreed jurisdiction clause; and
- where there is no agreed jurisdiction but it is argued that 'threshold jurisdiction' is not the 'proper' jurisdiction (i.e. *forum non conveniens*).

### 19.7.2.1 Where there is an agreed jurisdiction clause

As a general rule, but subject to important exceptions, the courts of most countries will recognise and enforce an agreed jurisdiction clause. However, recognition of a jurisdiction clause depends upon the court being satisfied that there is indeed agreement to confer jurisdiction on any particular court. Therefore, the court will examine whether the particular clause is valid and binding. However, this seemingly simple exercise can be quite complicated.

When the contract contains an express clause which provides that it is subject to a particular law the question can normally be answered with reference to that law. However, if the contract has no express law provision, or if one of the parties challenges the effectiveness of the contract on the ground that there is no consensus between the parties, or on the ground that the contract is void or voidable, or has been terminated by frustration, the question is not easy to answer. In general, the question whether a jurisdiction clause is effective depends on the law by which that clause would be governed assuming, on a provisional basis simply for this purpose, that the term is valid. For example, if the contract contained an English jurisdiction or arbitration clause, the English court would employ English law to determine if the clause was valid. Similarly, if the contract contained a Norwegian jurisdiction clause the English court (considering the issue at the 'threshold' jurisdiction stage) would consider whether it was valid under Norwegian law.

### 19.7.2.2 Where there is no Agreed Jurisdiction Clause but it is Argued that 'Threshold Jurisdiction' is not the 'Proper' Jurisdiction (i.e. *Forum Non Conveniens*)

Once the court is satisfied that it has 'threshold jurisdiction' and that it is not obliged by international convention to stay the proceedings, the court will normally continue with those proceedings unless there are 'special countervailing factors' or 'good reason' not to do so. In other words, the court will consider whether the court of another country is a more appropriate court to hear and adjudicate on the merits of the claim. If it concludes that the claim can be dealt with more appropriately in another country it may stay its own proceedings on the basis that it is not the convenient or appropriate jurisdiction, i.e. that it is a '*forum non conveniens*'.

In considering whether a particular court is a '*forum non conveniens*' different courts may consider different factors to be relevant and it is difficult to give a precise account of what, subjectively, the courts of different countries consider to be relevant. However, in most cases, the following factors are considered to be relevant:

- a** where is the evidence of fact situated or more readily available;
- b** does the law of the foreign court apply and, if so, does it differ in any material respect from the law of the country that is first seized of the claim;
- c** how closely is either party connected with another country;
- d** does the defendant genuinely desire trial before the foreign court, or is it only seeking procedural advantages;
- e** would the plaintiff be prejudiced by having to sue in the foreign courts because he would: (i) be deprived of security for his claim; (ii) be unable to enforce any judgment obtained; (iii) be faced with a time bar; or (iv) be unlikely for political, racial, religious or other reasons to get a fair trial.

The limitation of liability is another important issue to consider in the context of jurisdiction since different countries apply different limitation rules and amounts depending on the international limitation convention to which they are a party or, indeed, on whether they are parties to any such convention.<sup>21</sup> The traditional rule is that a party who wishes to start a limitation action may do so in the country of his choice notwithstanding the fact that the merits of the claim may be determined by a court in a different country. Therefore, the merits could be decided in country A and the courts of that country could render a judgement holding a defendant liable for, say, USD 1 million. However, if that claim is merely one of many claims arising as a result of one occurrence and the totality of those claims (including the judgement rendered in country A) exceed the ship's limitation fund in country B, the shipowner may be entitled to start a limitation action in country B and thereby limit his liability to all such claims including his liability for the judgement rendered in country A. In such circumstances, the court of country A may either proceed to determine the merits of the claim knowing that limitation will be determined in another jurisdiction, or stay the proceedings on the merits if it believes that all aspects of the claim (i.e. merits and limitation) can be dealt with more conveniently and appropriately in country B. The decision taken will depend on the particular facts of the particular case and it is difficult to give any consistent guidance in that regard.

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<sup>21</sup> For more detailed commentary see Chapter 21 (Limitation of Liability).



## 19.8 Anti-Suit Injunctions<sup>22</sup>

Quite frequently, a court in country A will decide that it should properly have jurisdiction (based frequently on the fact that the parties have agreed in the contract that a dispute is to be resolved according to the law and jurisdiction of country A) but nevertheless, one of the parties commences proceedings in country B, and a court in country B is prepared to entertain those proceedings. In such circumstances, the party who wishes to proceed in country A may apply to the courts of that country for an injunction restraining the other party from continuing to pursue the claim in the courts of country B (i.e. an anti-suit injunction) on the grounds that such proceedings are in breach of the agreed law and jurisdiction clause. In recent years, it has become quite common for courts to grant such injunctions and if they do so, a party who ignores the injunction runs the risk of being in contempt of court and subject to a substantial fine.

However, the use of anti-suit injunctions has been criticised by the European Court in cases where the competing proceedings are in countries which are members of the European Union and subject to the EU Regulation.<sup>23</sup> The European Court takes the view that even if it appears reasonably clear from an objective standpoint that the proceedings in country B have been started in breach of the agreed jurisdiction clause, the principle of mutual trust between member states requires the court in country A to leave it to the court in country B to reach its own view as to whether or not it should retain jurisdiction. Consequently, the European Court held in the case of the *Front Comor* that the English court was not entitled to issue an anti-suit injunction to prevent a party from proceeding in the Italian court contrary to the terms of an agreed arbitration clause since it was for the Italian court itself to decide whether or not it had jurisdiction.<sup>24</sup> However, the anti-suit injunction remains an important remedy in cases where the country first seized of the proceedings (i.e. country B in the above example) is not in the EU.

## 19.9 US Jurisdiction

The approach of the United States to jurisdictional issues follows many of the principles discussed above. However, there are important differences and it is not possible in this publication to comment on these in detail. Therefore, whilst the comments that are made below are intended to give a general overview, it is important that specific advice is taken from qualified US lawyers in relation to specific cases.

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<sup>22</sup> For more detailed commentary on injunctions see Chapter 23.7 (Remedies).

<sup>23</sup> See Chapter 19.6.1.1.

<sup>24</sup> See Chapter 19.6.1.1.

### 19.9.1 *In Rem* and *in Personam* Jurisdiction

Under the US constitution, the federal courts have exclusive jurisdiction for admiralty matters except for a limited number of cases (such as seamen's personal injury claims) which can be brought in state courts under the 'savings to suitors' clause. This has certain important implications including, in particular, the right of a seafarer to demand a trial by jury under state law procedures which is not available in federal courts in relation to other admiralty matters.

The US federal courts are entitled to exercise *in rem* jurisdiction (otherwise known as the Rule C procedure) to arrest ships in the territorial waters of the United States for claims that are subject to a maritime lien including, for example, claims for unpaid ship repairs or agency fees, or for claims arising as a result of a tort such as a collision. However, *in personam* jurisdiction can be established only if the constitutional threshold standard of 'minimum contacts' has been established. This means that a party must have engaged in certain minimum types of activity either within an individual state, or within the United States as a whole. For example, a party must have 'done business' within a state or otherwise sought to avail itself of the privilege of doing business within a state or states. US courts are also able to exercise quasi-*in rem* jurisdiction (better known under its procedural moniker, 'Rule B') to attach property belonging to the defendant in the United States (such as freight or hire held in the US bank account of an agent, or bunker fuel in a shore tank) if the defendant cannot be found within the jurisdiction.

### 19.9.2 Foreign Jurisdiction and Arbitration Clauses

The US Supreme Court case decisions<sup>25</sup> support the enforcement of such clauses both generally and, in particular, in maritime cases except in those limited circumstances when an objecting party can clearly show that a trial in the contractually agreed forum would be so difficult and inconvenient that it would in effect deprive that party of their day in court.

### 19.9.3 *Forum Non Conveniens*

US courts may decline jurisdiction if the defendant establishes an alternative forum that is considered to be more convenient after balancing factors similar to those mentioned in Chapter 19.7.2.2 above. This occurs most often in cases that involve multiple venues and/or nationalities such as, for example, when a non-US seafarer is injured in the United States and brings a legal action in the United States. If the

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25 *M/S Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1 (1972) – towage contract; *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991) – cruise passenger ticket; *Vimar Seguros y Reaseguros, S.A. v. M/V Sky Reefer*, 515 U.S. 528 (1995) – bill of lading.

claim is not brought pursuant to any contractually agreed jurisdiction clause, the US court may subsequently decide that the courts of another jurisdiction, such as that of the residence of the seafarer, is, on balance, a better place to adjudicate the dispute.

## 19.10 The Governing Law

It is natural and inevitable that the court that is seized of the claim will initially consider the matter from the standpoint of its own local law. However, the public policy of most (but not all) countries is to recognise the integrity of foreign systems of law and to apply foreign law rather than its own law in appropriate circumstances. However, in deciding whether it is appropriate to apply foreign law, the court will be guided by that country's private international law (more popularly known as its 'law of conflicts'). Such laws of conflicts will have detailed provisions specifying in what circumstances, and to what extent, the local law must give way to the foreign law.

### 19.10.1 Contractual Disputes

Traditionally, most countries have resolved questions relating to the applicable law for contractual agreements (the *lex contractus*) by reference to a series of rebuttable presumptions which have been developed by the courts over many years. Courts usually proceed on the basis that unless the governing law has been expressly identified in the contract, the contract shall be governed by the law of the country with which it is most closely connected. The determination of that issue normally involves a consideration of all the relevant facts and it can only be said that, ultimately, it depends on the objective assessment of the particular judge. However, a choice of arbitration in a particular country, or a reference to the exclusive court jurisdiction of a particular country, normally carries a strong implication that the law of that country is to apply.

If a court in the European Union is required to determine the applicable law it will be guided by the Convention on the Law Applicable to Contractual Obligations 1980 (The Rome Convention) which adopts, in effect, the same presumptions.

### 19.10.2 Non-Contractual Disputes

If the claim involves a non-contractual (i.e. a tort) claim which occurs within the territorial waters of a particular country, the likelihood is that the local court will have jurisdiction to determine the claim and will apply the domestic law of that country unless it is obliged to apply an international convention. When this question arises in a court in the European Union that court is obliged to apply Regulation (EC) No 864/2007 on the law applicable to non-contractual obligations (Rome II) whether the incident occurs within the territorial waters of an EU country or within the territorial waters of a non-EU country. Rome II also proceeds on the premise that the applicable law is that of the country where the damage occurs.

However, the matter is more complicated if the event (e.g. a collision) occurs in international waters since no domestic law will then be applicable. Various attempts have been made to find a solution to this problem through the medium of international conventions. However, such efforts have not been totally successful. For example, whilst The International Convention On Certain Rules Concerning Civil Jurisdiction In Matters Of Collision 1952 (The 1952 Collision Jurisdiction Convention) provides useful guidance in that regard, that convention has not been ratified by many countries. However, the 1952 Arrest Convention<sup>26</sup> has been ratified by many more countries and that convention entitles a claimant to arrest a ship which is flying the flag of one of the countries that have ratified the convention in any other country that has done so in respect of claims for damage or personal injury caused by that ship or any of its sisterships. Article 7 of the convention goes on to provide that the courts of the country where the arrest has been made shall also have jurisdiction to determine the case upon its merits if the domestic law of that country allows the local courts to do so or if:

- The claimant has his principal place of business in that country; or
- The claim arose in that country; or
- The claim concerns the voyage during which the arrest is made; or
- The claim arose out of a collision or other circumstances which are subject to the 1910 Collisions Convention; or
- The claim is for salvage; or
- The claim arises under a mortgage.

However, Article 7 also allows the involved parties to refer determination of the merits of the claim to another jurisdiction of their choice. Therefore, in the event of an incident such as a collision occurring on the high seas, it is normally necessary for the owners of the ships and other property or persons involved and their insurers to discuss and negotiate at an early stage a mutually acceptable jurisdiction and governing law for the non-contractual claims that will arise as a result of such an incident. If this is not done then the ships involved may be vulnerable to arrest and consequent delays.

### 19.10.3 Proof of Foreign Law in the Local Court

If the court seized of the case has determined that foreign law is to be applied that does not necessarily prevent that court from continuing to exercise jurisdiction over the claim. If the court decides that it should retain jurisdiction then it will normally call for expert evidence to be given of the relevant principles of the foreign law. That

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<sup>26</sup> The 1999 Arrest Convention is now also in force but has hitherto been ratified by very few countries, Article 7.1 of the 1999 Arrest Convention provides that *"The Courts of the State in which an arrest has been effected or security provided to obtain the release of the ship shall have jurisdiction to determine the case upon its merits, unless the parties validly agree or have validly agreed to submit the dispute to a Court of another State which accepts jurisdiction, or to arbitration."*

evidence can be given either in person by a lawyer qualified to comment on the foreign law, or in the form of a written brief from such a person, or both. However, it should be appreciated that, in most cases, the judge will assume that the relevant principles of the foreign law are the same as those of the local law unless there is clear evidence to the contrary.

### 19.11 Claims Management and Insurance<sup>27</sup>

The choice of jurisdiction and/or governing law can often have a fundamental impact on the merits of a claim or a defence to a claim. In some cases it may not be possible to have any influence on these issues, whereas in others, quick action by one party may steer the case into a jurisdiction or a law regime which can substantially improve that party's position and adversely affect the other party's position. Therefore, parties should consider these issues at an early stage of any dispute and advice should be taken in conjunction with those insurers who have an interest in the claim from knowledgeable lawyers in alternative countries so that a considered assessment can be made and an agreed strategy can be reached as quickly as possible.

Contractual and non-contractual claims will involve both property insurers such as hull and machinery underwriters, cargo insurers, war risk insurers etc., and liability insurers such as P&I clubs, charterers' liability insurers etc. All such insurers will expect the assured to act as a prudent assured and take the appropriate steps to both minimise the insurers' liability and to preserve the insurers' rights in subrogation against third parties.<sup>28</sup> Therefore, the assured must consult the relevant insurer before taking any decision in that regard since a failure to do so may prejudice his rights under the relevant insurance policy.<sup>29</sup>

### 19.12 Case Study

The FRONT COMOR came into contact with a jetty in Sicily in August 2000. At the time of the incident the ship was chartered to the refinery which owned the jetty and the charterparty included an English law and London arbitration clause. The charterers commenced arbitration proceedings against the shipowners in London pursuant to that clause in order to claim its uninsured losses. However, pursuant to their rights in subrogation, the jetty's insurers brought a claim against the shipowners in the Italian courts under Italian law. Consequently, the shipowners sought and obtained an anti-suit injunction from the English court obliging the jetty owners to discontinue the Italian proceedings as they were bound to pursue their subrogated action before the London arbitration tribunal. This issue was referred to

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<sup>27</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>28</sup> For further commentary see Chapter 25 (The Fundamental Principles of Marine Insurance).

<sup>29</sup> See for example, the Gard Guidance to the Statutes and Rules (Guidance to Part IV (Defence Cover) and to Rule 82 (Obligations with respect to claims)).

the European Court which held pursuant to the European Jurisdiction Regulation (EC) 44/2001 that only the Italian court could decide whether the London arbitration clause or the Italian court had jurisdiction to adjudicate on the claim. Consequently, the anti-suit injunction ordered by the English court was unlawful and ineffective.

Notwithstanding this ruling, the shipowners continued with the London arbitration and obtained an award from the arbitrators finding that they had no liability to the insurers of the jetty for the damage caused by the FRONT COMOR. The shipowners then applied to and obtained a judgement from the English court upholding the award. Finally, the shipowners obtained a further judgement of the English court entitling them to claim damages for breach of the agreement to arbitrate which damages included, *inter alia*, the various costs that they had been obliged to incur in the Italian proceedings.

This issue has taken nearly 12 years to resolve.

## Chapter 20

# Letters of Indemnity (LOI)<sup>1</sup>

### 20.1 General Principles

A letter of Indemnity (LOI) is an enforceable promise made by A to B to hold B harmless against any liability, loss or damage that B incurs as a result of complying with a request made by A, i.e. "If you (B) do what I (A) ask, I (A) will hold you (B) harmless against any loss, liability or damage that you (B) may incur as a result of doing what I (A) ask."

In many cases such an indemnity is contained within the fabric of the contract itself. For example most charterparties have clauses such as the following:

*"The Master shall be under the orders of the Charterers as regards employment, agency, or other arrangements. The Charterers shall indemnify the Owners against all consequences or liabilities arising from the Master, officers or Agents signing Bills of Lading or other documents or otherwise complying with such orders, as well as from any irregularity in the Vessel's papers or for overcarrying goods."*

However, A might ask B to perform some task which is not within the boundaries of the contract. For example, A as charterer might request B as owner to perform a voyage which is outside the agreed charterparty geographical limits. In such circumstances, even if B were prepared to comply with A's request, B might be concerned that the charterparty indemnity might not be sufficient to protect B against liability, damage, loss or additional expenditure which B might incur as a result of complying with A's request. Alternatively, B might wish to increase the scope of the indemnity in consideration for his agreement to provide extra-contractual

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<sup>1</sup> For more detailed commentary see *Letters of Indemnity* by Richard Williams, Volume 15 of the Journal of International Maritime Law, 2009, *Letters of Indemnity – A Guide to Good Practice* by Mills and Roberts, Anchorage Press. See also *Letters of Indemnity at Shipment and Letters of Guarantee at Discharge* by Prof. William Tetley which can be accessed at <http://www.mcgill.ca/files/maritimelaw/letters.pdf>.

services. In such circumstances, parties will often agree to provide and accept an extra-contractual (i.e. free-standing) LOI. However, such LOI are themselves binding contracts albeit separate and collateral to the original contract. Therefore, the terms of the LOI may differ from the terms of the underlying contract and their enforceability or otherwise is considered separately from that of the underlying contract.

Therefore, LOIs are often offered in order to persuade one party to comply with a request made by another party to perform some task which that party is not obliged to perform under the contract, or to persuade a party to do something when it is unclear whether or not there is an obligation to do so and the parties do not wish to delay the performance of the contract (e.g. to sign clean bills of lading when there is an honest difference of opinion as to whether the cargo is indeed in apparent good order and condition).

In circumstances such as this, the LOI performs a useful purpose in that it provides commercial flexibility. It enables the contract to be performed without delay whilst at the same time protecting the rights of the party who is being asked to perform the requested task and who may suffer damage or loss or liability as a result of performing the requested task. Therefore, the law recognises the usefulness of the LOI in such circumstances and courts are, subject to one major exception, ready to enforce the terms of the collateral contract contained in such an LOI.

However, LOIs are also often used to facilitate acts which are fraudulent or illegal. For example, most international contracts of sale and/or letters of credit will provide that payment is to be made against a clean bill of lading (which is defined in Article 27 of UCP<sup>2</sup> 600 as "... one bearing no clause or notation declaring a defective condition of the goods or their packaging") or bills of lading of a specific date. Therefore, if the shipper were to produce claused bills<sup>3</sup> or bills which were differently dated then they would not be able to obtain payment of the price from the buyers. In such circumstances, sellers of cargo sometimes request carriers to release clean bills of lading even though the cargo is clearly not in apparent good order and condition or to release ante-dated or wrongly dated bills of lading in order to deceive the buyer and obtain payment of the price in circumstances in which they should not be able to do so. Such requests are often accompanied by the offer of an LOI which is intended to protect the carrier if he were to incur liability to the buyer as a result of releasing such improper bills. In such circumstances, the LOI is being used as a mechanism to persuade the carrier to fraudulently deceive the buyer, and if the carrier were to do so, he would be knowingly become part of the fraud. Therefore, courts are not usually prepared to enforce the terms of the LOI in such circumstances

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2 Uniform Customs and Practice for Documentary Credits.

3 I.e. bills of lading which state that the cargo is not shipped in apparent good order and condition.



for public policy reasons, i.e. the courts are not prepared to encourage frauds. Therefore, it is likely that a carrier who knows that he is fraudulently deceiving the buyer but has agreed, nevertheless, to accept an LOI, will find that he has no effective defence to the buyer's claim, has probably prejudiced his P&I cover and may well be unable to enforce the LOI against the shipper.

## 20.2 Circumstances in which LOI are Requested

LOI are normally requested in the following situations:

- Delivery of cargo without surrender of original bills of lading;
- Change of destination/deviation;
- Releasing clean or ante-dated bills of lading;
- Switch bills of lading;
- Commingling.

### 20.2.1 Delivery of Cargo without Surrender of Original Bills of Lading<sup>4</sup>

If a carrier does deliver cargo without production of the original bills of lading, he does so at his risk since such an act might well amount to an interference with the rights of the true goods owner to possess and dispose of the cargo.

At the end of the voyage the carrier has a duty to deliver the cargo to the party that is entitled to take delivery of it and if the cargo is delivered to the wrong party, it would technically be a conversion of the cargo rendering the carrier potentially liable for the full value of the cargo to the true cargo owner. For example the English court has held that:

*"... the owners are at the very least not bound to obey an order to receiver Y, if in fact it is receiver Z who is the owner of the cargo and entitled to delivery of it. By doing so the owners, and their master as joint tortfeasors, would be liable for the tort of conversion, whether or not they would also be liable to Z for breach of contract."*<sup>5</sup>

Therefore, if the carrier delivers the cargo to the wrong party, the carrier may:

- be liable to the party who is truly entitled to the cargo for the full value of the cargo that has been misdelivered; and
- have no protection under any of the exclusion clauses in the bill of lading; and
- have prejudiced his right to limit his liability; and
- have lost his P&I cover for liabilities arising as a result of the misdelivery.

<sup>4</sup> For more detailed commentary see Chapter 3.2.8.2.3 (Cargo Claims), the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 i and ii) and Chapter 5 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006.

<sup>5</sup> *The Sagona*, [1984] 1 Lloyd's Rep. 194.

However, the problem is that neither the carriers nor the master know the identity of the true owner of the cargo. Therefore, the rule has evolved that the carrier should give delivery to the party that produces the original bills of lading to him since bills of lading are documents of title,<sup>6</sup> and the production of such documents proves to the carrier that he is giving delivery to the correct party. The issue is complicated by the fact that bills of lading have traditionally been issued in sets of three which means that each original is a separate document of title. However, unless the carriers or the master have been put on notice of a dispute as to the ownership of the cargo, delivery against the surrender of one original bill of lading is normally sufficient to protect the carrier against an allegation of misdelivery.

A bill of lading ceases to be an effective document of title which can, by endorsement, transfer the right to obtain possession of the goods only when delivery of the goods has been made to the lawful holder of the bill of lading. However, a bill of lading can often take many months to reach the ultimate holder since it may have to pass through the hands of many sellers, buyers and their banks before it reaches the ultimate receiver. Therefore, a claim for unlawful delivery may not be made against the carrier for some appreciable time after the event. In such circumstances, a carrier may be reluctant to give delivery of the cargo until the original bills of lading have been surrendered to the ship. However, that will inevitably result in delay to the ship the cost of which will normally be for the account of the charterers in terms of either hire (in the case of time charters)<sup>7</sup> or demurrage<sup>8</sup> (in the case of voyage charters).

Charterers and cargo owners are reluctant to bear the cost of such delay since the identity of the lawful receiver is normally known to them and the delay is, therefore, usually caused purely by the administrative delay in processing the production of the bill of lading through banking channels. Therefore, charterers and/or cargo owners will often request the carrier to deliver the goods without production of the original bills and, in order to persuade the carrier to do so, offer an LOI purporting to indemnify the carrier if the carrier incurs liability as a result of doing so. However, whilst such LOI are frequently offered, a carrier is not obliged to deliver cargo without production of the original bills against an LOI unless there is either a custom of the trade to do so or unless the carrier has agreed to the inclusion in the relevant contract of carriage of a clause obliging him to do so.

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6 For more detailed commentary see Chapters 3.2.4 and 3.2.9.2.3 (Cargo Claims).

7 For more detailed commentary see Chapter 4.5.1.1 (Charterparty Claims).

8 For more detailed commentary see Chapter 4.5.1.2.2 (Charterparty Claims).

### 20.2.1.1 Custom of the Trade

A custom is normally enforced only when it is proved that all parties in that trade abide by the relevant procedure. Therefore, whilst there appears to be a practise in the tanker trade for cargoes to be delivered against a letter of indemnity, it has been found when tested in court that, whilst this is a common practice, it is not a universal practice and cannot therefore, amount to a custom.<sup>9</sup> However, different courts may take different views about the existence of customs, and advice should be taken from experienced lawyers in the particular port if carriers are requested to deliver cargoes there without production of the original bills of lading.

### 20.2.1.2 Charterparty Clauses

Most charterparties entitle the charterers to require the shipowners to sign and release bills of lading and oblige the charterer to indemnify the shipowners if they incur any loss or damage or liability when complying with charterers' orders. Even if there is no such express indemnity in the charter the shipowner is normally entitled to an implied indemnity if he complies with charterers' instructions, provided that "*such an act is not apparently illegal in itself, but is done honestly and bona fide in compliance with the (Charterers') directions ...*"<sup>10</sup> Therefore, charterers may often require shipowners to deliver cargoes without production of the original bills pointing out that the shipowners already have an indemnity which protects them in such circumstances.

However, the fact that a shipowner has a *right* to an indemnity under a charterparty or to demand a letter of indemnity from another party does not necessarily *oblige* the shipowner to deliver without production of a bill of lading if so required by the charterer. This distinction is very important since a shipowner may be very reluctant to have to rely upon an indemnity from a party of dubious financial standing. If the shipowner is to be obliged to deliver cargo without surrender of the original bills against whatever indemnity is available under the terms of the charter, it appears that the particular clause must be clearly worded to that effect. For example, the English court was asked to consider the relevance of the following clause in *The Houda*.<sup>11</sup>

*"The master ... shall be under the orders and directions of Charterers as regards employment of the vessel ... and shall sign Bills of Lading as Charterers or their agents may direct ...*

<sup>9</sup> It was recognised in *The Sagona*, [1984] 1 Lloyd's Rep. at 201 and in *The Houda*, [1994] 2 Lloyd's Rep. 541 that there was a practice in the oil cargo trade for cargoes to be delivered against a letter of indemnity and it was argued that the practice amounted to a custom. However, this argument was subsequently withdrawn since in order to constitute a custom, the practise must be universal and it was found on the evidence as a whole that whilst it was a common practice in the carriage of oil cargo, it was not a universal practise.

<sup>10</sup> See Chapter 4.5.2 (Charterparty Claims).

<sup>11</sup> [1994] 2 Lloyd's Rep. 541.

*Charterers hereby indemnify Owners against all consequences or liabilities that may arise from the master ... otherwise complying with Charterers' or their agents' orders, (including delivery of cargo without presentation of Bills of Lading ..."*

It was recognised that this wording did not go so far as to *oblige* the shipowners to deliver without presentation of bills of lading. The court held that:

*"Clauses 13 and 50 do not in my view impose any express obligation on the Charterers to discharge a cargo in the absence of the Bill of Lading. They merely provide for a letter of indemnity if such discharge takes place. But I do not construe the clauses as imposing a contractual duty on the Owners."*

By way of contrast, the charterparty in another case called *The Delfini*<sup>12</sup> provided that:

*"Should Bills of Lading not arrive at discharge port in time **then Owners agree to release the entire cargo without presentation of the original Bills of Lading** against delivery by Charterers of letters of indemnity issued in accordance with Owners' *Pandl Club* wording, counter-signed by ..."*

The latter wording is clearly different in that the emphasised words place a positive obligation on the part of the shipowner to release the cargo without surrender of the original bills of lading if called upon to do so by the charterers. Therefore, provided that the shipowner does not deliver to someone whom he knows not to be the party entitled to take delivery of the cargo (in which case the owner would be agreeing to commit an illegal or fraudulent act), the shipowner is contractually obliged to proceed in this manner notwithstanding the fact that he will lose his P&I cover if he does so.

*Delfini* type clauses are common in charter forms used by the oil majors and carriers may be prepared to accept the commercial risk of such clauses when chartering to the oil majors. However, shipowners who use such forms regularly should be aware of the dangers of using such forms when chartering to charterers who are not oil majors and who may not, therefore, have the same financial backing for such LOI. In such circumstances, the shipowners may be obliged to deliver cargoes without surrender of the original bills if this is demanded by the charterers but the only security to which the shipowners may be entitled in such circumstances is an indemnity from those charterers.

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<sup>12</sup> *The Sagona*, [1984] 1 Lloyd's Rep. 194.

### 20.2.1.3 International Group of P&I Clubs LOI

The P&I clubs that are members of the International Group of P&I Clubs are obliged by the terms of their common reinsurance policy to adopt a rule which emphasises that if any of their members deliver cargo other than against surrender of the original bill of lading, that member will not have P&I cover for liabilities resulting from such act.<sup>13</sup> This rule applies to 'negotiable,' 'transferable' or 'to order' bills, and, in most cases, to straight bills.

However, such clubs have also recognised that despite the risks that may be run by their members in such circumstances, their member may often be obliged to do so for commercial reasons. Consequently, those clubs have attempted to assist their members by providing draft forms of LOI which the member may choose to adopt in such circumstances. However, P&I clubs have repeatedly re-emphasised in club circulars over the years that they are not, by doing so, waiving the rule described above. Therefore, even if the member chooses to deliver cargo without surrender of the original bills of lading against receipt of a LOI in the terms drafted by the relevant P&I clubs,<sup>14</sup> the member will still lose his P&I cover for liabilities, costs and expenses arising as a result of such delivery. Therefore, the member is wise to ensure that he has satisfactory alternative security by way of LOI since ultimately, this will probably be his only source of comfort if a claim is made by a third party who produces the original bill of lading in due course. Therefore, P&I clubs normally recommend that the LOI should be given by a first class bank or by someone of equal financial standing.<sup>15</sup>

### 20.2.1.4 Insurance

Although the rules of the International Group clubs exclude cover for liabilities arising as a result of the delivery of cargo without surrender of the original bills of lading, alternative insurance may be available outside the P&I mutual insurance system by payment of additional premium. For example, the Comprehensive Carrier's Liability Cover<sup>16</sup> provided by Gard insures a carrier against such liability:

- i where the assured has received an undertaking on the terms of the International Group Form A from either the charterer of the ship or the person to whom delivery of the cargo is made, or;
- ii where the assured is required by law to deliver or relinquish custody or control of the cargo without production of the bill of lading, or;

<sup>13</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 proviso i (Cargo Liability)).

<sup>14</sup> For further commentary on these LOI see Chapter 20.3 below.

<sup>15</sup> See Chapter 20.3.1 below.

<sup>16</sup> Details of the cover can be accessed at the Gard website: [www.gard.no](http://www.gard.no) and follow the links to *Covering Risks and Comp Carrier's liability*.

- iii where delivery is made against a forged, fraudulent, misappropriated or otherwise unauthorised version of the bill of lading, provided that the assured has satisfied the insurer that he took such steps as appear to the insurer to be reasonable to ascertain that the cargo was properly delivered to the person entitled to such delivery, save that liabilities, losses, costs or expenses arising out of any wilful misconduct or gross negligence on the part of the assured are always excluded, or;
- iv where an agent or other designated representative acting on behalf of the assured has caused the cargo to be delivered without production of the relevant bill of lading and this has been done without the assured's approval.

### 20.2.2 Change of Destination/Deviation

Once a contract of carriage provides for discharge at a particular port, the carrier is obliged to proceed to that port on the usual and customary voyage to that port and may be liable for deviation if the vessel either proceeds on a different route or to a different port. Traditionally, an *intentional* breach of this kind has been considered to be a deviation. The effect of deviation was explained by the English court in the case of *Hain v Tate & Lyle*<sup>17</sup> as follows:

*"It (the deviation) abrogates (i.e. sets aside) the special contract entirely."*

Consequently, a carrier who deviates:

- may not be able to rely on any exception clause in the contract of carriage to protect him against claims; and
- may lose his right to limit liability; and
- may prejudice his P&I cover.<sup>18</sup>

However, a diversion from the direct route may be justified in the following circumstances:

#### 20.2.2.1 By Custom of the Trade<sup>19</sup>

The relevant customary route will depend on the particular trade. For example, whilst the customary route for a bulk carrier proceeding from the Arabian Gulf to Tokyo would normally be the direct route between the two ports, the customary route for a container vessel might be via Bombay, Colombo, Singapore, Hong Kong and Shanghai, i.e. via the usual container hub ports.

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<sup>17</sup> [1936] 55 Lloyd's Rep. 159.

<sup>18</sup> See Chapter 20.2.2.7 below.

<sup>19</sup> See Chapter 20.2.1.1 above.

### 20.2.2.2 By Public policy

Notwithstanding the fact that much of the emphasis of ship distress response has shifted from a ship to ship basis to a ship to shore basis following the implementation of the Global Maritime Distress Safety System (GMDSS) under the SOLAS Convention a carrier is still justified in diverting to avoid perils which could affect the safety of life or the common venture or to save life on another ship.<sup>20</sup> For example, a ship would be justified in diverting to Honolulu as a port of refuge on a voyage from South East Asia to North West America in order to carry out urgent repairs or if a crew member urgently required hospitalisation. Similarly, a ship would be justified in diverting in order to answer a Mayday call from another ship and might well be instructed to do so by one of the Maritime Rescue Co-Ordination Centres around the world.

### 20.2.2.3 By International Convention

A ship may be obliged to divert in order to comply with the provisions of an international convention such as the dangerous cargo provisions of the SOLAS Convention.<sup>21</sup> Furthermore, Article IV Rule 4 of the Hague and Hague-Visby Rules provides that:

*“Any deviation in saving or attempting to save life or property at sea, or any reasonable deviation shall not be deemed to be an infringement or breach of these Rules or of a contract of carriage and the carrier should not be liable for any loss or damage resulting therefrom.”*

In deciding whether any particular diversion constitutes a ‘reasonable deviation’ tribunals will normally be influenced by whether the particular diversion was done for the joint benefit of ship and cargo (in which case it may well be a reasonable deviation) or whether it was done purely for the benefit of the carrier (e.g. diverting to buy non-essential but cheap stores) (in which case it will probably not be held to be a reasonable deviation).<sup>22</sup>

### 20.2.2.4 By Liberty (or Caspiana) Clauses

Liberty clauses are intended to give the carrier the right to divert from what would otherwise be the customary route in particular circumstances. The most common examples adopt and are based on the public policy justification described above (e.g. the BIMCO Ice Clause, VOYWAR 2004 Clause, the P&I Bunker Deviation Clause, the BIMCO Piracy Clause for Voyage Charter Parties etc.) but outline the carrier’s rights in more detail. Such clauses are intended to make the contract of carriage more flexible for the common good of ship and cargo and are consequently upheld unless the

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20 See para. 10.267 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006.

21 For more detailed commentary on dangerous goods see Chapter 7 (Dangerous Goods Claims).

22 See paras.10.264 to 10.284 of *Bills of Lading* by Aikens, Lord and Bools, Informa, 2006.

carrier abuses the flexibility that the clauses provide. By way of contrast, some clauses are extremely wide in ambit (e.g. the liberty to call 'at any port in any order' or 'for any purpose'). Such clauses are less likely to be enforced if they are used in circumstances purely for the carrier's own benefit (e.g. to load or discharge other cargo).

#### **20.2.2.5 Change of Destination**

If a bill of lading provides that the ship is to proceed to port A to deliver the cargo, the carrier is obliged to proceed to port A on the usual and customary route. Therefore, a subsequent request (usually by the charterers) for the vessel to proceed to deliver the cargo at a completely different port B is in effect a request for the ship to deviate, and if the carrier were to agree to do so, that might well be considered to be an intentional decision to commit a deviation. Therefore, the request is, in effect, asking the carrier to become subject to the risks outlined above and a carrier may be reluctant to do so.

However, the request to proceed to a different port is normally made in order to accommodate changes to the cargo sale contract, e.g. when the original sale has fallen through and the cargo has been sold to a new buyer. Therefore, charterers and/or cargo owners will often request the carrier to proceed to the revised discharge port and in order to persuade the carrier to do so, offer a LOI purporting to indemnify the carrier if the carrier incurs liability as a result of doing so. However, whilst such LOI are frequently offered, a carrier is not obliged to proceed to the revised discharge port unless the carrier has agreed to the inclusion in the relevant contract of carriage of a clause obliging him to do so.

##### ***20.2.2.5.1 Revised Orders Clauses***

It is becoming increasingly common, particularly in tanker voyage charterparties, to see clauses which are intended to give charterers the right to amend their voyage orders after cargo has been loaded, and to order the vessel to deliver the cargo at a port other than that first nominated. If such orders are given after a bill of lading has been issued this may cause the shipowner difficulty, in that the bill of lading is a completely separate contract between the shipowner and a holder in due course of the bill, and contractually obliges the shipowner to deliver the cargo to the holder of the bill at the port specified in the bill. Accordingly, any order given under the charterparty to deliver the cargo at a port which differs from that specified in the bill of lading potentially exposes the shipowner to a claim for deviation under the bill of lading unless the holder of the bill also agrees to the new port. The difficulty which the shipowner faces when receiving such instructions from the voyage charterer is that he may not know at that point in time whether a holder in due course of the bill has agreed to the diversion;



indeed, he may not know the identity of the holder in due course at that time. Furthermore, if he complies with the order and there is a deviation, then he may have prejudiced his contractual defences and his P&I cover.<sup>23</sup>

Such clauses are strictly construed by the courts but if the clause does not oblige the shipowner to commit a deviation under the bills of lading, there is no reason why the clauses should not be enforced by the court. One example of such a clause is Clause 4 (b) of the ASBA II form of charter which reads as follows:

*“(b) After loading or discharging port(s) have been nominated, charterers may change such port(s) and/or vary their rotation **consistent with Part I and bills of lading, if any**, and owner shall issue instructions necessary to give effect to such change.”*

The emphasised words make it clear that any revised orders must not be contrary to the terms of any bills of lading which have been issued in the meantime and that, accordingly, the clause does not oblige the shipowner to commit a deviation.

However, if the clause does oblige the shipowner to deviate if called upon to do so by the charterer, the court will enforce the clause if it is sufficiently clearly worded. The following is an example of such a clause:

*“Notwithstanding anything else to the contrary in this charterparty and **notwithstanding what** loading and/or discharging ports may have been nominated and **bills of lading issued**, charterer shall have the right to change at any time its nomination of the loading and/or discharging ports in accordance with Part I of the charterparty”*

#### 20.2.2.6 International Group of P&I Clubs LOI

For the reasons already explained above<sup>24</sup> the International Group clubs have jointly suggested a form of LOI<sup>25</sup> which their members may wish to use in such circumstances. However, as explained above, it must be appreciated that, even if the member chooses to use such form, he may still have prejudiced his club cover. The LOI is intended to be an alternative form of protection.

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<sup>23</sup> See Chapter 20.2.2.7 below.

<sup>24</sup> See Chapter 20.2.1.3.

<sup>25</sup> For further commentary on these LOI see Chapter 20.3 below.

### 20.2.2.7 Insurance

Unless the particular club exercises its discretion to allow cover, the rules of the International Group clubs exclude cover for liabilities arising as a result of unreasonable or unauthorised deviation.<sup>26</sup> Clubs are given a certain amount of discretion since the question of whether or not a diversion from the customary route should be treated in law as a deviation may not always be clear at the time that the decision to divert has to be taken. For example, a liberty clause may give a general right to avoid war, ice or piracy but the precise extent of the liberty may be open to debate. Therefore, there is a danger that a shipowner who followed a route that he believed in good faith to be necessary to avoid a danger could be held in due course to have taken a longer route than was strictly necessary and therefore, to have committed a deviation. In such circumstances, the relevant P&I club would probably wish to exercise its discretion to provide cover. However, a shipowner that loads cargo knowing at that time that he will have to interrupt the voyage to carry out repairs before he can complete the voyage is unlikely to persuade his club to exercise its discretion to provide cover. Therefore, clubs are less likely to exercise their discretion to provide cover if it appears that the shipowner has adopted a course of action that is intended primarily to benefit the shipowner whilst resulting in disadvantage to the other party to the contract.

However, if the standard P&I cover is not available, alternative insurance may be available outside the P&I mutual insurance system by payment of additional premium. For example, the Comprehensive Carrier's Liability Cover<sup>27</sup> provided by Gard insures a carrier against such liability where delivery is given at a port other than that stated in the bill of lading provided that the carrier has received from the charterers or the party to whom delivery is being made an undertaking on the terms of the International Group Form B.<sup>28</sup>

### 20.2.3 Releasing clean or ante-dated Bills of Lading<sup>29</sup>

It is necessary to consider this issue in two different circumstances:

#### 20.2.3.1 Where it is Obvious that Cargo is not in Apparent Good Order and Condition or that the Date of the Bill of Lading is False

The 'clean' nature of a bill of lading is a representation of the condition of the goods on shipment. Potential buyers of the cargo will rely on this representation when deciding whether or not to pay for the goods. Similarly, the date of the bill of lading

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<sup>26</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1iv and ix (Cargo Liability)).

<sup>27</sup> See footnote 16 above.

<sup>28</sup> See Chapter 20.3 below.

<sup>29</sup> For further commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1.ix (Cargo Liability)).

is often material to the underlying cargo sale contract in that it either confirms that the goods have been shipped within the agreed shipment period or it establishes the price of the goods.<sup>30</sup>

Cargo sale contracts and letters of credit will normally stipulate that a buyer need only pay against 'clean' bills of lading or bills which are correctly dated within the period for shipment allowed by the letter of credit. Therefore, if the seller of the goods were to obtain a bill of lading from the ship stating that the cargo has not been shipped in apparent good order and condition or a bill which was dated outside the shipment period agreed in the cargo sale contract, the seller might not be able to obtain payment from his buyer. Accordingly, there may be a temptation on the part of the seller to request the carrier to issue clean bills when the cargo is clearly damaged or to release wrongly dated bills in order to enable the seller to obtain payment from the buyer. However, the rules of the International Group clubs specify that their members will not have the protection of P&I cover in such circumstances. Consequently, such a request is often accompanied by the offer of a LOI in which the seller promises to indemnify the carrier if the carrier were to agree to the request and incur loss or liability as a result of doing so.<sup>31</sup>

The English court have held that it is a fraud to knowingly issue clean bills of lading when it is clear that the cargo is damaged, or to issue ante-dated bills of lading.<sup>32</sup> Consequently, it must be clearly understood that any LOI that may be given to the carrier in such circumstances is normally unenforceable as an illegal contract because its purpose is to commit a fraud on the buyer. Therefore, any carrier who agrees to comply with such requests will normally find that they may be liable for fraud without any protection either by way of insurance or by way of LOI.

### 20.2.3.2 Where it is Unclear whether Cargo is not in Apparent Good Order and Condition

The commentary in Chapter 20.2.3.1 proceeded on the premise that the shipowner issued a clean bill of lading which *he knew to be false*, and therefore, committed the tort of deceit. However, if there is a *bona fide* doubt whether or not the cargo is damaged, it may well be that an indemnity given in these circumstances is valid as there would be no intentional fraud or deceit. Therefore, the effectiveness or otherwise of a LOI which is given in these circumstances depends on whether the LOI was intended to facilitate a fraud or in order to break through an impasse in

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<sup>30</sup> For more detailed commentary on these issues see Chapter 3.5.1.1 (Cargo Claims).

<sup>31</sup> See also the commentary in Chapter 20.1 above.

<sup>32</sup> Since the date of the bill of lading is often crucial in either fixing the price of a commodity or to establish whether shipment has been made under the cargo sale contract within the agreed period it may well be that the same principle may now be extended to post-dated bills of lading.

good faith. However, the particular facts will be very important in each case as is emphasised in the last sentence of the quote below. For example, it was stated by the English Court of Appeal in *Brown Jenkinson v Percy Dalton*<sup>33</sup> that:

*“There may perhaps be some circumstances in which indemnities can properly be given. Thus, if a shipowner thinks that he has detected some faulty condition in regard to goods to be taken on board he may be assured by the shipper that he is entirely mistaken; if he is so persuaded by the shipper, it may be that he could honestly issue a clean bill of lading while taking an indemnity in case it was later shown that there had in fact been some faulty condition. Each case must depend upon its circumstances.”*

Furthermore, it is difficult to think of circumstances in which the master is not aware of the correct date of shipment and accordingly, it is unlikely that a letter of indemnity given in relation to ante-dated bills of lading would be enforced by the court since by issuing such a bill of lading and demanding an indemnity, the carrier would be committing the tort of deceit.

### **20.2.3.3 Insurance**

The rules of the International Group clubs exclude cover for liabilities arising as a result of the issuance of an ante-dated or post-dated bill of lading, waybill or other similar contract of carriage or the issuance of such contracts which to the knowledge of the member or master contain an incorrect description of the cargo or its quantity or condition.<sup>34</sup> Since these activities are usually tainted with fraud or deliberate wrong-doing, it is not normally possible for carriers to obtain alternative insurance cover for such risks.

### **20.2.4 Switch Bills of Lading**

A seller of goods may find after bills of lading have been issued and released by a vessel that the bills do not meet the requirements of the contract of sale of the cargo for various reasons. For example:

- The contract of sale or the letter of credit may call for a different form of bill of lading;
- The contract of sale or the letter of credit may call for a different port of discharge;
- The trader may wish to conceal the name of the party from whom he has bought the goods and may therefore, wish to conceal the name of the shipper on the bill of lading;

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<sup>33</sup> [1957] 2 Lloyd's Rep 1.

<sup>34</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 ix and x (Cargo Liability)).

- The trader may wish to conceal where the cargo was loaded or the date of shipment;
- The cargo which was originally loaded may have been co-mingled with another ingredient after loading in order to produce a commodity of a different specification which is now being sold to the customer.

The trader may therefore wish to obtain a different bill of lading from the carrier in order to enable him to fulfil the requirements of the sale contract. Since the bill of lading is a document which is signed by or on behalf of the carrier and which therefore, places legal responsibilities on the carrier, the trader cannot simply change or amend the bill of lading which is in his possession. He must ask the carrier to agree to such amendments or to issue new bills of lading in a different form or in different terms. He may therefore, need to ask the carrier to agree to 'switch the bills', i.e. collect in the bills which have already been issued and replace them with new bills in the requested form. However, if the carrier were to agree to switch the bills it may be exposed to the following dangers:

- If there are two different bills of lading in circulation at the same time, this would be a recipe for disaster as the carrier would be potentially under an obligation to deliver to two competing claimants. Even if the carrier were to ask a court to decide which of the two competing claimants is entitled to the goods, the carrier might be unable to recover the costs of doing so since these costs were occasioned by his bad practise in failing to ensure that the first set of bills had not been taken out of circulation. The carrier should therefore, ensure if he agrees to 'switch' the bills, that he will have collected in and destroyed the first set of bills before he has released the 'switch' bills.
- Bills of lading are important receipts for the goods. Many parties, especially the cargo buyers, rely on the truth of the information stated therein. Therefore, the new 'switched' bills must still record accurately the true details of the shipment. In other words, they must correctly represent the nature, condition and quantity or weight of the goods and state where and when the goods were loaded. If they do not do so then the carrier will be liable for misrepresentation to any party to whom the goods are transferred without notice of the true facts. This may be a logical conundrum if the bills are switched since the parties wish to conceal the true facts.
- The terms of the 'switched' bills may be different from the terms of the first set of bills and may expose the carrier to greater liability or expenditure, e.g. when the first set of bills were on FIOS terms whereas the 'switched' bills are on 'liner' terms (thereby increasing the liability of the carrier for the cost of discharge) or when the first set of bills were subject to the Hague or Hague-Visby Rules whereas the 'switched' bills are subject to the Hamburg Rules (thereby increasing the liability of the carrier for cargo claims).

- Even if care is taken to ensure that the terms of the 'switched' bills are the same as those of the first set of bills other factors may mean that the carrier is, nevertheless, exposed to unforeseen greater liability.
- Because of these difficulties P&I clubs may refuse to extend cover to a carrier for any liability which he incurs as a result of the fact that the Bills of Lading have been 'switched.' This is likely to be the case if the bills are switched for illegal or fraudulent reasons. Therefore, any carrier which receives a request to 'switch' bills should firstly discuss the matter in detail with its P&I club to ensure that cover is not prejudiced and that it complies with any recommendations made by the club.

The carrier is not obliged to agree to 'switch' the bills of lading simply because such a request is made by the charterers or the cargo owners. This is because the bills of lading which have been issued already constitute a binding contract between the carrier and the trader and it is a fundamental rule of contract law that neither party to a contract is unilaterally obliged to agree to any amendments to that contract. The situation may be different if there is a clause in the contract of carriage which obliges the carrier to 'switch' the bills if such a request is made by the charterer. However, such clauses are not common and, in any event, usually oblige the carrier to agree to 'switch' bills only in legal and non-fraudulent circumstances. Therefore, in order to persuade the carrier to agree to the request, the trader will often offer a LOI purporting to protect the carrier against any losses or liabilities which it may incur as a result of 'switching' the bills.

However, such letters of indemnity (LOIs) may not be sufficient protection in all circumstances. Requests for 'switched' bills of lading can be made for perfectly legitimate reasons (e.g. if the letter of credit requires a Conlinebill instead of a Combiconbill) or in order to mislead or defraud potential transferees of the bill (e.g. to amend the loading port to conceal a breach of an embargo.) If the 'switch' is being made for legitimate reasons, then an LOI given to protect the carrier in such circumstances is normally enforceable by the courts. However, for the reasons stated above, if the 'switch' is requested for illegal or fraudulent reasons, then the courts will probably refuse to enforce it, in which case the carrier may have lost the protection of P&I cover without securing alternative protection under the LOI.

#### **20.2.4.1 Insurance**

Unless the particular club exercises its discretion to allow cover, the rules of the International Group clubs exclude cover for liabilities arising as a result of the issue of bills of lading that are known to contain data which is untrue or incorrect.<sup>35</sup> The rules of the International Group clubs also exclude cover for liabilities arising as

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<sup>35</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1 b ix and x (Cargo Liability)).

a result of the deliberate or intentional or reckless misconduct of the member.<sup>36</sup> Therefore, the question of whether or not cover is available for liabilities arising as a result of 'switching' bills will normally depend on the reason why the bills have been 'switched' and on whether the replacement bills can be stated to be true and accurate receipts which do not fall foul of any of the normal exceptions to cover. Depending on these issues, the club may have the discretion to either confirm or reject cover.<sup>37</sup>

### 20.2.5 Co-mingling and/or Blending<sup>38</sup>

Co-mingling and blending are terms which are used most often in connection with liquid cargoes. The terms are sometimes used interchangeably but they are in reality two quite distinct practices and are treated as such for liability and insurance purposes. Co-mingling occurs when a vessel loads into the same cargo compartment different parcels of the same grade of cargo that have been supplied by different shippers, shore tanks or ports. However, blending occurs when two or more parcels of different grades are loaded into the same cargo space but these cargoes are then blended together on the ship with the aim of producing a product that is different from either of those that were originally loaded.

Co-mingling and blending may both have various cost advantages for charterers and are therefore, operations which can be commercial attractive to traders. However, whilst such operations may be technically possible provided there is no danger caused to the ship or crew,<sup>39</sup> they do have legal and insurance ramifications, namely:

- 1 Liability for physical problems for the co-mingled or blended cargoes; and
- 2 Documentary difficulties.

#### 20.2.5.1 Liability for Physical Problems for the Co-mingled and Blended Cargoes

The blending of one cargo with a subsequent cargo is a potential contamination of both the cargoes that have been loaded (or received for shipment) in apparent good order and condition and is, therefore, a potential breach of Article III Rule 2 of the Hague or Hague-Visby Rules (i.e. a failure to properly and carefully care for the cargo). Furthermore, the shipment of the 'second' cargo into a tank which already contains other cargo of a different source or specification is potentially a breach of Article III Rules 1 (i.e. a failure to exercise due diligence to "make the holds,

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<sup>36</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 72).

<sup>37</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1).

<sup>38</sup> For more detailed commentary see *LOIs for commingling or blending on board* in *Gard News* No. 171.

<sup>39</sup> The Maritime Safety Committee and Marine Environment Protection Committee of the IMO stated in their joint Circular 8 dated 3 August 2009 that commingling or blending should not be performed during a voyage but merely within port limits.

refrigerating and cool chambers, and all other parts of the ship in which goods are carried, fit and safe for their reception, carriage and preservation”) and/or 2 of the Hague or Hague-Visby Rules.<sup>40</sup>

The co-mingling of two or more consignments of the same grade in the same hold does not necessarily give rise to the same problems. Nevertheless, it cannot be guaranteed that the various consignments will be completely homogeneous and, if they are not homogeneous, then the carrier can potentially incur the same liabilities.

#### **20.2.5.2 Documentary Difficulties**

Once the co-mingling or blending has taken place, the carrier is often asked to replace the bills of lading which had originally been issued for the ‘first’ cargo by a new set of bills which reflect the fact that the ship now has additional cargo on board (in the case of co-mingling) and/or a cargo of a different specification (in the case of blending) (i.e. the carrier is asked to ‘switch’ the first set of bills). For example, Clause 5 of the EXXONMOBIL 2000 form of charter provides that:

*“Charterer will surrender to master all original Bills of Lading for the unblended cargo and the Master will provide new consolidated Bills of Lading on completion of blending operations which Bills will reflect the actual grade that has been blended.”*

However, such practise creates various difficulties. Firstly, the carrier may be uncertain how to describe the ‘blended’ cargo on the ‘new consolidated bills of lading’ particularly since the shipper may wish to describe the blended cargo in a manner which conceals the fact that the cargo has been blended. Secondly, the new set of bills must record the true place and date of shipment, For example, if 1,000 tons of product was loaded at Port A on 1 January, and a further 1,000 tons loaded on top of that product at Port B on the 15 January, what details are to be inserted on the new bills? One could not truly say that 2,000 tons was loaded at port A, or at port B, or say that 2,000 tons was loaded on either the 1 or the 15 January. It would be factually correct to say that 1,000 tons has been loaded at port A and then insert a clause on the face of the bill stating that this quantity had been subsequently co-mingled or blended at port B with another quantity of 1,000 tons on the 15 January. For example, the Intertanko Blending Clause<sup>41</sup> provides that:

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40 For further commentary see Chapter 3.2.9.2.1 (Cargo Claims).

41 The complete clause and an accompanying commentary can be accessed at: <http://www.intertanko.com/Topics/Legal-and-Documentary-/INTERTANKO-Model-Clauses/INTERTANKO-Model-Clauses1/INTERTANKO-Blending-Clause/>.



*“Owners shall on completion of blending sign new bills of lading for the blended cargo containing a full and accurate description of the cargo, together with the dates and places of shipment and description and quantities of the cargoes which have been blended.”*

However, whilst such an approach may be perfectly acceptable for carriers, it might be unacceptable to a trader since the presence of such a clause on the face of the bill might make such a bill unacceptable for the purposes of the contract of sale or letter of credit.

### 20.2.5.3 Insurance

The rules of the International Group clubs exclude cover for liabilities arising as a result of the deliberate or intentional or reckless misconduct of the member.<sup>42</sup> Therefore, the question of whether or not cover is available for liabilities arising as a result of co-mingling and/or blending will normally depend on the reason why this has been done, on the manner in which it has been done, and on whether the replacement bills can be stated to be true and accurate receipts which do not fall foul of any of the normal exceptions to cover. Depending on these issues, the club may have the discretion to either confirm or reject cover.<sup>43</sup>

P&I cover will normally be available for co-mingling provided that the bills of lading accurately record the fact that co-mingling has taken place. *Inter alia*, this will require the bills to state correctly what quantities have been loaded at which ports and the dates on which such loading took place. However, blending, is not part of the normal carriage process, but is more in the nature of a specialist operation. Therefore, because of the difficulties outlined above, P&I clubs emphasise that P&I cover is normally not available for liabilities, losses, costs and expenses arising from blending.

In both cases, the shipowner is being asked to run a risk and, therefore, in order to persuade the carrier to agree to co-mingle or blend the cargo, the trader or charterer will frequently offer the carrier an LOI purporting to protect the carrier against any losses or liabilities that it may incur as a result of doing so. However, there is no guarantee that such an indemnity will be enforceable in all circumstances. For the reasons emphasised in Chapter 20.2.4 above, the enforceability or otherwise of such an LOI will depend on whether the co-mingling or blending and subsequent switch of the bills of lading is done for legitimate or fraudulent reasons. The problem for the carrier is that it may not know the precise reason for the co-mingling or

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<sup>42</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 72).

<sup>43</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 34.1).

blending and the subsequent switch of the bills of lading at the time that it is asked to do so. Therefore, if carriers have concerns in that regard, they should, before agreeing to co-mingle or blend cargoes in exchange for a LOI, ask the charterer for further clarification and then consult the carriers' P&I club.

### **20.3 Practical Issues**

The effectiveness or otherwise of an LOI depends upon:

- its legal enforceability;
- the legal capacity of the entity issuing the LOI;
- the creditworthiness of the entity issuing the LOI;
- the beneficiary of the LOI; and
- the terms of the LOI.

#### **20.3.1 The Legal Enforceability of the LOI**

Comment on this issue has already been made in Chapters 20.2.1-4 above.

#### **20.3.2 The Creditworthiness of the Entity Issuing the LOI**

The relevance of creditworthiness is self-evident since in many instances the LOI is intended to replace P&I cover which has been prejudiced. Carriers who investigate the creditworthiness of charterers before agreeing to charter to them should be aware that the degree of creditworthiness that may be required for the sake of an LOI may be substantially greater than the degree of creditworthiness that may be required for assessing the charterer's ability to pay freight or hire. For example, the potential liability which could arise under an LOI given in order to persuade a carrier to deliver cargo without surrender of the original bills of lading will be at the very least, the full value of the cargo in question. In fact, the claim that would ultimately be made by the carrier under the LOI would normally also include interest and costs and therefore, it is normally recommended that the LOI should either be unlimited in quantum or limited to a minimum of 200 per cent of the value of the cargo at risk. Therefore, whenever possible, the creditworthiness of the party offering the LOI to honour the obligation contained in the LOI should be assessed on each occasion that an LOI is offered.

For this reason, the three forms of LOI (Forms A, B and C) which have been jointly produced by the P&I clubs which are members of the International Group of P&I Clubs have been drafted in the alternative. One form (the single letter forms A, B and C) is intended to be provided by only one indemnifying organisation whilst another form (the double letter forms AA, BB and CC) is intended to be counter-

signed by a bank or some other guarantor. It is a commercial decision for the member whether to use the single letter or double letter form but the International Group of P&I Clubs has strongly recommended the use of the double letter form.<sup>44</sup>

### 20.3.3 The Legal Capacity of the Entity Issuing the LOI

The LOI is usually given in order to protect a party against a liability which is potentially very large and it is unlikely that the individual who has signed or otherwise provided the LOI will have sufficient personal assets to honour it. Therefore, it is important to establish that that person has the authority of the organisation on whose behalf he or she is purporting to sign the LOI to bind that organisation to the terms of the LOI. If that person does not have actual or ostensible authority to bind the organisation then the organisation may well not be bound by it and the person signing may be personally liable for breach of an agent's warranty of authority. For example, in one case a bank refused to honour a LOI which had been countersigned on its behalf by one bank official on the grounds that internal regulations required such a document to be signed by two officials. The court finally determined that the one official had sufficient ostensible authority to bind the bank but the issue was closely fought. Similarly, if the agent does not disclose the fact that it is acting for an undisclosed principal the principal and agent may be both jointly and severally liable under the LOI.

There may not be sufficient time in many circumstances to make detailed enquiries into the legal capacity of the person providing the LOI. However, beneficiaries of an LOI should be aware of the need to make enquiries if they are in any doubt about the authority of the person providing the LOI. If that person acts without authority the principal may, but is not obliged to, subsequently ratify that person's acts and to treat those acts as though they were made with authority. However, there is no guarantee that the principal will do so in all circumstances.

If the person providing the LOI is a director of, or holds a senior position in the organisation in question, that person may have sufficient apparent or ostensible authority to bind the company. There is apparent (ostensible) authority when the company has by its words or conduct led a reasonable person to believe that the officer or person in question has authority to act on its behalf. Therefore, if a principal appoints someone to act in a particular role, then even if that person has no actual authority to do so, third parties who thereafter deal with that person are entitled to assume that he has authority from the principal to do the things that

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<sup>44</sup> Copies of the most recent forms of these LOI can be accessed via the web sites of those P&I clubs that are members of the International Group of P&I Clubs.

are normally entrusted to someone who occupies such a position. Therefore, it is normally easier to prove apparent (ostensible) authority after a prior course of dealing between organisations.

### **20.3.4 The Beneficiary of the LOI**

The beneficiary should be the party who will bear the liability in the first instance in the event that a claim is made under or in respect of the bill of lading. Therefore, if a ship which is time chartered is asked to deliver cargo without surrender of the original bills of lading, it is the shipowners who are likely to be vulnerable to any claim that may be brought by the party to whom delivery should properly have been given. Consequently, the beneficiary of the LOI should be the shipowners and should the LOI be given in favour of the time charterers, the shipowners will have no protection other than whatever indemnity there may already be in the terms of the time charter.<sup>45</sup>

### **20.3.5 The Terms of the LOI**

#### **20.3.5.1 Enforcing the Terms of the LOI**

The terms of the LOI are important since the LOI will normally be called upon when the beneficiary has either already paid a claim brought by a third party or will shortly be called upon to do so. Therefore, the beneficiary will wish to be able to enforce the terms of the LOI with the minimum of delay and complication. Some charterparties attempt to deal with this problem by providing that a LOI in agreed terms is 'deemed to be given' whenever the charterers require the shipowners to comply with a request made by the charterers. Such provisions may be helpful in avoiding the delay which might otherwise be incurred if the parties had to negotiate suitable terms whenever such a request was made. However, care needs to be taken in such circumstances to ensure that the agreed terms can be enforced quickly and without complication since it is unlikely that the beneficiary will be able to obtain better or alternative security if and when he incurs liability in due course as a result of complying with the charterer's request.

#### **20.3.5.2 Performance of the LOI**

Furthermore, parties should take care to ensure that these draft forms are completed accurately and that performance is strictly in accordance with the terms of the LOI since inadequate attention to detail in this regard can undermine the whole basis of the security that is thereby provided. For example, the International Group of P&I Clubs Form A provides as follows:

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<sup>45</sup> For further commentary on such indemnities see Chapter 4.5.2 (Charterparty Claims).

*“The above cargo was shipped on the above ship by [insert name of shipper] and consigned to [insert name of consignee or party to whose order the bill of lading is made out, as appropriate] for delivery at the port of [insert name of discharge port stated in the bill of lading] but the bill of lading has not arrived and we, [insert name of party requesting delivery], hereby request you to deliver the said cargo to **[insert name of party to whom delivery is to be made]** at [insert place where delivery is to be made] without production of the original bill of lading.*

*In consideration of your complying with our above request, we hereby agree as follows:*

- 1. To indemnify you, your servants and agents and to hold all of you harmless in respect of any liability, loss, damage or expense of whatsoever nature which you may sustain by reason of delivering the cargo in accordance with our request.*
- 2. In the event of any proceedings being commenced against you or any of your servants or agents in connection with the delivery of the cargo as aforesaid, to provide you or them on demand with sufficient funds to defend the same.”*

The beneficiary is entitled to demand specific performance of the LOI only if he proves that he has delivered the cargo to the party named by the provider of the LOI in the emphasised section quoted above. Therefore, if the beneficiary of the LOI is requested to deliver the cargo to, say, X but delivers instead to, say, Y then the beneficiary cannot call upon the provider of the LOI to either put up security to release the ship from arrest or to indemnify the beneficiary against damages paid by him to the true owner of the cargo as a result of the misdelivery of the cargo to some other party.

This problem arose in the English court case of the *Bremen Max*<sup>46</sup> as a result of which the International Group amended the wording emphasised above as follows:

*“we hereby request you to deliver the said cargo to **X (name of the specific party) or to such party as you believe to be or to represent X or to be acting for X ...**”*

For similar reasons, the forms of LOI which have been suggested by the International Group clubs for use by tankers or gas carriers delivering cargoes to terminals include the following additional provision:

*“If the place at which we have asked you to make delivery is a bulk liquid or gas terminal or facility, or another ship, lighter or barge, then delivery to such terminal, facility, ship, lighter or barge shall be deemed to be delivery to the party to whom we have requested you to make such delivery.”*

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<sup>46</sup> [2009] 1 Lloyd's Rep. 81.

### 20.3.5.3 The Benefits of a Carefully Drafted LOI

Carefully drafted LOI terms can provide unexpected benefits. In the case of *Laemthong v Artis*<sup>47</sup> a shipowner was asked by his time charterer to deliver cargo without surrender of the original bills of lading. The shipowner agreed to do so in consideration of receipt from his time charterers of a LOI in Form A recommended by the International Group of P&I Clubs. The time charterers gave such LOI only after they had themselves received a LOI in similar terms from the party requesting delivery of the cargo. The shipowner was subsequently held to have misdelivered the cargo and was held to be liable to the true owner of the cargo. Therefore, the shipowner sought to enforce the LOI given by the time charterers but by this time the time charterers were found to be bankrupt.

The shipowners subsequently sought to enforce the terms of the LOI which had been given to the time charterers by the party who had requested delivery of the cargo. Despite the fact that the shipowners were not a party to the contract contained in such LOI they were nevertheless, entitled to enforce its terms. The reason why they were entitled to do so was because Form A is subject to English law and, therefore, to the terms of the Contracts (Rights of Third Parties) Act 1999. This statute entitles a third party to enforce the terms of a contract which has been concluded for his benefit. Section 1 (1) of the Act provides that:

*“Subject to the provisions of this Act, a person who is not a party to a contract (a ‘third party’) may in his own right enforce a term of the contract if-*  
*(a) the contract provides that he may; or*  
*(b) subject to subsection (2), the term purports to confer a benefit on him.”*

The English court recognised that the LOI was intended “to indemnify (the time charterers), your servants and agents and to hold all of you harmless” and that, for the purposes of delivering the cargo, the shipowners were the agents of the time charterers. Therefore, since the contract contained in the LOI was intended to confer a benefit on the shipowner, the shipowner as a third party to that contract was entitled to enforce the terms of the LOI given to the time charterers.

### 20.3.5.4 For How Long should a LOI be kept in Force?

The person who has provided the LOI may either have to pay a bank or a guarantor a fee for providing the security or, at the very least, record that security in its accounts as a possible liability. Therefore, it will wish to release that liability as quickly as possible. On the other hand, the beneficiary of the LOI will wish to retain

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47 [2005] 1 Lloyd's Rep. 100.

the security for as long as possible as protection against future claims. Therefore, the LOI will normally need to remain in force until the claim against which it is intended to provide security becomes time-barred.

Under English law, the usual time limit for contractual claims is six years whereas the time limit for claims against the carrier under the Hague or Hague-Visby Rules is one year from the date of delivery or the date when the cargo should have been delivered. Therefore, the question of whether the letter of indemnity should be kept in force for six years or one year depends largely on which time limit applies to the particular claim for which the LOI is intended to provide protection.

If the contract of carriage is subject to the Hague-Visby Rules it seems likely<sup>48</sup> that the relevant time limit is one year since Article III Rule 6 of these Rules provides that the ship shall:

*"... in any event be discharged from all liability whatsoever in respect of the goods"*

unless legal proceedings are commenced within the one year. However, if the carriage is subject to the Hague Rules then the position is not so clear since Article III Rule 6 of those Rules is arguably more restrictive in that it provides that:

*"In any event, the Carrier and the Ship shall be discharged from all liability in respect of loss or damage unless it is brought within one year..."*

Case law on this issue is unclear and therefore, if there is a danger that the proper time limit is six years rather than one year, a carrier obviously runs a risk if he agrees to release a letter of indemnity before that period expires, particularly since, as stated above, he will in the meantime have lost the benefit of his P&I cover for liabilities arising as a result. For this reason, the single letter (i.e. A, B and C) forms of LOI which have been jointly recommended by the International Group of P&I Clubs do not provide for any particular time limit although Form A provides that the security will remain in effect until all negotiable copies of the bills of lading have been surrendered to the carrier. The double letter forms (i.e. AA, BB and CC) which are to be countersigned by a bank provide for a six year time limit.

However, it cannot be guaranteed that there will be no liability after the expiry of these periods. Much depends on the nature of the claim and the governing law.

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<sup>48</sup> See *The Captain Gregos*, [1990] 1 Lloyd's Rep. 310 at page 313.

### 20.3.5.5 Insurance Cover

It is important to re-emphasise that LOI are usually required either since there is no P&I cover for the particular risk or because P&I cover for that risk has been prejudiced. Therefore, the LOI is intended to be substitute cover for the absent P&I cover. It is also important to re-emphasise that P&I cover is not maintained in such circumstances if a party chooses to use one of the LOI forms drafted by the member clubs of the International Group of P&I Clubs.

## 20.4 Claims Management

Shipowners should not give or accept LOI without proper consideration of the reason why the LOI is required and the implications of taking or giving the LOI. In many circumstances, the LOI may be the only security that is available in respect of a particular risk and must therefore, be treated seriously. Furthermore, masters and crew should be made aware of the implications of agreeing to give or take a LOI and should never consent to do so without consulting their shore-based superiors.<sup>49</sup>

## 20.5 Case Studies

### Case Study 1

Cargo was shipped in the Russian Far East and the bill of lading which was issued was subject to the Soviet Maritime Code (as it then was) which provided the carrier with a very favourable package limitation. This form of bill was not acceptable for letter of credit purposes and, therefore, these bills were destroyed and a new set of bills in identical form confirming the true details of the shipment in Russia were issued and released in Hong Kong. Hong Kong is a party to the Hague-Visby Rules, Article X of which provides that the Rules will apply compulsorily to any bill of lading issued in a contracting state (which includes Hong Kong). The carrier was therefore, bound by the Hague-Visby Rules package limitation which was far more favourable to the cargo claimant.

The same situation can also arise when a bill of lading that is originally issued in a country of shipment which applies the Hague-Visby Rules compulsorily is switched for bills of lading in exactly the same form in a country which applies the Hamburg Rules compulsorily. Pursuant to Article 2 of the Hamburg Rules bills of lading which are issued in a Hamburg Rules country are compulsorily subject to the Hamburg Rules even if the cargo was actually shipped in a Hague-Visby Rules country. Therefore, the switch has resulted in the replacement of the Hague-Visby Rules by the Hamburg Rules although the terms of the bill of lading are otherwise the same.

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<sup>49</sup> See also Chapter 2.11.4 of the *Gard Guidance to Masters*.



## Case Study 2

The vessel was on voyage charter and at the first load port was ordered by charterers to load into tank 1 a full cargo of grade A product but from two different shore tanks and into tanks 2, 3, 4, a part cargo of product A. At the second load port, charterers ordered the vessel to load a further parcel of product A into tank 2 and a parcel of product B into tanks 3 and 4. The cargo in tanks 3 and 4 was to be circulated en route to the discharge port in order to blend the cargo into product C. An LOI was issued by charterers to owners in respect of the two parcels of different cargo loaded into tanks 3 and 4 to indemnify owners in respect of all losses arising from blending (more specially described as loading into the same tanks and circulating by the vessel) the cargo in tanks 3 and 4. Bills of lading are issued as follows

Tank 1 showing grade A – cargo shipped onboard at first load port.

Tank 2 grade A – cargo shipped on board at first and second load port (the bill of lading shows the correct quantities, dates and places loaded.)

Tank 3 and 4 grade C – cargo blended on board from parcels shipped on board from load ports 1 and 2.

The bill of lading for grade C describes only that cargo and does not mention the separate load ports.

At discharge port all cargoes are alleged to be offspec and the evidence suggests that the grade A cargo was off-spec at the time of loading at the first load port although conflicting evidence suggests that the vessel may have been responsible for the contamination. Irrespective of this, expert chemical evidence suggests that this would not have resulted in cargo C being off-spec as a blended product if blending had been achieved uniformly. Owners request cover from their P&I club for the cargo claims relating to the cargoes in all these tanks and also seek to claim against charterers under the terms of the LOI for their expected liabilities and losses.

P&I cover is available for claims concerning the cargo in tanks 1 and 2. For tank 2, the cargoes have only been co-mingled (not blended, i.e. with the intention to create a new third product) and the bills of lading are accurate. As such cover is not prejudiced. However, cover for claims for the cargo carried in tanks 3 and 4, the blended cargoes, is not available as the owners will have prejudiced their cover by blending cargo, if on the evidence the liability arises from the blending operation and/or from the issue of incorrect bills of lading.

The LOI was issued to cover only tanks 3 and 4 and so did not cover any claims in respect of tanks 1 and 2. Owners would have to rely on their bill of lading defences and/or any charterparty indemnity clauses in respect of the cargo in these tanks. The LOI was an indemnity only in respect of losses arising from blending. The issue

for owners is likely to be whether the cargo contamination arose solely from the blending operation or whether it arose from some other cause, possibly a failure by the owners to otherwise properly and carefully load, carry, care for and discharge the cargo. If expert evidence indicates the blending was not carried out uniformly and that this caused the alleged off-specification, then provided the LOI covers this situation, the LOI would be the owners' only possible right of recourse. If the blended cargo was off-spec for other, shipboard-related, reasons (i.e. ingress of water resulting from unseaworthiness), the LOI would not respond, but P&I cover would.

## Chapter 21

# Limitation of Liability<sup>1</sup>

### 21.1 Introduction

A person who causes loss or damage to another as a result of his negligence or breach of contract is normally obliged to indemnify the innocent party for the totality of the losses that have been suffered by the innocent party as a result of that negligence or breach of contract. Therefore, if the guilty party causes a loss of USD 100, the guilty party is normally liable to pay USD 100 to the innocent party by way of damages provided that the loss is foreseeable and not too remote. However, it has been a unique feature of international transportation law whether by sea, air, rail or road for a considerable time that the transporter is entitled in certain circumstances to limit his liability to a sum which is less than the loss suffered even if that loss has been caused by the transporter's negligence. This principle is called the limitation of liability.

This rule has a long history and is the product of public policy. At a time when the countries of Europe were rapidly developing their industrial output and were looking for foreign markets for their goods it was considered unhealthy for the development of that trade if a shipowner could be put out of business by one large claim whilst transporting the goods to their overseas destination. The continued justification of the principle has been repeatedly questioned since the end of the 18th century but the principle is now deeply engrained in the law of most countries of the world.

In the majority of cases limitation is available pursuant to international conventions. However, some countries have not adopted any of the international limitation conventions but have national statutes that provide for limitation rights. The most well-known example is the United States of America. Under the Limitation of Liability Act,

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<sup>1</sup> For more detailed commentary see Chapters 27 to 30 of the *Gard Handbook on P&I Insurance*, 5th edition and *Limitation of Liability of Maritime Claims* by Griggs, Williams and Farr, Inform, 4th edition, 2005.

46 U.S.C. 30501, *et seq.* a shipowner is entitled in principle to limit liability so long as the relevant conduct was not committed with the 'privity or knowledge' of the shipowner. However, US courts are, in general, reluctant to allow limitation and can justify their refusal to do so on a number of factual or legal grounds.

It is not possible to comment in detail on the individual limitation laws of those countries that have chosen not to adopt the international limitation conventions and therefore, enquiry should be made of local lawyers or other knowledgeable sources in such cases.<sup>2</sup> However, whether limitation applies by virtue of international conventions or domestic law, most countries have rules which emphasise that the right to limit liability is a privilege and that such right will be lost if the party seeking that right is guilty of a particular type of serious conduct.

## 21.2 Types of Limitation

Two different types of limitation are normally relevant:

- The limitation of individual claims of a particular type; and
- The collective limitation of various types of claims arising on any one occasion.

### 21.2.1 The Limitation of Individual Claims of a Particular Type

There are a number of international conventions which allow limitation in relation to particular types of claim. For example, the Hague, Hague-Visby and Hamburg Rules entitle a carrier of goods by sea to limit his liability for cargo claims<sup>3</sup> and similar rights are given to carriers by air under the Warsaw/Montreal Conventions, carriers by road under the CMR Convention and carriers by rail under the CIF/COTIF Convention. This type of limitation is normally referred to as 'package limitation'. The carriers of passengers by sea and air are also given similar rights under the Athens Convention 1974 and the 2002 Protocol thereto<sup>4</sup> and the Warsaw/Montreal Conventions respectively. These conventions provide that limitation is to apply to individual claims of the defined type. For example, a separate limit applies to each cargo claim that is brought by each individual claimant.

This type of limitation differs from global limitation (see Chapter 21.2.2 below) in that the carrier will normally use his right to limit as part of his defence to the particular claim, whereas a person seeking to use his right to global limitation may commence proceedings as plaintiff and apply for a decree of limitation which, if successful, will enable him to limit his liability for *all* claims that qualify for global limitation purposes and arise as a result of the particular event.<sup>5</sup>

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2 Details of the limitation laws of different countries may be found in Part B, Chapters 7 to 43 of *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, 4th edition.

3 For more detailed commentary see Chapter 3.2.9.4 (Cargo Claims).

4 For more detailed commentary see Chapters 11.3.2.1 and 11.3.2.4 (People Claims).

5 See Chapter 21.3.4.1 below.

**NB!** The right of shipowners to limit their liability for pollution claims under the CLC<sup>6</sup> and HNS<sup>7</sup> Conventions is treated differently in that these conventions have special characteristics and different funding mechanisms which make it necessary to consider such rights separately.<sup>8</sup> Therefore, if, for example, claims are brought against a shipowner following a collision, his ability to limit his liability for claims that may be brought for damage caused to the other ship, or for cargo damage, or for personal injury would normally be subject to the provisions of the global limitation conventions discussed in Chapter 21.2.2 below, whilst his ability to limit his liability for pollution would be subject to whichever pollution convention that was applicable. Therefore, if the pollution was caused by the spillage of oil carried as cargo, limitation rights would be governed by CLC, whereas if the pollution was caused by the spillage of hazardous or noxious substances, the HNS Convention would apply. However, if the pollution was caused by the spillage of bunkers from a non-tanker limitation rights would be governed by the global limitation conventions discussed in Chapter 21.2.2 below since the Bunker Convention<sup>9</sup> has no free-standing limitation rights similar to those of the CLC.

### 21.2.2 The Collective Limitation of Various Types of Claims Arising on any one Occasion

This type of limitation (which is normally referred to as 'global limitation') applies a cap to all claims of a defined type that arise as a result of any one occurrence and includes (amongst others) most of the types of claim that are specified in Chapter 21.2.1 above. In the majority of cases, this type of limitation will be governed by the Convention on Limitation of Liability for Maritime Claims (London 1976) (The 1976 Limitation Convention) or the 1976 Limitation Convention as amended by its Protocol of 1996 (The 1996 Protocol) whilst some countries still apply the International Convention relating to the Limitation of Liability of Owners of Sea-Going Ships (Brussels 1957) (The 1957 Limitation Convention). However, countries that have chosen not to adopt these international conventions will also normally allow this form of global limitation as part of their domestic law.

The 1957 Limitation Convention has been rapidly overtaken by the 1976 Limitation Convention and the 1996 Protocol but the relevant limit of liability under both conventions is calculated with reference to the tonnage of the ship. Therefore, the bigger the ship, the bigger the limit. Other countries such as the United States are

<sup>6</sup> The International Convention on Civil Liability for Oil Pollution Damage 1969 and its Protocol of 1992.

<sup>7</sup> The International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea Convention 1996 (as revised by the 2010 Protocol).

<sup>8</sup> For more detailed commentary see Chapters 12.4.1.1.1.4 and 12.3.1.2 (Pollution Claims).

<sup>9</sup> The International Convention on Civil Liability for Bunker Oil Pollution Damage 2001. See Chapter 12.4.1.1.2 (Pollution Claims).

not parties to any international limitation convention but have their own municipal legislation which calculates the global limit in accordance with the value of the ship on completion of the voyage.<sup>10</sup> This difference of approach can have a dramatic effect on the quantum of the limitation fund that is available in different countries and can cause a substantial degree of ‘forum shopping’ whereby claimants and defendants try to obtain the jurisdiction that is most favourable to them.<sup>11</sup>

Provided that the conditions imposed by the two separate types of limitation are satisfied a party seeking to limit its liability may use either the one type of limitation or both in order to put a cap on its liability. For example, if cargo is damaged during a voyage, a carrier may limit his liability to individual cargo claims under the Hague or Hague-Visby Rules. However, if the cargo claims have arisen as a result of a collision and claims of a different type (e.g. for damage to the hull of the other ship) are also made against the carrier, the totality of the claims arising out of that one occurrence may exceed the ship’s global limit even after the individual cargo claims have been capped by the package limits that are available under the Hague or Hague-Visby Rules. Therefore, the carrier may also wish to rely on rights that are given to him under the global limitation conventions to place a cap on all claims arising out of that one occurrence at the global limit.<sup>12</sup>

### 21.3 Global Limitation

Currently, global limitation is regulated internationally by three different regimes

- The 1957 Limitation Convention;
- The 1976 Limitation Convention; and
- The 1996 Protocol to the 1976 Limitation Convention.<sup>13</sup>

Under all three regimes a distinction is drawn between claims for loss of life or personal injury on the one hand, and claims for other types of loss or damage on the other hand. The limit for claims for loss of life or personal injury is higher than the limit for other claims and claims for loss of life or personal injury have priority over other claims in the event that the limit is not sufficient to satisfy all claims.

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10 For more detailed commentary see Chapter 29.2 of the *Gard Handbook on P&I Insurance*, 5th edition and Part B, Chapter 42 of *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, 4th edition, 2005.

11 For more detailed commentary see Chapter 19.2 (Law and Jurisdiction).

12 For an example of such a situation see the Case Study in Chapter 28.5 of the *Gard Handbook on P&I Insurance*, 5th edition.

13 A list of which countries have adopted which convention can be accessed on the IMO website at: <http://www.imo.org/About/Conventions/StatusOfConventions/Pages/Default.aspx>.

However, the three regimes differ in some important respects and therefore, it is necessary to make enquiries in any particular case to ascertain which regime applies in the particular country where an application for limitation is made. In general terms, the differences are as follows:

- The 1957 Limitation Convention provides for lower limits than the 1976 Convention which in turn has lower limits than the 1996 Protocol to the 1976 Convention;
- The right to limit liability can be lost under the 1957 Convention if the occurrence which gave rise to the claims resulted from *“the actual fault or privity”* (i.e. the negligence) of the party seeking to limit whereas, under the 1976 Convention and the 1996 Protocol the right to limit liability is lost only if *“the loss resulted from his personal act or omission, committed with the intent to cause such loss, or recklessly and with knowledge that such loss would probably occur.”* However, the relevant conduct must in all three cases be that of the alter ego of the company, that is to say, the person who is not merely a servant or agent of the company but the person for whom the company is liable since his actions are considered to be the very actions of the company itself. Therefore, such a person must normally be a member of the higher management of the company;
- Under the 1957 Convention the onus is on the person seeking to limit liability to prove that he is entitled to do so (which in the majority of cases means that he has to prove that the claims did not result from his *“actual fault or privity”*) whereas, under the 1976 Convention and the 1996 Protocol, it is presumed that the person seeking to limit his liability has the right to do so and the onus is on any party seeking to debar the right to limit to prove that they are not entitled to do so.

### 21.3.1 The Limits of Liability

Separate limits apply for:

- claims for loss of life or personal injury; and
- other claims.

Under all three regimes the relevant limitation fund depends on the size of the ship. In the case of the 1957 Limitation Convention, the limitation fund is calculated by applying a specified financial value to each ton of the ship, i.e. 3,100 francs per ton in the case of claims for loss of life or personal injury and 1,000 francs per ton in the case of claims for property damage or loss. In many cases the reference to the franc has been replaced by a reference to the currency of the particular country. However, whilst the limitation fund is also calculated under the 1976 Limitation Convention and the 1996 Protocol by applying a specified financial value to each ton of the ship, the financial value per ton differs depending on the size of the ship.

Article 6 of the 1976 Limitation Convention provides that:

*“The limits of liability ... arising on any distinct occasion, shall be calculated as follows:*

- (a) in respect of claims for loss of life or personal injury,*
  - (i) 333,000 Units of Account for a ship with a tonnage not exceeding 500 tons,*
  - (ii) for a ship with a tonnage in excess thereof, the following amount in addition to that mentioned in (i)*
    - for each ton from 501 to 3,000 tons, 500 Units of Account*
    - for each ton from 3,001 to 30,000 tons, 333 Units of Account*
    - for each ton from 30,001 to 70,000 tons, 250 Units of Account*
    - for each ton in excess of 70,000 tons, 167 Units of Account*
  
- (b) In respect of any other claims*
  - (i) 167,000 Units of Account for a ship with a tonnage not exceeding 500 tons,*
  - (ii) for a ship with a tonnage in excess thereof the following amount in addition to that mentioned in (i)*
    - for each ton from 501 to 30,000 tons, 167 Units of Account*
    - for each ton from 30,001 to 70,000 tons, 125 Units of Account*
    - for each ton in excess of 70,000 tons, 83 Units of Account.”*

The 1996 Protocol to the 1976 Limitation Convention provides that the above limits are replaced with the following:

*“The limits of liability ... arising on any distinct occasion, shall be calculated as follows:-*

- (a) in respect of claims for loss of life or personal injury,*
  - (i) 2 million Units of Account for a ship with a tonnage not exceeding 2,000 tons,*
  - (ii) for a ship with a tonnage in excess thereof, the following amount in addition to that mentioned in (i)*
    - for each ton from 2,001 to 30,000 tons, 800 Units of Account*
    - for each ton from 30,001 to 70,000 tons, 600 Units of Account*
    - for each ton in excess of 70,000 tons, 400 Units of Account*
  
- (b) In respect of any other claims*
  - (i) 1 million Units of Account for a ship with a tonnage not exceeding 2,000 tons,*
  - (ii) for a ship with a tonnage in excess thereof the following amount in addition to that mentioned in (i)*
    - for each ton from 2,001 to 30,000 tons, 400 Units of Account*
    - for each ton from 30,001 to 70,000 tons, 300 Units of Account*
    - for each ton in excess of 70,000 tons, 200 Units of Account.”*



The relevant “Unit of Account” is the Special Drawing Right (SDR) the value of which fluctuates from day to day but its value in terms of national currencies can be checked in the financial newspapers daily.

It is noteworthy that;

- The limits for loss of life and personal injury claims are higher than those for ‘other claims’;
- Bigger ships pays less per ton overall than smaller ships;
- The 1996 Protocol limits are much higher than the 1976 Limitation Convention limits;
- The 1996 Protocol provides that the limits may be updated in future pursuant to the tacit acceptance procedure that is now a feature of many IMO instruments. Pursuant to this facility, the IMO has announced that the above limits will be increased by 51 per cent as follows on 8th June 2015:

*“(a) in respect of claims for loss of life or personal injury,*

- (i) 3.02 million Units of Account for a ship with a tonnage not exceeding 2,000 tons,*
- (ii) for a ship with a tonnage in excess thereof, the following amount in addition to that mentioned in (i)*  
*for each ton from 2,001 to 30,000 tons, 1,208 Units of Account*  
*for each ton from 30,001 to 70,000 tons, 906 Units of Account*  
*for each ton in excess of 70,000 tons, 604 Units of Account*

*(b) In respect of any other claims*

- (i) 1.51 million Units of Account for a ship with a tonnage not exceeding 2,000 tons,*
- (ii) for a ship with a tonnage in excess thereof the following amount in addition to that mentioned in (i)*  
*for each ton from 2,001 to 30,000 tons, 604 Units of Account*  
*for each ton from 30,001 to 70,000 tons, 453 Units of Account*  
*for each ton in excess of 70,000 tons, 302 Units of Account.”*

### 21.3.1.1 Passenger Claims

As stated above in Chapter 21.2.1 passenger claims are subject to two different types of limitation. The carrier may have the right to limit his liability to individual passenger claims under the Athens Convention but he may also have the right to limit his liability further under the 1957 or 1976 Limitation Conventions or the 1996 Protocol.

Under the 1957 Limitation Convention a passenger must share the relevant limit with non-passengers but the 1976 Limitation Convention and the 1996 Protocol have totally separate provisions regulating the right of the carriers of passengers to limit their liability in respect of claims for loss of life or personal injury to passengers (i.e. those travelling on board pursuant to a travel ticket). The limit for such claims is calculated not in accordance with the ship's tonnage but with reference to the total number of passengers that the vessel is authorised to carry. Therefore, the limitation of claims for loss of life or personal injury to crew members or other supernumeraries on the one hand,<sup>14</sup> and to passengers on the other hand,<sup>15</sup> is regulated by completely different provisions of these conventions.

### 21.3.2 Separate Limitation Funds for Each Occurrence

The limitation amounts that are described above apply to all claims that arise on each distinct occasion or occurrence. Therefore, if a ship suffers two separate incidents during the course of a voyage, then separate limitation funds must be established in respect of each incident. In most cases, it is normally easy to establish whether there has been one or more separate incidents but this is not always the case. Historically, courts have had to consider a number of cases where, for example, a ship that has collided with one ship subsequently drifts on the tide and comes into contact with another ship. More recently, the Australian court has had to consider whether damage caused by a ship's anchor to an underwater gas pipeline was caused simply by one continuing act of negligence on the part of the ship or by separate negligent acts in anchoring in the wrong location, failing to keep a proper anchor watch and in raising the anchor.<sup>16</sup> In such circumstances, courts have tended to resolve the issue by considering whether the second incident was the inevitable consequence of the first incident (in which case there is only one occurrence) or whether the ship had the ability to avoid the second incident and failed to do so (in which case there is more than one occurrence). If the ship is a large ship with a large tonnage the answer to this question can have significant financial consequences both for the claimant and for the shipowners and their insurers.

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<sup>14</sup> Regulated by Article 6 of the 1976 Limitation Convention and 1996 Protocol.

<sup>15</sup> Regulated by Article 7 of the 1976 Limitation Convention and 1996 Protocol.

<sup>16</sup> *The APL Sydney*, [2010] 2 Lloyd's Rep. 555 further details of which are set out in the Case Study in Chapter 21.5 below.

### 21.3.3 Restrictions on the Right to Limit Liability

Only certain kinds of persons are entitled to limit their liability and the right to limit is available only in respect of certain kinds of claims. Therefore, a party seeking to limit his liability must prove that he and his claim fall within the defined parameters otherwise there will be no right to limit.

#### 21.3.3.1 The Persons Entitled to Limit

The following persons are entitled to limit their liability under all three regimes:

- i The owners of a seagoing ship;
- ii The charterers<sup>17</sup> of a seagoing ship;
- iii The managers of a seagoing ship;
- iv The operators of a seagoing ship;
- v Any person for whose act, neglect or default the parties identified in categories i-iv is responsible.

However, the following additional persons are entitled to limit their liability under the 1976 Limitation Convention and the 1996 Protocol, but not the 1957 Convention:

- vi Salvors;
- vii Any person for whose act, neglect or default the salvor is responsible;
- viii The insurers of liability of the parties identified in categories i-vii.

#### 21.3.3.2 The Claims which Qualify for Limitation

However, the mere fact that a party is a person that is entitled to limit under the various conventions does not by itself mean that that person can limit. The relevant person must also prove that the claim which is the subject of limitation is a claim which qualifies for limitation under the relevant convention.

Under the 1957 Limitation Convention the right to limit liability is limited to claims that arise as a result of the acts or omissions of any person:

- on board the ship; or
- in the navigation or management of the ship; or
- in the loading, carriage or discharge of cargo; or
- in the embarkation, carriage or disembarkation of passengers.

However, under the 1976 Limitation Convention, the position is more complicated in that Article 2 lists the claims which *do* qualify for limitation under the convention, and Article 3 lists the claims which *do not* qualify for limitation. The claims which do not qualify for limitation under Article 3 include a salvor's claim for salvage<sup>18</sup> and

17 It appears that this includes bareboat, slot, time and voyage charterers when acting in that capacity. See *The CMA Djakarta*, [2004] 1 Lloyd's Rep. 460 and *The MSC Napoli*, [2009] 1 Lloyd's Rep. 246.

18 For more detailed commentary see Chapter 14 (Salvage Claims).

claims relating to general average contribution,<sup>19</sup> oil pollution,<sup>20</sup> nuclear damage and certain claims by the ship's crew.<sup>21</sup> However, the mere fact that a particular claim is not listed in Article 3 does not mean that the claim is necessarily limitable. The person seeking limitation must also prove that the claim does nevertheless, fall within the provisions of Article 2.

Article 2 appears initially to include most of the types of claim that normally arise during the course of maritime activity but it does not in fact cover everything. For example, although Article 2 includes the following:

*“(a) Claims in respect of loss of life or personal injury or loss of or damage to property (including damage to harbour works, basins and waterways and aids to navigation) occurring on board or in direct connection with the operation of the ship or with salvage operations, and consequent loss resulting therefrom.”*

This wording does not provide the right of limitation in relation to physical damage that has been caused to the ship the tonnage of which is to establish the relevant limitation fund. Therefore, although charterers are 'persons entitled to limit', they would not be able to limit their liability for damage caused to the chartered ship as a result of sending the ship to an unsafe port<sup>22</sup> or as a result of the shipment of dangerous goods.<sup>23</sup> However, damage to a ship other than the ship the tonnage of which is to establish the relevant limitation fund would qualify for limitation. Therefore, a shipowner who established a limitation fund would be able to use that fund to limit his liability for claims brought against him by the owners of another ship with which his ship had collided.

Furthermore, those countries that have ratified the 1976 Limitation Convention and the 1996 Protocol are entitled to make reservations in relation to certain provisions (i.e. to exclude certain parts of the convention). A number of countries have exercised that right in relation to that part of Article 2 which provides that the right to limit liability is available in respect of claims for wreck removal<sup>24</sup> but have done so in different ways. For example, such claims do not qualify for limitation at all in the United Kingdom whilst, in the Netherlands and Norway, there are separate funds purely for wreck removal claims. In the latter circumstance, a shipowner may have to establish two funds – one for claims (other than wreck removal claims) under the 1976 Convention or the 1996 Protocol thereto (whichever is applicable) and another

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19 For more detailed commentary see Chapter 10 (General Average Claims).

20 For more detailed commentary see Chapter 12 (Pollution Claims).

21 For more detailed commentary see Chapter 15 of the *Gard Handbook on P&I Insurance*, 5th edition.

22 For more detailed commentary see Chapter 13.7 (Safe Ports Claims).

23 For more detailed commentary see Chapter 7.4 (Dangerous Goods Claims).

24 For more detailed commentary see Chapter 16 (Wreck Removal Claims).

quite separate fund for wreck removal claims. Therefore, enquiry should be made in each case to ascertain whether the country in which limitation is being determined has made reservations in relation to any particular provisions of the convention.

### 21.3.3.3 Counterclaims

When claims and counterclaims arise as a result of the same occurrence (as would be the case, for example, if two ships were to collide causing physical damage to both) these claims are firstly, set off against each other in accordance with the proportion of liability that is attributed to each ship, and limitation is applied to the balance that remains to be claimed by the one ship. For example, if 50 per cent blame for the collision is attributed to each ship and ship A suffers damage amounting to USD 1 million and ship B suffers damage amounting to USD 2 million, ship A is entitled to claim USD 500,000 from ship B and ship B is entitled to claim USD 1 million from ship A. These claims are then set-off against each other leaving Ship B with a balance of USD 500,000 which it can claim from ship A. If the limitation fund of ship A is less than USD 500,000, ship A can then apply limitation (if available) to reduce its liability further to the amount of the limitation fund.<sup>25</sup>

## 21.3.4 Limitation Procedure

Since the relevant issue is the limitation of *liability*, limitation will become relevant in most cases after the question of liability has been dealt with. However, courts may be prepared in some cases to consider the question of limitation, and, if necessary, rule on that issue, before ruling on the question of liability if it appears that such a procedure may save time and costs overall and encourage settlement of the dispute.

A party can utilise his right to limitation in two different ways. He can either:

- Start a limitation action in which he is named as plaintiff; or
- Rely on limitation as a defence to a claim.

### 21.3.4.1 Limitation Actions

This is the normal procedure when a party fears that a number of claims may be made against him as a result of an incident and he wishes to make sure that his total liability to all claimants will not exceed the global fund. The person seeking to limit appears in the action as the plaintiff and those making claims against him appear as defendants. If, as is often the case, it is not known who all the claimants are, the plaintiff usually names one defendant specifically and describes other claimants in general terms. However, the practicalities of such an action will differ depending upon the procedural rules of the country where the limitation action is commenced.

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<sup>25</sup> For an example see Chapter 6.10 Case Study (Collision Claims).

The traditional rule is that an owner of a vessel who seeks to limit his liability can choose the jurisdiction in which to limit his liability even though the merits of the claim may be determined by another court in another country. It is also the case in some jurisdictions such as the United Kingdom that a party who fears that claims will be made against him in due course can start a limitation action even before proceedings have actually been brought against him. However, in other countries, a shipowner may start a limitation action only if claims have already been made against him in that country. However, limitation is usually a fruitful cause of 'forum shopping'.<sup>26</sup>

Once a limitation action has been commenced the party seeking limitation must normally deposit the global limitation fund plus interest as from the date of the incident with the court that is being asked to make a limitation decree. This fund and any subsequent interest that may be earned on the deposit will be distributed between the various claimants in due course once the court has decided that the applicant is entitled to limit his liability and that the claims that are made against the fund are claims which qualify for limitation. If the court is satisfied that the claimant is entitled to limit his liability, the court will make a limitation decree that (insofar as the court making the decree is concerned) makes a final, global determination of the claimant's right to limit. However, that decree will be binding only in those countries that have adopted the particular convention pursuant to which the decree has been made. Therefore, for example, a limitation decree that has been made in a 1957 Limitation Convention country will not be binding in a 1976 Limitation Convention country or *vice versa*.

If the total quantum of the claims that qualify for limitation exceeds the limitation fund the fund will be distributed between the various claimants *pari passu*, i.e. in accordance with the proportion that each claim bears to the total claims. The manner in which the value of claims is established or proven depends on the procedures that have been adopted by different countries. However, an official appointed by the court normally carries out this function.

If the total claims are likely to substantially exceed the ship's limitation fund, it may be advantageous to the shipowner to apply for a declaration or decree of limitation before determining the merits of liability on the basis that, if the ship is held to be able to limit its liability in any event, the costs of proving liability and quantum may be unnecessary.<sup>27</sup> The English court has been prepared to proceed on such a basis in appropriate cases.<sup>28</sup>

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<sup>26</sup> For more detailed commentary see Chapter 19.2 (Law and Jurisdiction).

<sup>27</sup> See also Chapter 23.5 (Remedies).

<sup>28</sup> See, for example, *The BOS 400*, [1997] 2 Lloyd's Rep. 507.

#### 21.3.4.1.1 *The Limitation Fund as Bar against Arrest and other Action*<sup>29</sup>

A major aim of both the 1957 and the 1976 Limitation Conventions was to ensure that once a limitation fund had been constituted under the particular convention, the ships or other property of the person, on whose behalf the fund had been constituted, should be protected against further arrest or detention. However, this intention has been undermined in the case of the 1957 Limitation Convention by the manner in which some courts have construed the relevant provisions. The courts of some countries have held that such protection is afforded only after the party seeking limitation has proved that he is entitled to limit his liability. Since it may take some time to convince a court of this fact, the ships or other property of the party seeking protection may be vulnerable to arrest in the meantime.

However, the position is much clearer under the 1976 Limitation Convention. Provided that the fund has been established in a country which is a party to the 1976 Convention, the ships or other property of the party seeking the right to limitation are normally protected against subsequent arrest or detention.

#### 21.3.4.2 **Limitation as a Defence to a Claim**

It is possible in many countries for a party that wishes to limit his liability to simply rely on limitation as a defence in any proceedings that a claimant may bring against him. The benefit of relying on limitation as a defence is that the party seeking the right to limit need not commence an action or deposit the limitation fund in court but can simply defend the claim on its merits in the usual way. Therefore, the defendant will simply submit in the court proceedings that he is entitled to limit his liability in the event that the court should decide that he has no other defence to the claim. If it is held in due course that the defendant is liable, and that the claim against him exceeds the global limit of the ship, the defendant can tender the global limit in satisfaction of the claim and judgement will be given against him for the global limit.

However, such a strategy can be risky unless the defendant is certain that no other claims will be made against him as a result of the particular incident. The reason for this is that the global limit is intended to be a cap on all claims that may arise out of the one occurrence and is to be shared proportionately between all such claimants in satisfaction of a limitation decree which is binding on *all* such claimants. Therefore, if the defendant has used the whole of the limitation fund to satisfy

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<sup>29</sup> For more detailed commentary see Chapter 28.7.6 of the *Gard Handbook on P&I Insurance*, 5th edition and pages 74-78 of *Limitation of Liability for Maritime Claims* by Griggs, Williams and Farr, 4th edition, 2005.

a judgement that has been made simply in favour of *one* claimant, he has no protection against any other claim that may be brought against him arising out of the same occurrence. Consequently, the defendant may have to pay an additional sum in satisfaction of these additional claims.

#### **21.4 Insurances<sup>30</sup>**

Shipowners, charterers and all other parties that are entitled to limit their liability by convention or national law must ensure that they make full use of such rights since any failure to do so may mean that they are uninsured for any liability that exceeds the relevant limit. They may also suffer the same disadvantage if they accept contractual terms that have the effect of debarring or prejudicing their right to limit liability.<sup>31</sup>

Furthermore, if the assured is guilty of wilful misconduct this will not only debar his right to limit his liability, but will probably also prejudice his insurance cover under the various standard insurances that shipowners and charterers normally take out.<sup>32</sup> Such conduct will also provide P&I clubs with a defence under the certificates that they are obliged to provide under the CLC<sup>33</sup> and Bunker Conventions,<sup>34</sup> OPA 90,<sup>35</sup> the EU Passenger Liability Regulation No. 392/2009<sup>36</sup> and the 2002 Protocol to the Athens Convention<sup>37</sup> (when it comes into force) since the wilful misconduct of the shipowner is one of the few defences that exonerate the liability of the guarantor under such certificates. Finally, if the pollution Funds are obliged to make payment in such circumstances, they are entitled to claim an indemnity from the shipowners.

The Rules of many P&I clubs also stipulate that a member's right to be indemnified by the club for any sums that they have had to pay to third parties may also be prejudiced if the member has acted recklessly or with wilful misconduct.<sup>38</sup>

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30 For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

31 See *Gard Guidance to the Statutes and Rules* (Guidance to Rule 51 (General Limitation of Liability)).

32 For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

33 See Chapter 12.4.1.1.1.5 (Pollution Claims).

34 See Chapter 12.4.1.1.2 (Pollution Claims).

35 See Chapter 12.4.1.3.3 (Pollution Claims).

36 See Chapter 11.3.3.2 (People Claims).

37 See Chapter 11.3.2.4 (People Claims).

38 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 72 (Conduct of Member)).



## 21.5 Claims Management Issues

The potential right of a defendant to limit his liability is a fundamental issue that must be addressed in the case of most maritime claims since, if the defendant has the right to limit, costs incurred by the claimant in establishing or proving liability may be wasted costs. Furthermore, a failure on the part of an assured to make full use of limitation rights may mean that the assured is uninsured for any liability that exceeds the relevant limit.<sup>39</sup> Therefore, the sooner the merits of limitation are investigated, the sooner both parties can investigate the prospects of a sensible settlement. Limitation also plays an important role in the establishment of a sensible strategy to either pursue or to defend claims particularly since the prospects of limitation can vary substantially in different countries. Therefore, a member who wishes to have the support of his P&I club or Defence insurer to prosecute or defend a claim should discuss this issue at an early stage with such insurers since any failure to do so may prejudice that party's P&I or Defence cover.<sup>40</sup>

The investigation of whether or not a party has the right to limit his liability will often necessitate enquiry into the on board and onshore management systems of the party seeking to limit in order to investigate whether the alter ego of that company is guilty of the conduct that can debar the right to limit. The *alter ego* is normally the individual who has the ultimate decision-making power in the relevant organisation. However, if the *alter ego* has delegated some or all of his functions to a more junior official, that official may also be considered to be the *alter ego* for this particular purpose. The provisions of the IMO's International Safety Management Code (ISM Code) may be used in this connection in order to identify the *alter ego* since shipowners are now required to maintain a Safety Management System (SMS) covering a whole range of safety, environmental and related matters. Under that system, it will be necessary for a ship operator to appoint a 'designated person', with direct access and reporting obligations to the highest level of management. The relevant system must be recorded in writing and it is likely that the relevant documentation must be disclosed in legal proceedings in many countries. Therefore, claimants and defendants must be aware of this possibility and must take care to manage their reporting systems properly.<sup>41</sup>

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<sup>39</sup> See Chapter 21.4 above.

<sup>40</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 82 (Obligations with respect to claims) and Guidance to Part IV (Defence Cover)).

<sup>41</sup> For further commentary see Chapters 3.5.1.2 and 3.5.4 (Cargo Claims.)

## 21.6 Case Study

The APL SYDNEY arrived in Port Phillip Bay in December 2008 and anchored awaiting its berth at the port of Melbourne. Subsequently, the ship dragged its anchor which came into contact with a submarine pipeline which provided gas supplies to various commercial companies in the Melbourne area. These companies brought claims against the owners of the APL SYDNEY for, *inter alia*, the disruption of the gas supply and the consequent disruption to their production facilities which in turn resulted in the need to buy more expensive energy sources and the need to import material from abroad to satisfy their obligations to their customers. The owners of the APL SYDNEY established a limitation fund of approximately AUD 32 million pursuant to the 1976 Limitation Convention as incorporated into Australian law and submitted that it was entitled to limit its liability to such claims pursuant to Article 2.1 of the convention which provides that:

*"... the following claims, whatever the basis of liability may be, shall be the subject to limitation of liability;*

- (a) Claims in respect of ... loss or damage to property ... occurring in direct connection with the operation of the ship ... and consequential loss resulting therefrom";*
- (b) Claims in respect of other loss resulting from infringement of rights other than contractual rights occurring in direct connection with the operation of the ship ..."*

The Australian court held firstly that the claims were either claims for "*consequential loss*" or claims for "*loss resulting from infringement of rights*" which entitled the shipowners to limit their liability. However, the court then had to consider whether the damage was the result of one occurrence or of a series of occurrences since, if the claims were the result of one occurrence, the shipowner was entitled to limit his liability to all qualifying claims by the one limitation fund, whereas if the loss or damage was caused by more than one occurrence, the shipowner was obliged to establish a separate limitation fund for each occurrence and to use more than one limitation fund to satisfy claims. The court held that the claims were caused by two separate occurrences, namely the negligent navigation leading to, and immediately following, the fouling of the pipeline, and the chain of events leading to the subsequent rupture of the pipeline. The court then held that the shipowner was entitled to establish a limitation fund for the first occurrence which would be used to satisfy claims other than those which arose as a result of the separate acts of negligence which caused the second occurrence, and to establish a second and separate limitation fund which would be available to pay all claims that arose as a result of the separate act of negligence which caused the second occurrence. Consequently, the sum of AUD 64 million (i.e. two limitation funds) would be available to satisfy qualifying claims.

## Chapter 22

# Maritime Regulation and Compliance

### 22.1 Introduction

In view of the international nature of shipping it is inevitable that a framework of regulation is necessary and that such regulation should be predominantly international rather than national in nature. However, it is necessary to distinguish between those regulations that are primarily designed to ensure the safety and well-being of life and the environment and which give rise to breaches of the criminal or administrative laws of countries and those that are designed to provide civil compensation for those who suffer loss or damage as a result of breaches of these regulations. This chapter considers the first category of regulations whilst those which provide civil compensation are considered separately in other chapters that comment on specific types of claim. For example, pollution liabilities are considered in Chapter 12 (Pollution Claims) whilst collision liabilities are considered in Chapter 6 (Collision Claims).

Although the regulations that govern the safety and well-being of life and the environment are predominantly international in nature this does not mean that national laws are redundant. Indeed, some countries such as the USA take the view that national regulation is more effective than international regulation. Furthermore, the process of achieving international regulation has proved to be cumbersome as it requires the agreement of a large number of states many of whom have very different requirements and agendas. Therefore, regulation has tended to resemble a quilt with increasingly large areas of international regulation interspaced with smaller areas of regional or national legislation to cover the gaps that arise until further international regulation becomes available.

International or regional regulation is imposed initially through the medium of international conventions whereas national regulation is mostly imposed by national statutes, government decrees and court decisions. However, national statutes are relevant even if a country is a party to an international or regional

convention. Since international conventions are effectively agreements between governments, the instrument that makes the provisions of a convention binding in a particular country is the national statute which makes the convention part of the local law in that country. For example, the instrument that makes the International Safety Management (ISM) Code binding in the United Kingdom is the Merchant Shipping (International Safety Management (ISM) Code) Regulations 1998 of the United Kingdom.

## 22.2 International Bodies<sup>1</sup>

International conventions are generally the work product of various intergovernmental organisations which have a particular interest and responsibility for maritime matters. The most well-known organisations of this kind are:

- The International Maritime Organization (IMO);
- The United Nations Conference on Trade and Development (UNCTAD);
- The UN Commission on International Trade Law (UNCITRAL);
- The International Labour Organisation (ILO);
- The International Oil Pollution Compensation Fund (IOPC).

However, the work of these organisations is influenced by the large number of non-governmental organisations which represent the interests of various sectors of the industry. The following are important examples:

- The Baltic and International Maritime Council (BIMCO);
- The Comité Maritime International (CMI);
- The European Community Shipowners' Association (ECSA);
- The International Association of Classification Societies (IACS);
- The International Association of Dry Cargo Shipowners (INTERCARGO);
- The International Association of Independent Tanker Owners (INTERTANKO);
- The International Chamber of Shipping (ICS);
- The International Group of P&I Clubs;
- The International Maritime Bureau (IMB);
- The International Salvage Union (ISU);
- The International Tanker Owners Pollution Federation (ITOPF);
- The International Transport Workers Federation (ITF);
- The Oil Companies International Marine Forum (OCIMF).

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<sup>1</sup> A list of these international bodies can be found in Chapter 28 (Help Centre).

## 22.3 International Conventions<sup>2</sup>

### 22.3.1 The United Nations Convention on the Law of the Sea 1982 (UNCLOS)<sup>3</sup>

Most of the relevant international conventions implement the provisions of UNCLOS which defines the rights and responsibilities of nations in their use of the world's oceans and which establishes guidelines for maritime activities, the environment and the management of marine resources. UNCLOS is a 'framework convention' which requires states to "take account of", or to "conform to", or to "give effect to", or to "implement" international maritime rules and standards. However, since its provisions are general in nature, they can be implemented only through specific operative regulations in other international agreements that have been developed by, or through, "competent international organisations" such as the IMO (which is one of the seventeen Specialised Agencies of the United Nations) particularly in relation to the adoption of international rules and standards that concern maritime safety, efficiency of navigation, and the prevention and control of marine pollution from vessels. For example, UNCLOS establishes the basic features that govern the exercise of flag state jurisdiction in the implementation of safety regulations and defines the nature and extent of the jurisdiction of the coastal state (e.g. the extent of their territorial waters or exclusive economic zone (EEZ)),<sup>4</sup> but IMO instruments and conventions specify how compliance with safety and shipping anti-pollution regulations should be regulated within that jurisdiction. The implementation and updating of such IMO instruments and conventions is also facilitated by the adoption in many IMO conventions of the procedure known as 'tacit acceptance' of amendments. This procedure enables amendments to enter into force on a date selected by the conference or meeting at which they are adopted unless, within a certain period of time after adoption, they are explicitly rejected by a specified number of contracting parties representing a certain percentage of the gross tonnage of the world's merchant fleet.

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2 Up to date details of how many states have ratified or acceded to any particular IMO convention and a list of which countries have ratified which convention can be found on the IMO website: [www.imo.org](http://www.imo.org). The relevant details can be found under 'Legal/Status of Conventions-Summary' and 'Legal/Status of Conventions by Country'.

3 Over 160 countries and the European Union are parties to the United Nations Convention on the Law of the Sea (UNCLOS) and a detailed commentary on its provisions and on the provisions of the specific IMO instruments and conventions that implement its provisions can be accessed at the IMO website at: <http://www.imo.org/OurWork/Legal/Documents/Implications%20of%20UNCLOS%20for%20IMO.pdf>.

4 In the case of *The Erika* the French Court of Cassation decided in September 2012 that the French court had jurisdiction pursuant to UNCLOS to impose both criminal and civil liabilities arising from the ERIKA incident even though the ERIKA was a foreign-flagged vessel and the sinking had taken place in the Exclusive Economic Zone (EEZ) of France and not within its territory and/or territorial waters.

### 22.3.1.1 Safety at Sea

The basic obligations imposed upon the flag state in relation to safety of navigation are contained in Article 94 of UNCLOS, which requires flag states to take measures for ensuring safety at sea that conform to “*generally accepted international regulations, procedures and practices.*”<sup>5</sup> However, that general requirement is implemented by the following specific IMO conventions:

- The International Convention for the Safety of Life at Sea, 1974 (SOLAS 1974);
- The Protocol of 1988 relating to the International Convention for the Safety of Life at Sea, 1974 (SOLAS Protocol 1988);
- The International Convention on Load Lines, 1966 (Load Lines 1966);
- The Protocol of 1988 relating to the International Convention on Load Lines, 1966 (Load Lines Protocol 1988);
- The International Convention on Tonnage Measurement of Ships, 1969 (TONNAGE 1969);
- Convention on the International Regulations for Preventing Collisions at Sea, 1972 (COLREG 1972);
- The International Convention on Standards of Training, Certification and Watchkeeping for Seafarers, 1978 (STCW 1978); and
- The International Convention on Maritime Search and Rescue, 1979 (SAR 1979).

### 22.3.1.2 Preservation of the Marine Environment

Similarly, Article 192 of UNCLOS provides for the general obligation for states to protect and preserve the marine environment and that general requirement is implemented by the following specific IMO conventions:

- The International Convention Relating to Intervention on the High Seas in Cases of Oil Pollution Casualties, 1969 (INTERVENTION 1969);
- The Convention on the Prevention of Marine Pollution by Dumping of Wastes and Other Matter, 1972 (LC 1972);
- The Protocol Relating to Intervention on the High Seas in Cases of Marine Pollution by Substances Other Than Oil, 1973 (INTERVENTION PROT 1973);
- The International Convention for the Prevention of Pollution from Ships, 1973 (MARPOL 73), as modified by the Protocol of 1978 relating thereto (MARPOL 73/78);
- The Protocol of 1997 to amend the International Convention for the Prevention of Pollution from Ships, 1973, as modified by the Protocol of 1978 relating thereto, as amended (MARPOL PROT 1997);
- The International Convention on Oil Pollution Preparedness, Response and Cooperation, 1990, as amended (OPRC 1990);
- The 1996 Protocol on the Convention on the Prevention of Marine Pollution by Dumping of Wastes and Other Matter, 1972 (LC PROT 1996);

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<sup>5</sup> Articles 94 (3), (4) and (5).

- The Protocol on Preparedness, Response and Cooperation to Pollution Incidents by Hazardous and Noxious Substances, 2000 (OPRC-HNS 2000 );
- The International Convention on the Control of Harmful Anti-fouling Systems on Ships, 2001 (AFS 2001);
- The International Convention for the Control and Management of Ships' Ballast Water and Sediments, 2004 (BWM 2004); and
- The Hong Kong International Convention for the Safe and Environmentally Sound Recycling of Ships, 2009 (HONG KONG SRC 2009).

Articles 212 (3) and 222 of UNCLOS also require states to establish rules, standards and recommended practices and procedures to prevent, reduce and control pollution of the marine environment from or through the atmosphere. Annex VI of the 1978 Protocol to MARPOL and the closely related NO<sub>x</sub> Technical Code 2008 which has been adopted under the tacit acceptance amendment principle establishes Emission Control Areas (ECA) in which stringent limits are imposed for the emission of air pollutants from ships, together with phased-in reductions, to be achieved through engine design or equivalent technologies, in particular for SO<sub>x</sub> and NO<sub>x</sub>.<sup>6</sup>

Several provisions of UNCLOS refer to the jurisdictional powers that states have over foreign ships in their ports for the implementation of measures that may be necessary for the prevention, reduction and control of pollution from vessels. For example, Article 219 of UNCLOS establishes that port states shall take administrative measures to prevent the sailing of vessels which have been found to be unseaworthy and which consequently threaten damage to the marine environment. Accordingly, many states have entered into regional Memoranda of Understanding (MoU) in order ensure that all vessels in that region will comply with international rules and standards for the prevention, reduction and control of pollution from vessels.<sup>7</sup>

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<sup>6</sup> Details of the relevant ECA can be accessed via the IMO website at: <http://www.imo.org/ourwork/environment/pollutionprevention/specialareasundermarpol/Pages/Default.aspx>.

<sup>7</sup> See Chapter 22.3.3 below.

### 22.3.1.3 Compensation for Legal Liability<sup>8</sup>

Article 235 (2) of UNCLOS stipulates that States are obliged to ensure that “recourse is available in accordance with their legal systems for prompt and adequate compensation or other relief in respect of damage caused by pollution of the marine environment by natural or juridical persons under their jurisdiction.” This general requirement is implemented by the following IMO instruments and conventions:

- The International Convention on Civil Liability for Oil Pollution Damage, 1969 (CLC 1969), and the 1992 Protocol thereto (CLC PROT 1992), together known as the 1992 Civil Liability Convention or CLC 1992;
- The International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1971 (FUND 1971), and the 1992 Protocol thereto (the FUND PROT 1992), together known as the 1992 Fund Convention;
- The International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea, 1996 (HNS 1996);
- The International Convention on Civil Liability for Bunker Oil Pollution Damage, 2001 (BUNKER 2001);
- The Protocol of 2003 to the International Convention on the Establishment of an International Fund for Compensation for Oil Pollution Damage, 1992 (FUND PROT 2003); and
- The Protocol of 2010 to amend the International Convention on Liability and Compensation for Damage in Connection with the Carriage of Hazardous and Noxious Substances by Sea, 1996 (HNS PROT 2010).

## 22.3.2 Specific Conventions

### 22.3.2.1 Safety at Sea

The most important international conventions which regulate safety at sea are the following:

#### 22.3.2.1.1 *The Safety of Life at Sea Convention 1974 (SOLAS 1974) and the 1988 Protocol thereto (SOLAS Protocol 1988)*

The SOLAS Convention has a long history. The sinking of the TITANIC in 1912 caused legislators to pay more attention to safety issues in the maritime sector and to the development of internationally uniform standards resulting in the first convention dealing with the Safety of Life at Sea (SOLAS) 1914. The current SOLAS Convention came into force in 1974 and regulates international standards relating to the construction of ships, fire safety measures, life saving appliances, the carriage of navigational equipment and other aspects of the safety of navigation and the carriage of goods.

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<sup>8</sup> For more detailed commentary see Chapter 12 (Pollution Claims).



SOLAS has been adopted by the vast majority of the world's flag states, covering about 96 per cent of the world's merchant tonnage and its provisions are enforced by the country where the vessel is registered (the flag state). Inspectors appointed by the flag state inspect the vessel on a regular basis to ensure that the vessel meets the minimum SOLAS standards. If the vessel meets those requirements, a certificate confirming that fact will be issued, and all countries that have ratified SOLAS accept the validity of these certificates. Port authorities will check the validity of these certificates when a vessel calls at their port, and if the certificates have expired, or there are clear grounds for believing that the vessel or its equipment has not been maintained after the issuance of certificates, the port state has the right to detain the vessel until it can proceed without danger to the ship or persons onboard.<sup>9</sup>

The convention has been amended and updated on numerous occasions since 1974 and to facilitate amendment, the SOLAS Convention employs the 'tacit approval' mechanism which means that an amendment will automatically come into force for all signatory states after a given period of time unless an agreed number of states object. Such 'tacit approval' mechanism has been used to introduce the following international instruments:

#### 22.3.2.1.2 *The International Code for the Safe Operation of Ships and for Pollution Prevention (ISM Code) 1998*<sup>10</sup>

The ISM Code became Chapter IX of the SOLAS Convention in 1994 and has far-reaching implications for all aspects of ship operation, including pollution prevention. Article 1.2.1 of the Code states that its objective is

*"to ensure safety at sea, prevention of human injury or loss of life, and avoidance of damage to the environment, in particular to the marine environment and to property."*

The code obliges ship operators (owners and managers) to implement a quality assurance programme designed to ensure that there are safe practices in ship operation and the working environment. Ship operators must also adopt a "safe management system" designed to ensure compliance with internationally accepted safety rules and standards, and to properly document such compliance. One of the most important requirements is the implementation of an emergency contingency plan to co-ordinate the company's and the vessel's effective response to potential emergency situations.

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<sup>9</sup> See Chapter 22.3.3 below.

<sup>10</sup> Annex to Chapter IX of The International Convention for the Prevention of Pollution from Ships (1973/1978) (MARPOL). For a detailed commentary on the ISM Code see *ISM Code: A practical guide to the legal and insurance implications* by P. Anderson, 2nd edition, 2005, London.

The code requires systems to be closely monitored and for there to be a close analysis of the cause and effect of any non-conformity on the part of the vessel. To facilitate this process, the code requires the ship operators to appoint “a *designated person*” ashore who is to have access to the highest level of management, and to have the authority to be a direct link between the ship and shore management. The “*designated person*” must have the responsibility and the authority to ensure that adequate resources and management support is available to the ship whenever they are required.

If the authorities of the flag state are satisfied that the ship operators are complying with the ISM Code they will issue a Document of Compliance (DOC) relating to the particular operator which is valid for five years subject to annual verification and a Safety Management Certificate (SMC) relating to the particular ship which is valid for five years subject to one intermediate audit. The original SMC and a copy of the DOC must be carried on board and such documents are regularly checked as part of the Port State Control System.<sup>11</sup>

Implementation of the ISM Code necessitates the production of a ‘paper trail’ documenting compliance or lack of compliance. Such documents are normally available to litigants when considering issues such as the seaworthiness of the ship or the right of the operators to limit their liability and can have an important impact on the merits of such litigation.<sup>12</sup> Such documents may also be important when considering whether the operator is entitled to claim under the various insurance policies that a shipowner will normally require.<sup>13</sup>

#### **22.3.2.1.3 *The Convention on Standards of Training, Certification and Watchkeeping for Seafarers (STCW 95)***

Traditionally, the training of seafarers was left to individual governments but this resulted in many instances in casualties which could be traced to unacceptably low standards of training. STCW 1978 and subsequently STCW 95 were designed to implement internationally accepted minimum standards of training, certification and watchkeeping for seafarers worldwide, and introduced a strict compliance procedure whereby countries that supply seafarers to the industry are obliged to submit evidence to the IMO of the proper implementation of STCW training standards.

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11 See Chapter 22.3.3 below.

12 See Chapter 3.5.4 (Cargo Claims).

13 See Chapter 26 (The Structure of Marine Insurance).

Paragraph 6.2 of the ISM Code provides that *"The Company must ensure that each ship is manned with qualified, certificated and medically fit seafarers in accordance with national and international requirements."* However, the details of the required qualifications, certificates etc., are governed by the STCW 95. Therefore, a breach of the requirements of STCW 95 is considered to be a serious breach of the ISM Code.

STCW 95 consists, on the one hand, of a series of legally binding obligations on the flag state administrations and, on the other hand, of a series of interlocking legal obligations on the ship's owners and operators.

- a The flag state of each vessel must:
- Establish suitable training centres and uniform standards of training and competence;
  - Issue its own certificates of competency for its own nationals, and either its own certificates or endorsements of foreign certificates for foreign nationals employed on the flag state's ships;
  - Establish an infrastructure to ensure the orderly administration of the system, and submit evidence to the IMO that the system is being regularly monitored by satisfactory quality standards inspectors.
- b Each shipowning company operating in a contracting state must ensure that:
- All seafarers that are employed on board hold valid certificates of competence for their rank and responsibilities. Officers' certificates must be revalidated every five years;
  - All seafarers undergo medical examination every five years;
  - All seafarers demonstrate that they are able to co-ordinate their actions in an emergency in a common language;
  - All personnel who have safety or pollution prevention responsibilities receive appropriate training;
  - All watchkeeping personnel have the minimally prescribed rest periods;
  - All newly recruited personnel are provided with written instructions in a language that they understand explaining the on board operating procedures;
  - Readily accessible records are kept of each seafarer's experience, competence, training and medical fitness. For the reasons given above,<sup>14</sup> such documents are normally disclosable to litigants and may have an important impact on the merits of a case.

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<sup>14</sup> See footnote 12 above.

A ship, which is required to comply with STCW 95 is subject to control and compliance measures under the Port State Control system.<sup>15</sup> Furthermore, if it is suspected that an incident has arisen because of some negligence or other deficiency on the part of any seafarer, inspectors may assess the competence, training etc., of the particular seafarer at that time.

#### 22.3.2.1.4 *The International Ship and Port Facility Security Code (ISPS Code) 2002*<sup>16</sup>

The ISPS Code was adopted as Chapter IX-2 of the SOLAS Convention in 2002 and is described by the IMO as “a comprehensive **set of measures to enhance the security of ships and port facilities**, developed in response to the perceived threats to ships and port facilities in the wake of the 9/11 attacks in the United States”. The purpose of the code is to provide a standardised, consistent framework for evaluating security risks for ships and port facilities by determining the security levels and corresponding security measures that are appropriate in different circumstances. The code is based on the premise that the security of ships and port facilities is a risk management activity and that, in order to determine what security measures are appropriate, an assessment of the risks must be made in each particular case.

The code consists on the one hand of a series of legally binding obligations on the vessel, her owners and operators and, on the other hand, a series of interlocking legal obligations on the contracting or member governments of the IMO, flag state administrations and port facilities and their administration. The code is composed of two parts:

- Part A is compulsory and sets out the duties and obligations of relevant parties (i.e. shipowners and operators, contracting states and port facility administrations) and mechanisms for discharging these duties; whereas
- Part B is voluntary and contains guidance notes explaining the basis upon which the mandatory provisions of Part A of the Code should be implemented and operated.

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<sup>15</sup> See Chapter 22.3.3 below.

<sup>16</sup> The ISPS Code is implemented through Chapter XI-2 Special measures to enhance maritime security in the International Convention for the Safety of Life at Sea (SOLAS).

- a Each shipowning company operating in a contracting state must
- Make sure that each of its vessels carries on board a ship security plan (SSP) approved by the relevant administration. The SSP is a plan developed to ensure the application of measures on board the ship designed to protect persons on board, cargo, cargo transport units, ship's stores or the ship against the risk of a security incident;
  - Appoint a ship security officer (SSO) for each of its vessels who is responsible for the implementation and maintenance of the ship security plan and for liaison with the management of the vessel and other on-shore authorities;
  - Designate a shore based company security officer (CSO) for each vessel who is to be responsible for monitoring the security of the particular vessel including ensuring that the ship security assessment is carried out, that personnel responsible for the security of the ship are adequately trained, and that there is effective communication between the SSO and relevant administrative bodies;
  - Retain a substantial volume of records relating to training, drills and exercises; security threats and incidents; breaches of security; changes in security level; communications relating to the direct security of the ship such as specific threats to the ship or to port facilities the ship visits; internal audits and reviews of security activities; periodic review of the ship security assessment; periodic review of the ship security plan; implementation of any amendments to the plan; and maintenance, calibration and testing of security equipment, if any, including testing of the ship security alert system.
- b The flag state of each vessel must
- Appoint officers who will verify compliance of the SSP with the requirements of the ISPS Code and, if they are satisfied, issue an International Ship Security Certificate (ISSC) which is normally valid for a period of five years;
  - Review and approve the SSP of each ship flying its flag.

A ship, which is required to comply with the ISPS Code is subject to control and compliance measures under the Port State Control system.<sup>17</sup> A ship must contact the port facility security officer prior to arrival at a port and provide whatever information that is required by the port authority. Whilst security plans are not normally subject to inspection unless an inspector has 'clear grounds' for suspecting an infringement, if a ship is found not to have a valid certificate that ship may be refused entry into the port, or detained in port, or it may be expelled from the port.

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<sup>17</sup> See Chapter 22.3.3 below.

- c Each ISPS contracting state must
- Complete a port facility security assessment (PFSA) for each port facility within its territory and, if necessary, develop and maintain a port facility security plan (PFSP);
  - Appoint a port facility security officer (PFSO) for each port or facility;
  - Set security levels for the ships flying its flag, ships within its jurisdiction, and port facilities within its territory. Security levels range from 1 to 3;
    - Security level 1 establishes the minimum appropriate protective security measures which are to be maintained at all times;
    - Security level 2 is a heightened security level at which appropriate additional protective security measures are to be maintained for a period of time as a result of the heightened risk of a security incident;
    - Security level 3 is an even higher security level at which further specific protective measures should be maintained for a limited period of time if a security incident is probable or imminent, although it may not be possible to identify the specific target;
  - Determine when a Declaration of Security (DOS) should be completed by vessels visiting their ports. The main purpose of a DOS is to ensure agreement is reached between the ship and the port facility as to the respective security measures that each will undertake in accordance with the provisions of their approved security plans.

#### *22.3.2.1.5 The Load Line Convention 1966 as modified by the Protocol of 1988 (ICLL)*

Many ships have been lost as a result of overloading. This convention regulates how much cargo may be loaded on a particular ship (taking into account the season, size and construction of the ship) when arriving at, sailing through or putting to sea in different loadline zones.

The 1998 Protocol introduced a 'tacit approval' mechanism similar to that which applies to SOLAS.

#### 22.3.2.1.6 *The International Regulations for Preventing Collisions at Sea 1972 (COLREGS)*<sup>18</sup>

In the same way that most countries have a 'Highway Code' that establishes the rules which must be implemented by vehicles on public roads, the COLREGS establish the rules with which seaborne vehicles must comply whilst proceeding at sea. The need for such regulations has been recognised since the nineteenth century and the first set of international regulations was introduced in 1897. The COLREGS 1972 have been widely accepted around the world and apply "to all vessels upon the high seas and in all waters connected therewith".

The COLREGS lay down rules of general application and specific rules relating to steering, signalling, lighting etc.

#### 22.3.2.2 **Marine Pollution**<sup>19</sup>

The most important international conventions which regulate marine pollution are the following:

##### 22.3.2.2.1 *The International Convention for the Prevention of Pollution from Ships (1973/1978) (MARPOL)*

The first convention to deal with oil pollution from ships was the International Convention for the Prevention of Pollution of the Sea by Oil from Ships (OILPOL) Convention in 1954. It prohibits the intentional, operational discharge of oil, oily mixtures and residues from vessels within 50 miles of the nearest land, confines ballast discharges to permitted areas and obliges ships to record all loading and discharging operations in an oil record book that can be inspected by government authorities. Subsequently, following the major TORREY CANYON oil pollution disaster in 1967, amendments to the OILPOL Convention were introduced with the aim of limiting the size of tanks on oil tankers, thereby minimising the pollution damage in the event of collision or stranding.

However, although accidental pollution is a more spectacular incident, operational pollution (e.g. that which results from tank cleaning or the discharge of dirty water) has a far greater and wide-spread effect on the global marine environment. Consequently, in 1973, the IMO adopted the MARPOL Convention (1973/1978) which adopted the OILPOL Convention but widened its scope to deal with all kinds of marine pollution not only oil pollution. The MARPOL Convention has been extended and modified by several subsequent protocols and has been widely adopted, but some countries still give effect to OILPOL.

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<sup>18</sup> For more detailed commentary see Chapter 6.2.1 (Collision Claims).

<sup>19</sup> For more detailed commentary see Chapter 12 (Pollution Claims).

The MARPOL Convention is divided into various Annexes. Annexes I and II have compulsory application for member states and deal with the following issues:

- The banning of the operational discharge of oil within 50 miles of the nearest land (as under OILPOL);
- The establishment of how much oil waste may be legitimately discharged over what distances;
- The fitting of oil tankers with filtering systems and slop tanks in order to minimise the risk of pollution when disposing dirty ballast water from cargo tanks, and stricter regulations concerning the survey and certification of ships. It is also mandatory that new oil tankers of 5,000 dwt or more be constructed with double hulls;
- The banning of the discharge of noxious substances within 12 miles of the nearest land and the banning anywhere at sea of a list of 250 noxious liquid substances in bulk.

Annexes III to VI are not compulsory for member states although many states choose to adopt them. These annexes deal with the following issues:

- General regulations relating to the packing, marking, labelling, documentation, stowage, quantity limitations, exceptions and notifications for the prevention of pollution by harmful substances which are carried in packaged form;
- Regulations relating to where and how garbage may be disposed at sea, particularly in the case of 'special areas' which have been identified as being particularly sensitive to the risk of pollution;
- Regulations relating to the emission of sulphur oxide and nitrogen oxide from ship exhausts and the deliberate emission of ozone depleting substances in special emission areas.<sup>20</sup>

Ships (other than very small ships) engaged on international voyages must possess certificates confirming that they comply with the requirements of the convention. Tankers are issued with an International Oil Pollution Prevention Certificate (IOP) if they pass survey satisfactorily. Port authorities will check the validity of these certificates when a vessel calls at their port, and if the ship does not carry a valid certificate, or there are clear grounds for believing that the vessel or its equipment does not correspond with the terms of the certificate, the port state has the right to detain the vessel until it can proceed without being a threat to the marine environment.<sup>21</sup>

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<sup>20</sup> For more detailed commentary see Chapter 2.3 (Bunker Claims).

<sup>21</sup> See Chapter 22.3.3 below.



#### 22.3.2.2.2 *The International Convention Relating to Intervention on the High Seas in Cases of Oil Pollution 1969 and the Intervention Protocol 1973 (INTERVENTION 1969)*<sup>22</sup>

INTERVENTION 1969 gives a coastal state the right to take action outside its territorial sea in order to prevent, mitigate or eliminate grave and imminent oil pollution dangers to its coastline as a result of a marine casualty caused by collision, stranding, fires on board etc. The coastal state may use its own vessels to intervene and the threat of such intervention can often influence the conduct of insurers, shipowners, masters and salvors in the event of a casualty.

#### 22.3.2.2.3 *The International Convention on Oil Pollution Preparedness, Response and Co-operation 1990 (OPRC 1990)*

The EXXON VALDEZ incident in 1989 revealed certain weaknesses in response and preparedness in the event of a major oil spill which required international attention. OPRC 1990 sets out the requirements for on board and land based pollution emergency plans that vessels, offshore drilling units and shore based establishments must have to tackle and minimise such risk. The convention also sets out the requirements relating to mutual assistance and international co-operation in matters such as the exchange of information on the capabilities of states to respond to oil pollution incidents, the preparation of oil pollution emergency plans, the exchange of reports on incidents of significance that may affect the marine environment as well as research and development on combating oil pollution.

#### 22.3.2.2.4 *The Convention on the Prevention of Pollution by Dumping of Wastes and Other Matter 1972 (The London Dumping Convention 1972) and the 1996 Protocol thereto*

This convention regulates the deliberate disposal of wastes and other matter from ships and aircraft as a result of human activity. The 1972 Convention identifies some substances which may never be disposed at sea, some substances which require permits, and some substances that require national approval. However, the 1996 Protocol reverses this partly permissive approach and adopts a restrictive approach. It prohibits the dumping of all substances other than the wastes that are itemised on the so-called 'reverse list' which includes, *inter alia*, dredged material, sewage sludge, fish waste, inert, inorganic geological waste such as mining waste etc. Most countries are parties to the 1972 Convention but fewer countries are parties to the 1996 Convention although the number is constantly growing.<sup>23</sup>

<sup>22</sup> For more detailed commentary see Chapter 16.2.2 (Wreck Removal Claims) and Chapter 11.3 of the *Gard Handbook on Protection of the Marine Environment*, 3rd edition.

<sup>23</sup> Details of which countries are parties to the convention and protocol can be accessed at [www.ilo.org/english/convdisp/1.htm](http://www.ilo.org/english/convdisp/1.htm).

#### **22.3.2.2.5 *The Convention on the Transboundary Movement of Hazardous Wastes and their Disposal 1989 (The Basel Convention)***

There developed in the second half of the twentieth century a trade dealing with the transportation of hazardous materials from developed and highly regulated parts of the world to other less developed and less regulated parts of the world. In a number of cases, ships were refused permission to discharge their cargoes in any jurisdiction resulting in the unacceptable spectre of a volatile cargo that could not find any refuge. The Basel Convention prohibits the carriage of such hazardous waste products and directs countries that are parties to the convention to dispose of such materials within their own territorial limits.

#### **22.3.2.3 Pending Conventions**

In addition to the international conventions which are currently in force there are others which are currently in the process of implementation such as:

##### **22.3.2.3.1 *The Nairobi International Convention on the Removal of Wrecks 2007 (The Nairobi Convention)*<sup>24</sup>**

Intervention 1969 does not entitle coastal states to take intervention action when the relevant casualty does not pose an oil pollution threat. However, the presence of a wreck may nevertheless, cause other concerns to the coastal state. Consequently, it has been thought necessary to develop an international convention which is designed to deal with that problem. The Nairobi Convention will come into force twelve months after it has been either signed without reservation as to ratification, acceptance or approval or has been ratified, accepted, approved or acceded by ten countries.

The convention permits a state party to take reasonable measures to remove a wreck that is a hazard to navigation or the marine environment in the Exclusive Economic Zone (EEZ) of that state. A 'wreck' is defined to include a ship, or any part of a ship, or object that has been on board a ship but has become detached (e.g. cargo, that as a consequence of a maritime casualty has sunk or stranded or is adrift) and includes a casualty that is not yet a wreck but may reasonably be expected to become a wreck. A 'hazard' is defined as a danger to navigation or a condition giving rise to harmful consequences to coastlines or other wider coastal interests such as ports or fisheries, tourism, offshore and underwater infrastructure.

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24 For more detailed commentary on wreck removal see Chapter 16 (Wreck Removal Claims).

### **22.3.2.3.2 *The Hong Kong International Convention for the Safe and Environmentally Sound Recycling of Ships 2009*<sup>25</sup>**

In recent years there has been much debate as to whether the Basel Convention regulates the movement of ships to scrapping yards and this has now resulted in The Hong Kong International Convention for the Safe and Environmentally Sound Recycling of Ships 2009 which is currently open for signature and will come into force 24 months after the date on which 15 states, representing 40 per cent of world merchant shipping by gross tonnage, have deposited instruments of ratification, acceptance, approval or accession with the Secretary General of the IMO.

The new convention recognises the fact that ships that are sold for scrapping may contain environmentally hazardous substances such as asbestos, heavy metals, hydrocarbons, ozone-depleting substances and others and addresses concerns raised about the working and environmental conditions at many of the world's ship recycling locations. Ships that are to be sent for recycling will be required to carry an inventory of hazardous materials and an appendix to the convention contains a list of the hazardous materials the installation or use of which is prohibited or restricted in shipyards, ship repair yards, and ships of those countries that are parties to the convention. Ships will be required to have an initial survey to verify the inventory of hazardous materials, additional surveys during the life of the ship, and a final survey prior to recycling.

Finally, ship recycling yards will be required to provide a 'Ship Recycling Plan', to specify the manner in which each ship will be recycled, depending on its particulars and its inventory. Convention countries will be required to take effective measures to ensure that ship recycling facilities under their jurisdiction comply with the convention.

### **22.3.2.3.3 *The International Convention for the Control and Management of Ships' Ballast Water and Sediments 2004 (BWM Convention)***

The impact on the marine environment of aquatic bio-invasions facilitated by the disposal of ships' ballast water and sediments has been recognised since the 1970s and in 1991 the Marine Environment Protection Committee (MEPC) of the IMO adopted *Guidelines for Preventing the Introduction of Unwanted Organisms and Pathogens from Ships' Ballast Water and Sediment Discharges*. Since that date the MEPC has been considering the problem in great detail resulting in the adoption by the IMO in 2004 of the International Convention for the Control and Management of Ships' Ballast Water and Sediments. The convention will enter into force 12 months after ratification by 30 states, representing 35 per cent of world merchant shipping tonnage.

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<sup>25</sup> For more commentary see Chapter 12.6 (Pollution Claims).

The convention requires all ships to implement a Ballast Water and Sediments Management Plan, to carry a Ballast Water Record Book and to carry out ballast water management procedures to a given standard. In 2006 the MEPC adopted the *Guidelines for approval and oversight of prototype ballast water treatment technology programmes* (G10), which are part of a series of guidelines developed to assist in the implementation of the BWM Convention.

It has been estimated that more than 50,000 ships will have to be retrofitted with a ballast water management (BWM) system at considerable cost to shipowners in order to meet the new standards that will be imposed by the convention.

### 22.3.3 Compliance Systems

There is little point in producing international conventions which are designed to safeguard marine safety if there is no infrastructure for the enforcement of such measures. Countries that are parties to the SOLAS and MARPOL Conventions undertake to introduce legislation that imposes criminal liability and disciplinary procedures for violations of the conventions.<sup>26</sup> However, it is also necessary to develop a system that has wider impact. Consequently, various regional conventions have been concluded with that aim in mind.

#### 22.3.3.1 The Memorandum of Understanding on Port State Control in Implementing Agreements on Maritime Safety and Protection of the Marine Environment 1982 (Paris MOU 1982)

This MOU was originally implemented by the member countries of the European Union but has subsequently been adopted by other non-EU countries. The MOU sets out guidelines for an improved and harmonised system of port state control and strengthened co-operation in the exchange of critical information on ship safety and marine pollution prevention. The MOU was originally intended to implement IMO safety conventions and the International Labour Organisation (ILO) labour regulations but has subsequently been extended to apply to most safety related issues.

The countries that are parties to the MOU agree to carry out inspections of vessels in each other's ports to check on safety and pollution-prevention matters. The inspecting authorities are given the power to demand rectification of serious problems before ships are allowed to sail, and the exchange of information between MOU countries ensures that suspect ships are continuously monitored and that details of sub-standard ships are provided on an internationally accessible website.<sup>27</sup>

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<sup>26</sup> For more detailed commentary on the criminalisation of seafarers see Chapters 12.4.2.2 and 12.4.2.3 (Pollution Claims).

<sup>27</sup> Inspection results can be viewed at [www.equasis.org](http://www.equasis.org). See Chapter 22.3.3.5 below.

### 22.3.3.2 Other Regional Memoranda of Understanding

The success of the Paris MOU has encouraged the adoption of other regionally based MOU such as

- The Memorandum of Understanding on Port State Control in the Asia-Pacific Region 1993 (Tokyo MOU 1993);
- The Latin American Agreement on Port State Control 1992 (Viña del Mar Agreement 1992);
- The Caribbean Agreement on Port State Control 1996 (Caribbean MOU 1996);
- The Mediterranean Memorandum of Understanding (Mediterranean MOU 1997);
- The Indian Ocean Memorandum on Port State Control (Indian Ocean MOU 1998);
- The West and Central African Memorandum of Understanding on Port State Control (West and Central African MOU 1999);
- The Memorandum of Understanding on Port State Control for the Black Sea (Black Sea MOU 2000);
- The Riyadh Memorandum of Understanding on Port State Control in the Gulf Region (Riyadh MOU 2005).

Whilst there are some differences in detail, all of these MOU follow the basic approach adopted by the Paris MOU. Consequently, ships visiting ports situated on all of the world's navigable oceans and seas are now subject to an internationally accepted basis of regulation.

### 22.3.3.4 The Role of Classification Societies

Many of the conventions referred to above require the flag state to produce certificates of compliance. However, the technical and operational issues that are involved make it extremely unlikely that officials of the flag states will have the necessary expertise to perform this task. Consequently, this task is normally delegated to classification societies, albeit that the ultimate responsibility remains with the flag state. Classification societies that wish to perform this task must meet the minimum criteria that are required by the relevant international authorities and, if they do so, are known as 'Recognised Organisations'.

Classification societies exist in order to research, develop and monitor the structural safety of ships. In the majority of cases classification societies provide such services privately to shipowners and ship builders pursuant to contract. However, many third parties (such as charterers, cargo owners and insurers) may also rely on the work of classification societies to ensure that the ship is fit and safe for the particular venture or for the carriage of the goods. When classification societies provide services to shipowners and others on a private basis, the society and its surveyors are normally protected against liability by the terms of the contract which is concluded between them. Classification societies have also tended to escape liability to third parties

in such circumstances when claims have been brought against them in tort<sup>28</sup> or negligence.<sup>29</sup> However, if the classification society is found to be negligent when acting as a 'Recognised Organisation' in the discharge of the obligations that the flag state has under international conventions, the position may be more complex.

In such circumstances, third parties who have relied on the integrity of the relevant certificates may try to bring claims both against the flag state and the classification society. The claim against the flag state may fail if the state pleads sovereign immunity and consequently, third parties may try to sue the classification society as happened in the case of *The Erika* and *The Prestige*. In the case of *The Erika* the French government brought claims against the Italian classification society Registro Italiano Navale (RINA) and the case was heard in the French courts. The French Court of Appeal held that RINA was entitled in principle to rely on sovereign immunity in that it was acting in an administrative capacity as representative of the flag state when renewing the ERIKA's class certificate, but that it had waived that right by voluntarily taking part in the proceedings. The Court de Cassation did not deal with the basic issue of immunity on appeal and merely held that RINA had waived any immunity that it might have had. The French Court of Cassation<sup>30</sup> then went on to hold that RINA had acted with "*imprudence in renewing the ERIKA's classification certificate on the basis of an inspection that fell below the standards of the profession*" and that whilst it was entitled in principle to rely on the channelling provisions of the CLC to escape liability, it could not do so in the case of *The Erika* since it had acted recklessly. Therefore, the court concluded that RINA was both civilly and criminally liable directly to the third party claimants.

Similar proceedings have also been commenced by the Spanish government against the American Bureau of Shipping (ABS) classification society in the US courts in the case of *The Prestige*. At the date of writing the current position is that the US courts appear to be of the view that whilst a classification society acting in such an administrative capacity may owe a duty of care to the flag state that has appointed it, it has not determined one way or another whether it owes a similar duty to other parties. The District Court in New York held that a classification society does not owe a duty "*to refrain from reckless behaviour to all coastal States that could foreseeably be harmed by failures of classified ships.*" However, the Court of Appeal for the Second Circuit preferred not to express an opinion either way, preferring instead to find on the facts that ABS had not acted recklessly which made it unnecessary to consider the wider issue of duty of care.

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28 For more detailed commentary on liability in tort or negligence see Chapter 14 of the *Gard Handbook on P&I Insurance*, 5th edition.

29 See, for example, *The Nicholas H*, [1995] 2 Lloyd's Rep. 299.

30 Details of the judgment that was delivered on 25 September 2012 may be accessed on the IOPC website/Incidents.

Alternatively, if the flag state incurs liability to those third parties who have suffered loss or damage, the flag state may seek an indemnity from the classification society. The merits of such indemnity claims will depend on the terms agreed in the contract between the flag state and the classification society. However, the European Commission has sought to ensure that classification societies should indemnify the flag state in such circumstances by obliging member states to include a duty to indemnify in contracts between the society and the flag state.<sup>31</sup>

#### **22.3.3.5 Trade Associations and Industry Vetting Programmes**

Some trade associations, private industry vetting programmes and other non-governmental organisations also inspect vessels for compliance. Some schemes are ship-based whereas others are company-based. Ship-based programmes such as the Ship Inspection Report (SIRE) Programme that is operated by the Oil Companies International Marine Forum (OCIMF) inspect tankers and oil carrying barges on an industry-wide basis whereas company based schemes inspect only those vessels that are operated by organisations that are members of that organisation. For example, the International Association of Independent Tanker Owners (Intertanko) inspects oil, gas and chemical carriers whereas the International Association of Dry Cargo Shipowners (Intercargo) inspects dry cargo bulk carriers. In some cases, information is provided by such organisations to centrally based statistics-gathering organisations such as the Equasis programme that has been jointly established by the European Commission and the French Maritime Administration and is published by them, whereas in other cases, the information is gathered merely for private use. However, in both cases, the information that is gathered by these organisations is used by charterers and terminal operators as well as governmental bodies as a risk assessment tool.

### **22.4 National Regulation**

The various international regulations that are described above may be given effect in a national context by a national or regional statute. Alternatively, a country that is not a party to the international conventions may apply similar rules through the medium of its own national laws. In both cases, the local laws will often impose greater responsibility and liability than the relevant international conventions.

#### **22.4.1 Regulation in the USA**

Whilst the USA is not a party to any of the international conventions which regulate safety and pollution, it has its own statutes and complex rules which regulate the discharge and escape of polluting substances, the carriage on board of anti-pollution equipment, and general safety standards which are at least equal to those set out under MARPOL 73/78 if not higher. The Vessel General Permit (VGP)

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<sup>31</sup> Directive 2009/15/EC.

program, more particularly known as the National Pollution Discharge Elimination System (NPDES), also sets certain standards for the discharge from ships in US waters of *inter alia*, ballast water, bilge water, graywater, and anti-foulant paints. The program requires ships to monitor, report and maintain certain records relating to the discharge of effluent from ships. Fines for contraventions are very high, criminal prosecution may involve imprisonment, and delays are often inevitable.

The principal federal acts governing safety and marine pollution are The Comprehensive Environmental Response, Compensation and Liability Act, 1980 (CERCLA), the Oil Pollution Act, 1990 (OPA 90) and the Federal Water Pollution Control Act, 1948, as amended (FWPCA).<sup>32</sup> OPA 90 contains regulations relating not only to pollution but also to the licensing and certification of ships' officers, drugs and alcohol testing, the review of criminal records and the establishment of general crewing, equipment, and vessel condition requirements. Furthermore, there are also other federal and state statutes which, individually and collectively, outlaw substandard ships and the discharge of any type of pollutant into waters under US jurisdiction.

The administration and enforcement of these regulations is the responsibility of two US government agencies, the US Coast Guard (USCG) and the Environmental Protection Agency (EPA). The USCG performs a similar function to that performed by other port state control authorities and is empowered to inspect vessels, compliance certificates, Vessel Response Plans (VRP), oil record books etc., and to detain vessels or arrest violators. The EPA is authorised to respond to the release or threat of release of any hazardous substance from any facility or vessel into the environment with emergency removal action, as well as permanent remedial action.

#### **22.4.2 Regulation in the European Union**

The European Union will often implement EC directives to impose liability even when the international conventions to which the member states are parties do not provide a remedy. For example, the EU Directive 2004/35 on environmental liability relating to the prevention and remedying of environmental damage imposes strict liability on the owners of a refinery, jetty etc., of a facility for environmental damage and the duty to pay compensation for costs incurred in cleaning up the environment. Similarly, the Environmental Damage (Prevention and Remediation) Regulations 2009 imposes liability when the CLC and Fund Conventions<sup>33</sup> are inapplicable. Finally, Directive 2005/35/EC seeks to impose criminal liability on seafarers for pollution.<sup>34</sup>

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<sup>32</sup> For more detailed commentary see Chapter 12.4.1.3 (Pollution Claims).

<sup>33</sup> For more detailed commentary on the CLC and Fund Conventions see Chapter 12.4.1.1.1 (Pollution Claims).

<sup>34</sup> For more detailed commentary see Chapter 12.4.2 (Pollution Claims).



Maritime safety is regulated in the EU by the European Maritime Safety Agency (EMSA) which is a 'specialist branch' of the European Commission. EMSA has the responsibility<sup>35</sup> to

- Assist the Commission to prepare, update and develop Community legislation and regulations relating to maritime safety and security, and pollution prevention;
- Liaise between the Commission and the member states in developing and monitoring traffic systems and accident investigations;
- Gather information and data relating to maritime safety, security and pollution.

## 22.5 Seafarers' Working Conditions<sup>36</sup>

Historically, seafarers were often exploited since they had few rights which were often not explained to them. Furthermore, once the ship put to sea, the welfare of the seafarers was very much in the hands – for good or bad – of the ship's master. Matters started to change with the establishment in 1919 of the International Labour Organisation<sup>37</sup> which set out to secure minimum standards for the employment, payment and general welfare of all workers (not just seafarers). However, since 1919, the ILO has promulgated over 65 conventions relating to seafarers, a substantial number of which are still enforced by most of the world's seafaring countries.<sup>38</sup>

It is not possible to comment in detail on the provisions of the large number of individual conventions that regulate labour relations. However, the most important issues that are regulated are the following

### a Continuity of Employment

- The Continuity of Employment (Seafarers) Convention 1976 aims to secure continuous employment by requiring member states to keep a register of seafarers and to provide adequate safety, health, welfare and vocational training for those seafarers;
- The Recruitment and Placement of Seafarers Convention 1996 regulates the terms on which recruitment agencies are allowed to operate and ensures that seafarers are to be allowed basic human rights including the right to belong to a trade union;
- The Seaman's Articles of Agreement Convention 1926 regulates the terms of employment that are to be contained in seafarers' articles;<sup>39</sup>
- The Seafarers' Identity Documents Convention (Revised) 2003 regulates the issuance and contents of seafarers' identity documents; and

35 Pursuant to Regulation (EC) No 1406/2002 (as amended).

36 For more detailed commentary see *The Maritime Labour Convention 2006* by McConnell, Devlin and Dombia-Henry, Martinus Nijhoff Publishers, 2011.

37 The ILO is now an agency of the United Nations. See Chapter 22.2.

38 Full details of such conventions can be accessed via the ILO website at: [www.ilo.org](http://www.ilo.org).

39 For more detailed commentary on seafarers' terms of employment see Chapter 11.2.1.1 (People Claims).

- The Merchant Shipping (Minimum Standards) Convention requires each member state to ensure the minimum safety, social security and living conditions on board.
- b** Qualifications and Fitness for Employment
- The Certification of Able Seamen Convention 1946 establishes the minimum standards required for employment as an able seaman;<sup>40</sup>
  - The Officers' Competency Certificates Convention 1936 establishes similar minimum standards for employment as a ship's master or other officer;
  - The Minimum Age Convention 1973 permits each member state to specify the minimum age at which a seafarer may be employed;
  - The Medical Examination (Seafarer's) Convention 1946 specifies that no person shall be employed as a crew member unless that person produces a certificate signed by a medical practitioner confirming his medical condition and fitness to work on board.
- c** Health and Safety
- The Seafarers' Hours of Work and the Manning of Ships Convention 1996 regulates the maximum number of hours that a seafarer is permitted to work per work period;
  - The Prevention of Accidents (Seafarers) Convention 1970 requires member states to ensure that accidents are reported and properly investigated, and that proper records and statistics are kept.
- d** Accommodation and Catering
- The Accommodation of Crews Convention (Revised) 1949 and the Accommodation of Crews (Supplementary Provisions) Convention 1970 regulates the standard and location on board of accommodation relating to sleep, recreation, sanitation etc., and requires all ship's construction or alteration plans that affect accommodation to approved by a competent authority;
  - The Food and Catering (Ship's Crews) Convention 1946 regulates the quantity and quality of food and beverages on board and requires the master and a senior member of the catering department to carry out regular checks of the hygienic standards of the galley, refectory and food storage locations and to record their findings.

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40 The STCW has additional requirements relating to the qualification of seafarers.

e Seafarers' Welfare and Healthcare

- The Seafarers Welfare Convention 1987 requires member states to ensure that minimum standards of welfare facilities and services are available for seafarers both on board and in port;
- The Shipowner's Liability (Sick and Injured Seamen) Convention 1936 obliges shipowners to pay medical, repatriation, funeral and any other ancillary costs and expenses that may be incurred due to the sickness, injury or death of a seafarer during his period of employment on board;
- The Social Security (Seafarers) Convention (Revised) 1987 requires member states to provide at least three social security benefits out of the following list: sickness benefit, unemployment benefit, old-age benefit, employment injury benefit, family benefit, maternity benefit, invalidity benefit or survivor's benefit;
- The Repatriation of Seafarers Convention (Revised) 1987 obliges shipowners to allow and pay for the repatriation of seafarers in specified circumstances;
- The Unemployment Indemnity (Shipwreck) Convention 1920 obliges shipowners to indemnify seafarers for all losses that they may suffer as a result of unemployment following a shipwreck;
- The Seafarer's Pensions Convention 1946 obliges the employers of seafarers to provide the seafarer with a pension;
- The Seafarer's Annual Leave with pay Convention 1976 obliges employers to pay no less than 30 days of paid leave for each year of full employment.

The Constitution of the ILO gives it the mandate to regularly monitor compliance by member states by requiring member states to make an annual report to the ILO specifying the steps that have been taken to enforce the various conventions. Furthermore, trade unions and other bodies are entitled, on discovering examples of non-compliance, to notify the ILO which can then require the relevant member state to comment. The relevant member state should then bring pressure to bear on the shipowner or employer through its own national laws.

The problem with this system is that it does not provide for action to be taken directly against the ship and relies on the good will of the flag state. In recent years there has been a distinct disenchantment in some parts of the industry with the ability or the readiness of some flag states to enforce the provisions of the conventions with the result that organisations such as the International Transport Workers Federation (ITF) has taken the view that it must intervene directly with shipowners on behalf of seafarers. Such action has frequently resulted in the unofficial detention of ships in port pending negotiation with the particular shipowner.

### 22.5.1 The Maritime Labour Convention 2006<sup>41</sup>

It is obvious that the traditional regulatory regime is seriously fragmented and consequently, the ILO adopted in 2006 the Maritime Labour Convention (MLC) which was intended to incorporate in the one international instrument the fundamental provisions of the preceding plethora of conventions, and to stand alongside the SOLAS, MARPOL and STCW Conventions as the fourth fundamental pillar of shipping regulation.

The convention establishes minimum standards for:

- age, medical condition, training and qualifications, recruitment and placement;
- terms and conditions of employment;
- accommodation, recreational facilities, food and catering;
- health protection, medical care, welfare and social protection.

The MLC achieved the minimum required number of ratifications on 20 August 2012 and therefore, the convention will enter into force on 20 August 2013 as between the countries that have ratified the convention. It is expected that other countries will also ratify the convention in the next few years but in the meantime, those countries that have not adopted the MLC will continue to operate the fragmented system described above. However, the MLC is a useful 'one-stop shop' guide to the various matters that are dealt with separately in the preceding conventions.

The MLC requires the flag state to establish an inspection and certification system to ensure that the minimum standards imposed by the convention are met and also require labour-supplying states to monitor recruitment agencies to ensure that they also comply with such minimum standards. The ship must be issued with, and carry on board, a maritime labour certificate confirming that such minimum standards have been met and compliance is to be regulated by port state control in much the same manner as is currently the case under the conventions described in Chapter 22.3.3 above.<sup>42</sup>

Finally, the MLC requires shipowners to arrange 'financial security' to cover the repatriation costs of seafarers that are abandoned as a result of the bankruptcy of the shipowners. Traditionally, P&I clubs have not provided insurance in such circumstances and, therefore, could not logically provide such security in a form

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41 For further commentary see Gard News Issue No. 194 of May/July 2009 which can be accessed on [www.gard.no](http://www.gard.no) and the ILO website: [www.ilo.org/mlc](http://www.ilo.org/mlc). See also *The Maritime Labour Convention 2006* by McConnell, Devlin and Doumbia-Henry, Martinus Nijhoff Publishers, 2011.

42 To assist inspectors the ILO has promulgated the *Guidelines for Port State Control Officers Carrying Out Inspections under the Maritime Labour Convention 2006* which can be accessed at: [http://brill.nl/MLC\\_2006](http://brill.nl/MLC_2006).

similar to the 'blue cards' or COFRs that they provide for pollution.<sup>43</sup> This issue is currently under review by the International Group but, in the meantime, several clubs including Gard have agreed to cover the risk as from 20 August 2013 subject to a limit which is equal to that club's individual retention under the Pooling Agreement.

## 22.6 The Right of Unhindered Passage

Traditionally, a coastal state has claimed sovereignty over its territorial waters but has allowed foreign flag ships the right of free passage through those waters. The breadth of those territorial waters varied between three and twelve miles from shore depending on the particular coastal state but Article 3 of the United Nations Convention on the Law of the Sea 1982 (UNCLOS) has now fixed the breadth at twelve miles. However, the location of the shore baseline from which the breadth is measured is still open to argument with the result that conflicts continue to arise between contiguous states.

Coastal states also lay claim to a wider sea area known as the Exclusive Economic Zone (EEZ) which is defined in Articles 55 to 75 of UNCLOS as a maximum of 200 miles from the baseline. However, the sovereignty that is exercised relates to rights for exploration in, and the economic exploitation of, the EEZ, which means that the EEZ is considered to be part of the high seas (i.e. international waters) for the purposes of navigation.<sup>44</sup>

### 22.6.1 Regulation within Territorial Waters

Article 17 of UNCLOS obliges a coastal state to allow foreign flag ships the right of innocent passage through its territorial waters and Article 24 obliges the coastal state to notify ships of any danger to navigation of which it is aware. However, this right of innocent passage is subject to restrictions. The following are examples of activities that are not allowed:

- Stopping and anchoring unless this is a natural incident of the particular voyage, or is necessary for safety reasons, or to render assistance to others in distress;
- Activities that are likely to cause pollution;
- The use of force against, or the gathering of information for use against, the coastal state;
- Military activity;
- Fishing activity;
- Research or survey activity;
- Activity that is criminal under the national law of the coastal state.

<sup>43</sup> For further commentary see Chapters 12.3.1.1.1.5 and 12.4.1.3.3 (Pollution Claims).

<sup>44</sup> Article 58 (1) of UNCLOS.

The duty of the coastal state to allow innocent passage has been challenged in recent years as a result of well-publicised cases such as the PRESTIGE when ships have sought entry into territorial waters to seek a port or place of refuge and have been refused entry.<sup>45</sup>

Article 9 of the International Convention on Salvage 1989 also maintains the right of coastal states to intervene in salvage operations pursuant to rights given under other international conventions such as UNCLOS, the Intervention Convention 1969<sup>46</sup> or other regional agreements, and give directions in order to protect its coastline from the threat of pollution. Therefore, coastal states can be expected to exercise such rights and may sometimes do so merely to remove the problem from their coastline to a neighbouring coastline.

Although UNCLOS prohibits coastal states from interfering with the right of innocent passage through territorial waters, it does not deal with the right of coastal states to regulate entry to its ports. Therefore, a coastal state can impose conditions for entry. However, most states see the economic benefit of allowing free passage to and from its ports and do not impose unreasonable conditions. Furthermore, those states that are members of the World Trade Organisation (WTO) agree by virtue of Article V:2 of the General Agreement on Tariffs and Trade to allow freedom of transit through their ports. Nevertheless, ships are obliged when using a port to comply with terms and conditions that are either imposed by a contract between the owner of the port and the ship or by the local law.<sup>47</sup>

### **22.6.2 Regulation on the High Seas (i.e. in International Waters)**

No state has sovereignty over international waters. However, it is necessary in a civilised world to ensure that events and incidents that occur in international waters are subject to the jurisdiction of a particular state. Consequently, Article 9 of UNCLOS provides that ships shall be subject to the jurisdiction of the country of its flag unless jurisdiction is granted to other states pursuant to other international conventions which deal with specific issues.<sup>48</sup> Subject to such other conventions, the flag state has jurisdiction over the ship and on everything that is on it, and also over all personnel that are on board regardless of their nationality.

However, other states may interfere with the jurisdictional prerogative of the flag state in certain circumstances. The most common examples are the following

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45 For more detailed commentary see Chapter 14.7 (Salvage Claims).

46 See Chapter 22.3.2.2.2.

47 See also Chapters 9.2.2 and 9.2.3 (Fixed and Floating Objects (FFO) Claims).

48 For more detailed commentary see Chapter 19 (Law and Jurisdiction).

- Article 110 of UNCLOS entitles the warships of a state to apprehend and, if necessary, board, ships flying the flag of another state on the high seas if there are reasonable grounds for believing that the ship is engaged in unlawful activity such as piracy or slave running. The 2005 Protocol to the Suppression of Unlawful Acts against the Safety of Navigation 1988 affords similar rights when there are reasonable grounds for believing that the ship is carrying explosive, radio-active, biological or chemical weapons;
- Article 111 of UNCLOS entitles a coastal state to engage in the 'hot pursuit' into international waters of ships that are suspected of having committed within the territorial waters or the EEZ of the coastal state various offences against the fishing, customs, immigration, sanitary etc., laws of the coastal state.

When exercising such rights, the use of force is forbidden unless this is necessary to preserve the safety of personnel or to overcome obstruction on the part of the crew of the pursued or boarded ship. In any event, the degree of force must not exceed the minimum amount that is necessary and reasonable in the circumstances.

## 22.7 Insurance<sup>49</sup>

The Rules of most P&I clubs provide that cover may not be available if a member fails to maintain the vessel's classification status or its obligations under the SOLAS, ISM, STCW 95 or ISPS Conventions.<sup>50</sup> The Rules may also provide that the club may cease to cover a member in such circumstances.<sup>51</sup>

## 22.8 Claims Management

Ship operations are regulated by a complex plethora of international, regional and national legislation and it is often difficult for shipowners and operators to grasp the full detail of their requirements. However, it is of the utmost importance that shipowners and operators take their responsibilities seriously and take all necessary steps to make sure that all personnel (whether on board or ashore) understand, comply with, and monitor their responsibilities. In this respect, it is worth repeating Section 1.2.3 of the ISM Code which provides that:

*"The safety management system should ensure:*

1. *compliance with mandatory rules and regulations; and*
2. *that applicable codes, guidelines and standards recommended by the Organization, Administrations, classification societies and maritime industry organizations are taken into account."*

<sup>49</sup> For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

<sup>50</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 8).

<sup>51</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 25.2 (h)).

A failure to comply may not only seriously prejudice the safety and security of the ship and its personnel, but may also have a seriously prejudicial impact on the merits of any claims with which the shipowners or operators may be involved and the various insurances to which they may turn for protection. Shipowners and operators must ensure in particular that they regularly reconsider, and then test, the company's Emergency Response Plan, and ensure that shipboard personnel follow the guidelines set out in the *Gard Guidance to Masters*.<sup>52</sup> Specialist guidance can be given in this respect by many public and private industry organisations.

Shipowners and operators should also ensure that ships carry on board the various certificates and documents that are required by the various international, regional and national regulations. A failure to do so may cause delay at the very least and may result in the imposition of substantial fines or the detention of the ship.<sup>53</sup> A failed inspection may also severely restrict a ship's trading or chartering ability. A list of the most relevant certificates and documents can be found in Annex 1 of the *Gard Guidance to Masters*.

## 22.9 Case Studies

### Case Study 1

A tanker that was heading south was observed to have discharged pollutants in international waters off the Californian coast in 1998. The vessel was identified and the US Coast Guard sought and obtained coastal and flag state permission to board the vessel and to carry out an investigation whilst the vessel was on the high seas off the Central American coast. A criminal charge was brought against the shipowners and a fine of USD 9.4 million was imposed.

### Case Study 2

On 23 July 1998 a fire started on deck 4 of the pure car carrier EURASIAN DREAM while in the port at Sharjah. The fire which was not extinguished by the master and crew, eventually destroyed or damaged the vessel's cargo of new and second-hand vehicles and rendered the vessel itself a constructive total loss. The claimants, who were the relevant cargo interests claimed against the defendant carrier in respect of destruction or damage to the vehicles.

The claimants' case was that the EURASIAN DREAM was unseaworthy in many respects and that there was a wholesale failure by the vessel's technical managers to exercise due diligence to make the vessel seaworthy. At the time of the fire the EURASIAN DREAM was not ISM certificated as she was not obliged to be so yet. Nevertheless the ship was provided with copies of the fleet ISM procedural

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<sup>52</sup> See Chapter 27 (Claims Management) for an illustrated example of the importance of such a plan.

<sup>53</sup> For more detailed commentary see Chapter 8 (Fines and Criminal Sanctions Claims).



documentation and was subject to the same procedures. Notwithstanding the fact that the code was not yet obligatory, the English court agreed with the claimants that *“the ISM Code ... is a framework upon which good practices should be hung”* and that a failure to do so represented a lack of due diligence. The court then went on to find that

- the vessel was provided with a large amount of irrelevant and/or obsolete documentation;
- the documentation placed on board by the managers was too voluminous to be digestible;
- the master was directed by a standard form briefing letter to read all the literature on board the vessel. This was an inadequate means of instructing the master;
- no ship specific manual dealing with fire prevention control was provided to the vessel;
- the Emergency Procedures Manual failed to give proper guidance;
- the fire-fighting instructions (and procedures in particular) that should have been provided in accordance with SOLAS should have been concentrated in one concise and clear manual, catering specifically for the vessel.

The court held that the vessel was not, but ought to have been, provided with specific documentation dealing with

- the characteristics of car carriers in general and the EURASIAN DREAM in particular;
- the carriage of vehicles in general and on the EURASIAN DREAM in particular;
- the danger of fire on car carriers;
- the precautions to be taken to avoid fire on car carriers, including: (i) instructions for the safe handling of second-hand vehicles; (ii) instructions for the supervision of stevedores and the prohibition of hazardous activities by stevedores or others, such as simultaneous and proximate jump-starting and refuelling operations in the same area or on the same vehicle;
- the importance of gas-tight doors in fire fighting;
- the importance of using CO<sub>2</sub> as a front line defence and without delay in the event of a deck fire and simple instructions for its use;
- procedures for evacuating the fire zones or keeping personnel out of such zones.

A reasonably prudent owner, knowing the relevant facts, would not have allowed the EURASIAN DREAM to put to sea with the master and crew, with their state of knowledge, training and instruction. Consequently, the shipowners were liable for the damage caused to the cargo of cars.

### Case Study 3

In 1999 the Maltese flagged ERIKA, which was over 25 years old, broke in two during a storm off the west coast of France and 10,000 tons of fuel oil spread to, and severely polluted, the French coastline. A small coastal community that had been directly affected by the oil spill submitted a claim in the French court against Total, the owner of the oil and charterer of the vessel, for the costs incurred in cleaning up and disposing of the oil. Total argued that since the 'channeling' provisions of CLC 92 made the shipowner exclusively liable for such pollution, Total was, consequently, entitled to escape liability. However, the claimants argued that the oil which had been deposited on the shoreline and which had been admixed with water and sediment constituted "waste" for the purposes of Directive 75/442/EEC of the EU which imposed strict liability on Total as the waste producer for the cost of waste disposal and management without the benefit of any limitation of liability. Therefore, they claimed that Total should pay all the costs arising out of the disposal of that waste notwithstanding the applicability of CLC 92.

The French High Court referred the case to the European Court of Justice (ECJ) for a preliminary ruling on the Waste Directive. The ECJ ruled that:

- hydrocarbons that had been accidentally spilled at sea following a shipwreck and which had become admixed with water and sediment and washed up on the coast of a member state of the EU, constituted 'waste' for the purposes of the EU Waste Directive since the mixture was not commercially exploitable without prior processing;
- the seller of the oil and its owner at the time of the incident were producers of the waste for the purposes of the Directive;
- a producer of the waste was liable without the benefit of limitation of liability if his conduct had contributed to the risk of pollution (for example by lack of diligence in the choice of carrier);
- the liability of a charterer under the Waste Directive can be excluded by the 'channelling' provisions in CLC 92.

The ECJ refused to allow Total France SA to benefit from the exemption of liability of the charterer under CLC 92 on the grounds that the entity within the Total Group that had vetted the ship was not the charterer but the separate company that owned the oil. Therefore, that company was held liable to pay the clean-up costs in full.

The moral of the tale is that, in certain circumstances, victims of ecological damage may be entitled to compensation under regional laws notwithstanding the application of international conventions.

## Chapter 23

# Remedies<sup>1</sup>

### 23.1 Introduction

Maritime claims are truly international and may be governed by the law of many different countries. Legal obligations and legal remedies can differ substantially from country to country and it is beyond the scope of this publication to comment in detail on these differences. However, whilst the terminology and practise can be very different from country to country the fundamental approach tends to be similar. The following commentary is based on the remedies that are normally available under the common law but should be treated with caution for the reasons stated above. Advice should be sought in each case from experienced lawyers who have expertise in maritime litigation under the relevant applicable law.

A claimant will normally consider remedies at two different stages of any litigation – interim remedies and primary remedies. Interim remedies are remedies which a claimant may wish to consider at an early stage of the litigation in order to ensure either that the merits of the claim will be protected pending the full hearing of the claim in due course or that the defendant will have sufficient assets to satisfy any subsequent primary remedy such as a judgement or award for damages.<sup>2</sup> Examples of such remedies are

- Ship arrests;<sup>3</sup>
- Mareva injunctions or Freezing Orders;<sup>4</sup>
- Orders demanding disclosure of documents or the preservation of evidence;
- Stay of actions;
- Anti-suit injunctions.<sup>5</sup>

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1 This chapter should be read in conjunction with Chapter 24 (Security Enforcement Measures). For a general commentary see also Chapter 13 of *Bills of Lading* by Aikens, Lord and Bools, 2006, Informa.

2 For more detailed commentary see Chapter 24.6 (Security Enforcement Measures).

3 See Chapter 24.6.1 (Security Enforcement Measures).

4 See Chapter 24.6.2 (Security Enforcement Measures).

5 See Chapter 19.8 (Law and Jurisdiction).

### 23.2 The Variety of Available Primary Remedies

The most common primary remedies are the following

- Damages;
- Termination of the contract;
- Declarations of liability or non-liability;
- Rectification;
- Permanent injunctions; and
- Specific performance.

The type of remedy that may be available depends on the particular claim. For example, a court may be reluctant to order specific performance of a contract (i.e. an order forcing a party to comply with its obligations) if to do so would be to force a person to perform a task that is contrary to that person's sense of morality. However, it may be prepared to award damages to the other party if the person in question is, nevertheless, contractually bound to perform the contract.

Similarly, it may be that a particular form of remedy may not be an adequate remedy in particular circumstances. For example, the most commonly used form of remedy is a claim for damages which is intended to compensate a claimant for his loss by the payment of a sum of money. However, the payment of a sum of money may not be an adequate remedy in all circumstances. For example, if a charterer required a ship of a certain speed to ensure the regular and timely delivery of cargoes to a customer who required prompt delivery to ensure the continuous production of its factory, and chartered a vessel of the required speed in reliance on the shipowner's promise that the vessel could maintain such a speed, a claim for damages might not be an adequate remedy for the charterers if the vessel persistently steamed at a much slower speed. In such circumstances, a more favourable remedy for the charterer would be the ability, if possible, to terminate the charter since continued bad performance would at the very least undermine his reputation in the eyes of his customer and might also persuade the customer to terminate the contract between him and the charterer. The payment of a financial compensation in such circumstances would probably not be an adequate remedy as it is very difficult to quantify the loss of reputation in financial terms.

### 23.3 Damages<sup>6</sup>

Damages are intended to compensate a party financially for the loss, damage or injury that such party has suffered as a result of the acts or omissions of another party. A commonly used description of damages is the following

*"... that sum of money which will put the party who has been injured or who has suffered, in the same position as he would have been in had he not sustained the wrong for which he is now getting his compensation or reparation."*

When considering damages as a remedy it is normally necessary to consider two separate but linked issues:

- The remoteness of damage; and
- The measure of damage.

#### 23.3.1 The Remoteness of Damage

A party will not always be able to recover financial compensation for all the effects of a wrongful act or breach of contract. In one sense, every event in life is the result of an earlier event and it could truthfully be said in many circumstances that a particular loss or damage would not have occurred but for an earlier wrongful act or breach of contract. However, the public policy of most countries is to recognise the fact that a line must realistically be drawn at some point between events which are the direct result of a wrongful act or breach of contract and which may be compensated by the payment of damages, and events which are too remote from the original wrongful act or breach and which are not subject to compensation by damages.

The precise location of where to draw the line in each case is a notoriously difficult exercise. The English court has stated in the seminal case of *Hadley v Baxendale* that the only loss or damage that can normally be compensated by damages is that which may

*"fairly and reasonably be considered arising naturally, i.e. according to the usual course of things, from the breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it."*

In the case of non-contractual claims in tort or negligence, the test is effectively the same but is applicable at the time that the negligent act or omission is committed.

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<sup>6</sup> For more detailed commentary see *McGregor on Damages*, 18th edition, 2010, Sweet & Maxwell, Chapter 21 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, 3rd edition, 2007, Informa, Chapter 13 of *Bills of Lading* by Aikens, Lord and Bools, 2006, Informa and Chapter 19 of *Scrutton on Chaterparties* by Eder, Bennet, Berry, Foxton and Smith, 22nd edition, 2011, Sweet & Maxwell.

In other words, the particular loss or damage may be compensated by damages only if that loss or damage was foreseeable. In the majority of cases, the court or tribunal will determine that issue by considering whether a reasonable man would, at the time of entering into the contract (in the case of a claim for breach of contract), or at the time of committing the wrongful act (in the case of a claim in tort), consider the particular loss or damage to be a probably foreseeable consequence of his wrongful act or breach of contract. The 'reasonable man' in question will normally be presumed to have that degree of knowledge which would be expected to be available to a reasonable man engaged in the particular trade or activity in question. Therefore, the reasonable expectation of a ship's master will normally be assessed against the standard of a 'reasonably prudent and competent mariner' or that of a shipowner against the standard of a 'reasonably prudent and competent carrier' etc.

However, if a wrongdoer is made aware before entering into the contract (in the case of a claim for breach of contract), or at the time of committing the wrongful act (in the case of a claim in tort), of special circumstances which would result in the innocent party suffering special loss or damage over and above that which could otherwise be expected as a result of that wrongful act or breach of contract, then that 'additional' loss or damage may be considered to be foreseeable for the purposes of the recovery of damages.

### **23.3.2 The Measure of Damage**

If the court or tribunal determines that a particular loss or damage is recoverable as damages it must then go on to determine how to quantify those damages. This is also a notoriously difficult exercise compounded by the fact that different countries may follow different rules. However, a distinction is generally drawn between the measure of damages that are recoverable in tort and that which is recoverable in contract. In the case of tort the measure of damages is that which is necessary to put the innocent party back in the position in which he would have been if the wrongful act or omission had not been committed. However, in the case of a claim in contract, the measure of damages is that which is necessary to put the innocent party back in the position in which he would have been had the contract been performed properly.

#### **23.3.2.2 Claims in Tort**

In the case of claims in tort to property the measure of damages is usually calculated with reference to the cost which it is necessary to incur in order to restore the property to the condition in which it was in before the wrongful act together with any consequential losses such as loss of income during the period of repair. However, it may not be possible in some jurisdictions (particularly in the United Kingdom) to recover damages where a claimant has incurred purely financial loss but no physical damage as a result of a tortious act. For example, the owner of a ship

that has been damaged in port as a result of the negligence of another ship may be entitled to recover both for the physical damage and for any loss of income which it might suffer as a result of the damage. However, if another ship which has not been damaged by the collision is unable to leave the port as a result of the blockage caused by the collision, the owners or charterers of that ship will probably not be able to claim damages for the loss of income caused by the delay to that vessel since their loss is a purely financial loss.

Where the claim relates to injury to the person the calculation is more complicated. Claims for medical treatment and loss of earnings may be capable of assessment in financial terms but it is difficult to calculate pain and suffering or the loss of limbs or other organs or the life of a person in financial terms.<sup>7</sup> Most countries have developed detailed rules which place a particular value on such issues but such values can vary dramatically from country to country. Consequently, such divergence has resulted in a substantial degree of forum shopping in which claimants and defendants seek to have the claim determined in the country which they believe will provide them with the best result.

### **23.3.2.3 Claims in Contract**

In the case of claims in contract the measure of damages is usually calculated with reference to the market value of the property in question. Therefore, if goods are damaged in transit due to the negligence of the carrier the recoverable damages would normally be the difference between the sound market value of the goods at the time when they should have arrived and the actual market value of the goods in damaged condition at the time that they actually arrived.

### **23.3.2.4 Other Principles**

When quantifying loss, the court or arbitration tribunal is also normally guided by a number of principles:

- 1 The innocent party must normally give credit against the claim for any monies that he has saved as a result of the wrongful act or breach of contract, since if this were not so, the innocent party would be profiting from the wrongful act or breach of contract. For example, if shipowners were to claim damages (deadfreight) for the freight that they have lost as a result of the charterers' failure to provide a cargo, the shipowners must give credit against their claim for the voyage expenses that they would have had to bear in order to earn the freight if the charterers had provided a cargo for carriage and which they have, therefore, saved as a result of the charterers' failure to do so.

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<sup>7</sup> For more detailed commentary on personal injury claims see Chapter 11 (People Claims).

- 2 The innocent party has the duty wherever possible to take reasonable steps to mitigate his loss, i.e. to minimise his loss. Therefore, damages are not recoverable for loss or damage which could have been avoided if the innocent party had taken whatever steps that were reasonably possible for him to take in order to avoid or to minimise the loss or damage. However, the innocent party is entitled to include any expenses that he has been obliged to bear in order to mitigate his loss as part of his claim for damages. For example, if charterers were to tender redelivery to shipowners after six months of a ship that had been time chartered to them for one year, the shipowners could logically claim that they have lost the hire that they should have received for the remaining six months. However, the shipowners cannot claim the loss of that six months' hire as damages if it is possible for them to obtain alternative employment for their ship for those six months. If such alternative employment is possible then the shipowners must give credit against their claim for any income that they have received, or should have been able to receive, from the alternative employment less any costs that they have incurred, or would have incurred, in order to earn that alternative income.

In some instances it is not possible for the innocent party to mitigate his losses. For example, because of the recent downturn in world trade, many time chartered ships were redelivered to the shipowners much earlier than had been agreed in the time charter (i.e. cases of underlap).<sup>8</sup> However, because of the downturn in world trade, it was not possible for many shipowners to find alternative employment for their ships for the duration of the time charter. If it is not possible to mitigate losses, the innocent party is normally entitled to claim its losses in full. Therefore, if it was not possible for the shipowners in the example given above to find alternative employment for the remaining six months of the one year time charter, the shipowners would be entitled to claim as damages the full six months hire that they should have received from the time charterers less any expenses that they have saved as a result of the early redelivery.

- 3 Damages are to be awarded on the basis that the guilty party has taken advantage to the maximum extent of any defences that are available to him under the contract or at law. For example, in the case of *The Golden Victory*<sup>9</sup> a ship was time chartered for seven years but was wrongfully redelivered to the shipowners after three years. The shipowners claimed the loss of the remaining four years hire as damages. However, the charter included a clause which provided that either party could terminate the contract if a war broke out between certain countries. Such a war did break out in (what would have been) the fourth year of the charter.

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8 See Chapter 4.5.6.2.1 (Charterparty Claims).

9 [2007] 2 Lloyd's Rep. 164.



The English court awarded damages for one year rather than three years on the basis that the charterers would probably have terminated the charter legitimately on the outbreak of war in any event.

- 4 Notwithstanding the normal rules that determine the quantum of recoverable damages, the party liable may be able to limit its liability to a lower sum pursuant to various international limitation conventions or similar provisions of local law unless it is guilty of conduct which disentitles the right to limitation under the relevant convention or law.<sup>10</sup>

## 5 Penalty Damages

Punitive damages may be awarded in the United States in addition to compensatory damages in cases that involve gross negligence, reckless conduct or wilful failure to pay maintenance and cure, and in cases that involve wilful damage to the environment. Under the general maritime law of the United States, seamen, who have traditionally been treated as 'wards of the court', are able to recover punitive damages and/or attorneys' fees if their employers have failed to pay maintenance and cure without just cause. There are also statutes that specifically permit recovery of penalty or punitive damages. For example, the Seaman's Wage Act<sup>11</sup> permits seamen whose wages have been wrongfully withheld in an arbitrary, wilful or unreasonable manner to recover two days' wages for each day payment is delayed. Until recently, it was thought to be settled law that seamen could not recover punitive damages under the Jones Act for injuries caused by the vessel's unseaworthiness, but this has been called into question by recent jurisprudence in some jurisdictions. In a decision involving the award of punitive damages in the case of *The Exxon Valdez*<sup>12</sup> the Supreme Court suggested that punitive damages in maritime cases should not exceed the amount of compensatory damages, but this too is not yet settled law.

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<sup>10</sup> For more detailed commentary see Chapter 3.2.9.3 (Cargo Claims), Chapter 11.3.2.1 (People Claims) and Chapter 21.3 (Limitation of Liability).

<sup>11</sup> 46 U.S.C. s. 10313(g).

<sup>12</sup> 554 U.S. 471, 513-515 (2008).

### 23.3.3 Agreed Compensation (Liquidated Damages)

In some instances, parties will assess and agree in advance what compensation is to be paid in the event of a breach of contract and will include a clause in the relevant contract to that effect. Such clauses can be found in many contracts but the most common and well-known example is the demurrage clause that is found in most voyage charters. This clause provides that if the charterers take longer than the time that is allowed to them in the charter to load or discharge the cargo (i.e. the laytime) the shipowner is entitled to receive an agreed amount of money by way of compensation (i.e. demurrage).<sup>13</sup>

Another common example can be found in shipbuilding contracts which provide that, if the construction of the ship is delayed, an agreed amount of money is payable for each day of the delay.

Agreed compensation (liquidated damages) clauses are often advantageous to both parties. They may be advantageous to claimants since they have no need to prove exactly how much loss they have suffered in financial terms as a result of the breach of contract. In the absence of an agreed compensation clause such losses may often be difficult to prove. For example, if voyage charterers were to delay the loading of the ship by two days, the shipowners might have difficulty in proving exactly what they have lost as a result. The loss may logically be the loss of an opportunity which does not arise until end of the charter, i.e. the shipowners would have to prove that, if the ship had finished the charter two days earlier, they would either have secured a 'follow-on' charter that was better than the one that they actually managed to secure, or that they would have earned two days additional hire on the open market. Both claims would be difficult to establish whereas the claim for demurrage makes such proof unnecessary. Such clauses may also be beneficial to defendants since they avoid the cost and loss of time which may otherwise be inevitable in litigating or, in any event trying to settle, a claim.

However, such clauses can also be disadvantageous. Since such clauses constitute the agreed compensation for a particular breach, it follows that the innocent party cannot recover additional damages for loss or damage caused by the same breach. For example, if the charter provides that demurrage is to be the agreed compensation for loss resulting from the charterers' failure to complete the loading or discharging within the laydays, the shipowners cannot also claim as damages the additional amounts that they may have had to pay as port fees or agency fees or for additional bunkers. On a more substantial level, the shipowners might not be able

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<sup>13</sup> For more detailed commentary see Chapter 4.5.6.1.1 (Charterparty Claims).

to claim as damages the loss of any 'follow-on' charter that has been cancelled by the 'follow-on' charterers as a result of the current charterers' failure to discharge the cargo within the laytime.

### 23.3.4 Penalty Clauses<sup>14</sup>

Common law courts are normally happy to enforce the terms of agreed compensation clauses since they are happy to encourage parties to control their own affairs in a responsible manner. However, common law courts will not enforce clauses which they consider to be designed to punish rather than compensate. Agreed compensation clauses are normally designed to allow parties to make a reasonable assessment of the financial impact of breaches of contract. However, if a clause provides for the payment of a sum that is considered to be 'extravagant and unconscionable' in the sense that it bears no realistic comparison to the damages that would normally be awarded by a court or arbitration tribunal, such a clause is considered to be a penalty and will not be enforced. However, common law courts are normally reluctant to come to such a conclusion, and so long as the party which seeks to enforce the clause can give a reasonably convincing explanation to justify the level of compensation specified in the clause, the clause will normally be enforced.

### 23.3.5 Interest<sup>15</sup>

The law of most countries entitles a claimant to claim interest on top of recoverable damages since a claimant will rarely obtain compensation immediately. The rate of interest varies from country to country and it is beyond the scope of this commentary to comment in detail in this respect. However, in most cases, a claimant will normally be entitled to a rate of interest which is 1-2 per cent above the LIBOR bank rate.

## 23.4 Termination of the Contract

For obvious reasons this remedy is available only in the case of contractual claims.

Whilst, subject to any exclusion clause in the contract, the party that has suffered loss or damage as a result of a breach of contract is normally entitled to recover damages, it does not necessarily follow that it may terminate the contract. For reasons explained above, termination may be a better remedy in some circumstances. However, if the claimant wishes to terminate the contract he must normally prove either that:

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<sup>14</sup> See paragraph 21.123 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, 3rd edition, 2007, Informa.

<sup>15</sup> See paragraph 13.29 of *Bills of Lading* by Aikens, Lord and Bools, 2006, Informa, and paragraph 21.215 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, 3rd edition, 2007, Informa.

- There is a term of the contract that expressly allows him to terminate the contract; or
- The contractual term that has been broken entitles him to terminate the contract as a matter of law; or that
- The breach amounts to a repudiation of the contract by the defendant.

However, if the claimant does have the right to terminate the contract in such circumstances, he usually also has the right to claim damages for any losses that he has suffered as a result of the other party's breach of contract. In other words, the remedies are cumulative rather than alternative.

### **23.4.1 There is a Term of the Contract that Expressly Allows him to Terminate the Contract**

In some instances parties will have agreed that one party has the right to terminate the contract in the event of a breach of a particular kind by the other party and the contract will include an express clause to that effect. The most well-known examples are clauses that give:

- voyage charterers the right to cancel the charter if a vessel is not ready to load by an agreed date;<sup>16</sup>
- shipowners the right to withdraw a vessel from the time charterers' service and thereby terminate the charter if hire is not paid in accordance with the terms of the charter;<sup>17</sup> and
- the parties to shipbuilding contracts the right to terminate the contract if refund guarantees are not provided in time.<sup>18</sup>

In such instances, the party that wishes to terminate does not need to apply to a court or arbitration tribunal for permission to do so since the other party is contractually bound to allow such a remedy. However, courts and arbitration tribunals will usually construe the words of the clause strictly and, in the event of a dispute, will wish to be satisfied that the party terminating the contract has complied strictly with any formalities or notices that apply to the right to terminate.

### **23.4.2 The Contractual Term that has been Broken Entitles the Claimant to Terminate the Contract<sup>19</sup>**

If there is no express contractual term that allows termination by agreement, the party that wishes to terminate must be able to show that he has the right to do so under the law of the country that governs the particular contract. The laws of

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<sup>16</sup> See Chapter 4.4.3.2.1 (Charterparty Claims).

<sup>17</sup> See Chapter 4.5.1.1.4 (Charterparty Claims).

<sup>18</sup> See Chapter 1.4.9.1 (Building and Sale and Purchase Claims).

<sup>19</sup> For further commentary see paragraphs 1.127 to 1.132 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, 3rd edition, 2007, Informa.

different countries may differ quite substantially in this regard and, therefore, it is not possible to give detailed guidance in all cases. However, the common law classifies contractual terms as:

- Conditions; or
- Warranties; or
- Intermediate (or innominate) terms,

and the remedies that are available depend on which term has been broken.

#### **23.4.2.1 Warranties**

A warranty is a term of less importance, the breach of which will normally allow the innocent party to claim damages but not to terminate the contract. However, it should be appreciated that in the context of marine insurance a 'warranty' is a very important provision.<sup>20</sup>

#### **23.4.2.2 Conditions**

A condition is a term of such importance that any breach of it, no matter how small may entitle the innocent party to terminate the contract forthwith. The contract will rarely specify expressly whether a term is considered to be a condition and therefore, the court or arbitration tribunal will normally have to determine whether the particular term is sufficiently important to justify treating it as a condition. They will therefore, have to try to ascertain the intention of the parties from the words used and the potential impact of the term on the well-being of the contract. The court or arbitration tribunal may be influenced in some instances by phrases which state that a party 'guarantees' to do something since the use of such a strong word indicates that the parties consider that issue to be very important. However, the use of such terms is not conclusive.

Examples of terms that are normally considered to be conditions are the following:

- A clause stating that the ship is fully classed;
- A clause stating that the vessel is 'expected ready to load' by a certain date;
- A clause stating the ship's flag;
- A clause stating that no dangerous or unlawful goods are to be shipped.

However, the issue depends in each case on the words used and the particular facts.

#### **23.4.2.3 Intermediate (or Innominate) Terms**

An intermediate (or innominate) term differs from a condition in that some breaches of the term may have an insignificant effect on the contract whilst other breaches may have a catastrophic effect. Consequently, it is not every breach of

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<sup>20</sup> For more detailed commentary see Chapter 25.2 (The Fundamental Principles of Marine Insurance).

an intermediate term that justifies the innocent party in terminating the contract; the question of whether or not the contract can be terminated depends on the seriousness of the breach and the seriousness of the effect that it has on the contract. The English court has held that a breach of such a term does not entitle the innocent party to terminate the contract unless it could be said that the particular breach:

*"... deprived [the innocent party] of substantially the whole benefit which it was the intention of the parties that he should obtain from the contract."*<sup>21</sup>

Normally, terms which relate to the description of a vessel are more likely to be held to be intermediate terms, e.g. terms describing the ship's speed or bunker consumption or cargo capacity. The English court has also held that a term describing the ship's seaworthiness is to be considered to be an intermediate term rather than a condition since a breach of such a term may have a minor or a major impact on the contract depending on the particular facts. For example, if a ship was obliged to be taken out of service for repairs because of a breach of the seaworthiness provision, such a breach would have a major impact if it occurred during the course of a voyage charter which would normally be expected to last three weeks but a minor impact if it occurred during the currency of a two year time charter which had more than fifteen months still to run. In the first scenario it is likely that the breach would have *"deprived [the innocent party] of substantially the whole benefit which it was the intention of the parties that he should obtain from the contract"* whilst it is probably not so in the case of the second scenario.

**NB!** It must be emphasized that the question of whether the term that has been broken is a warranty or a condition or an intermediate term is a highly technical legal issue which requires the advice of experienced lawyers. Parties should not attempt to terminate a contract without taking legal advice since if a contract is terminated without justification the party doing so will normally be held to have repudiated the contract and that may entitle the other party to terminate the contract and claim damages. This issue is considered next.

### 23.4.3 The Breach Amounts to a Repudiation of the Contract by the Defendant<sup>22</sup>

A party is normally held to have repudiated a contract when he fails to perform his duty under the contract. This must be distinguished from circumstances in which the party does attempt to perform his duties but does so negligently or

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21 *The Diana Prosperity*, [1976] 2 Lloyd's Rep. 60.

22 For more detailed commentary see paragraphs G27 to G33 of *Time Charters* Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

insufficiently. In the latter case there is no repudiation (unless the bad performance is deliberate) whereas there may be repudiation if a party makes no attempt to perform his obligations. Such failure to perform may be either intentional or forced by circumstances, e.g. when the party is bankrupt and cannot honour its payment obligations. Nevertheless, there may be repudiation in both circumstances. Furthermore, there may be repudiation if one party makes it clear before the time of performance falls due that he either intends not to perform that obligation in due course or that he is unable to do so.

If the conduct of a party is sufficient to amount to a repudiation the other party has the right to accept that conduct as a repudiation and thereby terminate the contract and claim damages. In some circumstances, the other party may be obliged to terminate the contract on that basis since a failure to do so may be considered to be a failure to mitigate losses.

### **23.5 Declarations of Liability or Non-liability<sup>23</sup>**

In some instances, the only or main dispute between the parties relates to liability rather than the quantum of loss. In such circumstances, one or both parties may apply to the court or arbitration tribunal for a judgement or award in the form of a declaration of liability or non-liability on the basis that once such a declaration is made, the dispute will either be resolved or will be capable of settlement. In other cases, parties may submit alternative calculations of the quantum of loss to a court or tribunal and ask for a declaration as to quantum. In general, courts and arbitration tribunals are ready and willing to make such declarations since they appreciate that such a service may save substantial costs.

Applications for a declaration can either relate to the whole of the subject matter of the dispute or to one distinct part of it. In complicated cases, it may be advantageous to obtain a declaration in relation to one issue since the resolution of that issue will assist in the disposal or settlement of the wider dispute and avoid the costs that would otherwise be incurred in litigating each and every issue that the case may involve.

It may also be advantageous in some cases to obtain, at an early stage, a declaration on a particular issue which would otherwise have to await resolution of complex issues. For example, it may be advantageous to both parties in the case of a large claim in which the total claims are likely to substantially exceed the ship's limitation

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<sup>23</sup> See paras. 13.44 to 13.45 of *Bills of Lading* by Aikens, Lord and Bools, 2006, Informa.

fund, to apply for a decree of limitation before determining the merits of liability on the basis that, if the ship is held to be able to limit its liability in any event, the costs of proving liability and quantum may not be commercially viable.<sup>24</sup>

Finally, the application for declarations of liability or non-liability may be strategically advantageous in the context of forum-shopping where one party wishes to ensure that the dispute is determined by the court of its choice. In some instances, jurisdiction is determined by the order in which different courts may become seized of the dispute. Therefore, if a party that is potentially liable for a claim is able to secure the jurisdiction of the court of its choice by making an application for a declaration of non-liability before the claimant has started an action to pursue the claim in the court of its choice, the second court may have to stay its proceedings in favour of the court that is to hear the application for a declaration.<sup>25</sup>

### **23.6 Rectification**

Under the common law there may be a binding contract before the terms of the contract are recorded formally in writing. For example, there is a binding contract under the common law once the parties have reached agreement whether orally or, more probably, by exchange of correspondence. Therefore, a written contract that may subsequently be drawn up to record the terms of that contract is merely considered to be written evidence of that earlier contract. Therefore, if the formal contract does not accurately record the terms that have previously been agreed, one or both parties are entitled to apply to the court to rectify the contract, i.e. to amend the terms of the document to record the correct terms.

However, rectification is an equitable remedy and is subject to the same general restrictions that apply in relation to injunctions (see below). Therefore, it is not available in all circumstances. In particular, the party that alleges that the written contract is not a true record must apply to the court promptly for rectification otherwise the court may be increasingly less ready to assist with the passage of time since other third parties may have, in the meantime, acted to their detriment based on terms of the contract that they had understood to be agreed terms.

The same concern will also affect the readiness of the court to allow rectification in the case of contracts which are transferable. The classic example is the 'to order' bill of lading which is initially a contract between the carrier and the shipper but which will, after negotiation (i.e. transfer) to a buyer of the goods, constitute a contract between the carrier and the buyer as endorsee or consignee. The endorsee or consignee will normally have agreed to accept the bill of lading based on the terms

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<sup>24</sup> See also Chapter 21.3.4.1 (Limitation of Liability).

<sup>25</sup> For more detailed commentary see Chapter 19.2 (Law and Jurisdiction).



that are expressly set out in the bill and will not normally be aware of any other terms that may have been agreed between the carrier and the shipper and which are not recorded in the bill. Therefore, once the bill of lading has been transferred by the shipper to a consignee or endorsee, it is not open to either the carrier or the transferee to obtain rectification of the bill to include any other terms that may have been agreed between the carrier and the shipper.<sup>26</sup>

### 23.7 Injunctions<sup>27</sup>

An injunction is an equitable remedy which takes the form of an order of the court that forbids a party from performing certain acts. For example, a court may grant an injunction forbidding a factory from continuing to expel polluting substances into neighbouring rivers or land or forbidding a shipowner from using his vessel to breach international sanctions. A failure to comply with the order constitutes a contempt of court and is punishable by civil or criminal penalties including fines, the imposition of sanctions, or in very serious cases, imprisonment.

Since injunctions are equitable remedies they are not available in all circumstances, common law courts will not usually grant injunctions if:

- The claimant does not come before the court 'with clean hands,' i.e. the claimant's conduct must be free from criticism and the claimant must make full and frank disclosure of all material facts when making the application for an injunction;
- Damages are an adequate remedy and there is no special need for an injunction. A common reason for the grant of an injunction is where it is necessary to protect the reputation of a person or a company pending trial;
- The court is not satisfied that it will be able to enforce the order if the injunction is ignored by the other party;
- The interests of innocent third parties may be adversely prejudiced by the order.

The court has wide discretion whether to grant an injunction at all or merely in limited circumstances or subject to certain conditions. Therefore, depending on the circumstances, injunctions may be temporary or final. However, in the majority of cases, injunctions are temporary since they are designed to maintain the status quo pending a final determination of the issue in dispute.

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<sup>26</sup> For more detailed commentary see Chapter 3.2.4.2 (Cargo Claims).

<sup>27</sup> For a fictional example based on the principles outlined in the *Elbe Maru* [1978] 1 Lloyd's Rep. 206, see the Case Study in Chapter 23.11 below and see also Chapter 24.6.2 (Security Enforcement Measures) and Chapter 19.8 (Law and Jurisdiction).

The application for an injunction is normally made *ex parte*, i.e. in proceedings in which the other party is not represented. Therefore, the court will be asked to grant an injunction based purely on the information provided by the claimant either in person or more usually by sworn affidavit. Consequently, the court will be anxious to ensure that the rights of the other party are not unjustifiably prejudiced and, if the court is persuaded by such evidence that an injunction should be granted, it will often be made subject to conditions. In most cases, the claimant will be asked to confirm that it is ready to indemnify the other party against any losses or damage that it has suffered as a result of the imposition of the injunction if it is determined in due course at a full hearing involving both parties that the injunction was unjustified.

### **23.8 Specific Performance**

Specific performance differs from an injunction in that whilst an injunction is an order of the court *not to do something*, specific performance is an order of the court *to do something*. However, it is also an equitable remedy and is subject to the same general restrictions as discussed above in relation to injunctions. However, orders of specific performance are rarely made where the dispute involves the need for personal services since the court is reluctant to involve itself in the degree of active superintendence that may be required in order to ensure that the order is complied with.

### **23.9 Costs**

It is the usual rule in most (but not all) countries that the winner in litigation is entitled to recover most if not all of its legal costs from the loser. However, the court or arbitration tribunal has a discretion in this respect, and the usual rule may be varied if the court or tribunal considers that some of the costs were unnecessary, or that the winner has caused the costs to be incurred by its own unreasonable conduct. Indeed, the court or tribunal may have the discretion to order the winning party to pay some of the costs of the losing party if it considers that some of those costs were unnecessarily incurred as a result of the unreasonable conduct of the winning party.

The position may also be different in the United States. US courts tend to require parties to bear their own legal costs, including lawyers' fees (with some exceptions for specific items designated under applicable court rules). However, it is important to understand that this general rule may not be applied if there is a contractual or statutory provision to the contrary or the law governing the underlying dispute permits or requires legal costs to be awarded. Arbitrators in the US will award legal costs if permitted by the rules governing the arbitration, by agreement of the parties, or by the law of the applicable contract.

### 23.10 Insurance and Claims Management

The question of which remedy is the appropriate remedy in any particular circumstance is a complex one that requires legal expertise and experience. Therefore, parties are strongly urged to consult their own legal departments, and in the case of doubt, other experienced lawyers, before embarking on any litigation. Should the case involve insurers, care should be taken to ensure that the insurers also agree to any course of action before it is undertaken since otherwise, the relevant insurance cover may be prejudiced. In particular, parties who have defence cover with a P&I club or other legal costs insurers should consult with the club or other insurers before taking any action since the terms of such insurance give the insurers wide authority to control and direct the litigation and such cover may be prejudiced if the insurers are not consulted promptly, or if the recommendations of the insurers are not followed.<sup>28</sup>

### 23.11 Case Study<sup>29</sup>

A liner operator chartered space on a container ship to carry cargoes for its customers from Europe to Asia. The liner operator issued its own form of bill of lading in which it acted as carrier (i.e. a NVOC – non vessel owning carrier). The bill of lading contained a Circular Indemnity Clause in which the cargo owner promised to bring claims solely against the carrier and to indemnify the carrier should it break that promise. The goods were carried on the chartered vessel and were found to be damaged on delivery in Asia. Contrary to the promise contained in the bill of lading, the cargo owners brought claims against the owners of the ship alleging that the shipowners were liable in tort and in bailment and accordingly, did not have the protection of the bill of lading defences. They also threatened to arrest the ship in order to demand security for their claims. The shipowners notified the charterers (i.e. the NVOC) that, if they were held liable to the cargo owners, they would seek an indemnity from the charterers pursuant to the terms of the charterparty. The NVOC applied to the court for an injunction ordering the cargo owners to refrain from bringing the claim against the shipowners arguing that although they would have a claim against the cargo owners in damages for breach of the bill of lading terms, that would not be a sufficient remedy since they would have been obliged in the meantime to incur substantial costs and time in defending the various claims and in providing the shipowner with security for their claims. The court agreed to issue the injunction order since the cargo owners were deliberately breaking the bill of lading terms and to allow the claim to continue would merely force both the shipowners and the NVOC to engage in completely unnecessary litigation.

28 For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV (Defence Cover) and to Rule 82 (Obligations with respect to claims)).

29 This is a fictional example based on the principles outlined in *The Elbe Maru*, [1978] 1 Lloyd's Rep. 206.

If the cargo owners were to ignore the injunction and continue with the claim they would be obliged in due course not only to pay to the NVOG all the sums that they might recover from the shipowners but also any costs that had been incurred by the shipowners and the NVOG in defending the claims under the bill of lading and the charterparty. They would also be in contempt of the court order and vulnerable to a substantial criminal fine if not worse. In such circumstances, it is likely that the shipowners and the NVOG would have had the support of their Defence clubs in defending the claims and in applying for the injunction whereas it is unlikely that the cargo owners would be able to recover their costs under any legal costs insurance that they might have.

## Chapter 24

# Security Enforcement Measures

### 24.1 Introduction

In many cases it can take months if not years before a claim is finalised, and the claimant runs the risk that the defendant may disappear or succumb to financial difficulties in the meantime. This is particularly important if the defendant's sole asset is a ship which may founder, or be sold at any time, or if his assets are liquid assets such as cash which may be quickly moved from place to place. Therefore, unless the claimant is able to obtain quick settlement of his claim or security for his claim, any judgment or award that he may receive in due course may be worthless.

However, a claimant will normally be able to persuade a defendant to offer quick settlement or security for a claim only after he has succeeded in putting pressure on the defendant to do so. Therefore, even if the defendant disputes the validity or quantum of the claim, he may be persuaded to put up security for the claim in the form of a cash deposit or a bail bond or a letter of guarantee or undertaking from his P&I club or other insurers.<sup>1</sup>

### 24.2 Measures to Enforce the Provision of Security

Claimants can normally put pressure on defendants to settle or offer security by the use of:

- Self-help measures; or
- Interim court orders.

However, this distinction is not true in all circumstances. For example, measures which are considered to be pure self-help measures in some countries may require confirmation by a supporting court order in other countries. Therefore, care has to be taken when exercising such measures to ensure that the proper formalities are followed in the relevant jurisdiction.

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<sup>1</sup> See Chapter 24.7 below.

### 24.3 Self-Help Measures

It is normally beneficial for a claimant to have a speedy remedy. If it is necessary for the claimant to obtain that remedy through a court or arbitration tribunal there is likely to be delay whilst the necessary procedures and formalities are completed. Therefore, the laws of most countries provide that claimants are entitled to resort to self-help measures in some instances.

The most common form of self-help is the use of a lien. However, the term 'lien' can be used in the following different senses and it is important to understand which meaning of the term is intended in any particular situation:

- A possessory lien;
- A lien on sub-freights;
- A maritime lien;
- A statutory lien.

#### 24.3.1 Possessory Liens

The most well established form of self-help measure is the right which is given to a claimant to retain property (i.e. to exercise a lien over that property) in order to enforce payment of a debt. For example, a car repairer is normally entitled to retain possession of a car which has been left with him for repair until his repair bill has been paid.

Such a right is used regularly in the shipping industry and its effectiveness has been recognised by the courts. For example, the English High Court has stated that:

*"It has been a feature of shipping practice for many years that the shipowner looks primarily to his lien in case of dispute ..."*<sup>2</sup>

A lien has been defined as:

*"... a defence available to one in possession of (property) who is entitled at common law or by contract to retain possession until he is paid whatever he is owed ..."*<sup>3</sup>

Therefore, if property is subject to a lien, it gives the claimant a right to retain possession of that property until the claim is paid or security is provided for the claim. Possessory liens of this type are regularly exercised by carriers on cargo, by ship builders and repairers on ships etc.

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2 *The Miramar*, [1983] 2 Lloyd's Rep. 319 at p. 324-325.

3 *The Chrysovalandou Dyo*, [1981] 1 Lloyd's Rep. 159 at 165.

The right to exercise a lien on property exists even if the debt is owed by someone other than the owner of that property provided that the owner of the property has consented to the lien. This makes it a particularly effective remedy since, if the party who is liable for the debt refuses to pay, or is unable to pay, it enables the claimant to enforce either immediate payment of the debt, or alternatively, security for payment of the debt, from another party who may not be personally liable for the debt. For example, if a shipowner is entitled to receive freight from a charterer under a charterparty, but the charterer fails to pay, the shipowner may be entitled to exercise a lien on cargo which has been sold by the charterer to a third party consignee if the bill of lading which has been transferred from the charterer to the consignee makes the cargo subject to a lien for that freight.

However, if a claimant purports to exercise a lien on property in circumstances where he is not entitled to do so, he will be depriving the owner of that property of his right to peaceful enjoyment of that property and will probably be liable in damages to the owner of the property.

If a ship builder or repairer exercises a lien on a ship there is normally little complication since he will do so in the jurisdiction where he carries on business and will have experience of what is required in that country. However, where a carrier purports to exercise a lien on cargo, the situation is more complicated since the carrier may do so in a foreign location and may have little experience of what is required in that location.<sup>4</sup> The right of a carrier to exercise a lien on cargo is often subject to:

- legal difficulties; and/or
- practical difficulties.

#### 24.3.1.1 Legal Difficulties<sup>5</sup>

For a lien to be effective it is normally necessary for it to be effective under both of the following systems of law:

- The law that governs the contract of carriage; and
- The law of the country where the lien is being exercised.

A lien is not available in all circumstances and a distinction must be drawn between:

- Liens which exist at law and which do not require the express agreement of the owner of the property; and
- Liens which exist only if the owner of the property has consented to the lien.

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<sup>4</sup> Useful guidance in that regard may be found in the BIMCO publication *Check Before Fixing* which gives a detailed country by country commentary on the right to exercise a lien on cargo.

<sup>5</sup> For more detailed commentary see Chapter 17 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Inform, 3rd edition, 2007.

### **24.3.1.2 Liens which Exist at Law and which do not Require the Express Agreement of the Owner of the Property**

In these circumstances, it is not necessary for the party exercising the lien to prove that the owner of the property has consented to the lien since the lien is given in any event at law and is binding on the owner of the goods with or without express consent. However, not all countries have the same laws and therefore, should a claimant wish to exercise a lien in circumstances where the owner of the property has not expressly consented to the lien,<sup>6</sup> enquiries should be made to ensure that the claimant is entitled to do so under the relevant law or laws.<sup>7</sup>

In the majority of cases, the laws of most countries allow possessory liens to be exercised on cargo in the following circumstances regardless of the need for consent on the part of the owners of the cargo:

- A carrier of goods is entitled to exercise a lien on cargo for:
  - Freight which is payable on delivery of that cargo;<sup>8</sup>
  - That cargo's contribution to General Average;<sup>9</sup>
  - Expenses incurred in preserving that cargo;<sup>10</sup>
- A salvor is entitled to exercise a lien on a ship, cargo, containers, bunkers or any other property at risk that is to contribute to the salvage award.<sup>11</sup>

### **24.3.1.3 Liens which Exist only if the Owner of the Property has Consented to the Lien**

If a claimant wishes to exercise a lien in circumstances other than those described in Chapter 24.3.1.2 then he must normally prove in one way or another that the owner of the goods has consented to the goods being subject to a lien for the particular claim. In practice, the relevant consent is normally proved by the existence of a lien clause in the contract between the claimant and the goods owner. The most usual scenario in which this type of lien is relevant is when a carrier of goods wishes to exercise a lien on the cargo that is being carried for claims which arise under the contract of carriage, e.g. claims for demurrage, damages for detention, hire etc.

In the majority of cases, the relevant contract of carriage between the carrier and the cargo owner will be a bill of lading or sea waybill. Therefore, if the claim arises under that bill of lading or sea waybill, and that contract provides expressly that the carrier has the right to lien the cargo for such claims, the carrier can normally prove

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6 See Chapter 24.3.1.3 below.

7 See Chapter 24.3.1.6 below.

8 For more detailed commentary see Chapter 4.5.1.2.1 (Charterparty Claims).

9 For more detailed commentary see Chapter 10.6 (General Average Claims).

10 For more detailed commentary see Chapter 10.8 (General Average Claims).

11 For more detailed commentary see Chapter 14.2 (Salvage Claims). Such a lien may also constitute a maritime lien – see Chapter 24.4 below.



that the goods owner (the receiver) has thereby consented to the lien. The same applies if the relevant contract of carriage between the carrier and the cargo owner is a charterparty and the charterparty provides expressly that the carrier has the right to lien the cargo for such claims.

However, if the relevant contract of carriage between the carrier and the cargo receiver is a bill of lading or sea waybill but the claim lies against the charterer under a charterparty, then the mere fact that the charterparty purports to give the shipowner a lien over the cargo for claims arising under the charterparty is not sufficient to prove that the receiver is bound by such lien clause since the relevant lien clause is in a contract to which the receiver is not a party. The cargo will be subject to a lien in such circumstances only if the carrier proves that:

- The bill of lading or sea waybill has a similar lien clause; or that
- The lien clause in the charterparty is effectively incorporated into the bill of lading or sea waybill.

It is only in such circumstances that the carrier can prove that the receiver has consented to the lien.

If the relevant incorporation clause in the bill of lading or sea waybill incorporates the charterparty lien clause specifically (e.g. *“The lien Clause 8 of the charter dated ... is hereby incorporated”*) the shipowner is normally entitled to exercise a lien on cargo owned by the receiver. However, if the relevant incorporation clause in the bill of lading or sea waybill merely refers generally to the terms of the charter (e.g. *“All the terms, conditions and exceptions of the charter dated ... are hereby incorporated”*) the shipowner would normally be entitled to exercise a lien on cargo owned by the receiver only if it was not necessary to change the wording of the charterparty lien clause in order to make it sensible in the context of the bill of lading or sea waybill. For example, a charterparty lien clause which provides that:

*“Owners shall have a lien on the cargo for freight, dead-freight, demurrage and damages for detention”*

requires no change of wording to make sense in the context of a bill of lading or sea waybill and may therefore, be binding on a third party receiver under such contracts.<sup>12</sup>

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<sup>12</sup> For more detailed commentary see Chapter 17.16 to 17.18 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition, 2007.

However, if the claim arises under a time charter, then it is extremely unlikely that a lien clause in the time charter purporting to give the shipowner a lien on cargo for such a claim will provide the shipowner with a realistic remedy in practice. Firstly, it is usually unlikely that the time charterer will be the goods owner, and it is likely that the goods will be owned by a third party receiver and carried under a bill of lading or sea waybill. Secondly, it is unlikely that such a bill of lading or sea waybill will have a specific lien clause giving the shipowner the right to lien the cargo for claims arising under a time charter. Finally, it is unlikely that a bill of lading or sea waybill can validly incorporate a time charter lien clause since it normally makes little sense for bills of lading or sea waybills (which are contracts based on geography) to incorporate the terms of a contract based on time. For example, a time charter lien which is intended to enforce payment of hire, bunkers etc., does not usually make sense in the context of a bill of lading.<sup>13</sup>

#### **24.3.1.4 For What Amounts can the Lien be Exercised?**

Unless the lien clause states otherwise (which would be unusual) a lien can normally be exercised only for amounts which have accrued due by the time that the lien is exercised, i.e. a lien cannot usually be exercised for future debts. For example, a lien can be exercised on Monday for demurrage which has accrued due by Monday but not for further demurrage which will be incurred by the following Friday even if it is clear on Monday that the ship will still be detained until the following Friday. However, if further demurrage is subsequently incurred between Monday and the following Friday, the shipowner can increase his lien demand to include that additional demurrage on Friday.<sup>14</sup>

#### **24.3.1.5 The Exercise of the Lien**

In the majority of countries a lien can be exercised without any formalities. However, in some countries it is necessary to obtain an order from the local court.<sup>15</sup> Therefore, it is good practice to take legal advice from an experienced local lawyer before attempting to exercise a lien since, if local requirements are not satisfied, the party purporting to exercise the lien may incur liability and/or fines.

Once possession of the cargo is lost, the right to lien is normally lost.<sup>16</sup> Therefore, it is very important for the carrier to ensure that he retains control of the cargo and this can usually be done best by retaining the cargo on board. If the carrier cannot

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<sup>13</sup> For more detailed commentary see Chapter 30 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

<sup>14</sup> See Paragraphs 17.31 to 17.34 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition, 2007 and paragraph 30.38 of *Time Charters* Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

<sup>15</sup> See footnote 4.

<sup>16</sup> See paragraph 17.28 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition, 2007.

exercise secure physical control over the cargo ashore, he is entitled to withhold delivery of the goods and to claim demurrage or hire whilst the ship is being detained for this purpose. However, this may create possible difficulties for the carrier. If the ship is delayed, this may have an effect on subsequent voyages and, if the delay occurs at the end of the charter, the shipowner may miss the cancellation date under his next fixture with the result that his 'next' charterer may exercise his option to cancel the next fixture.<sup>17</sup>

Alternatively, if the shipowner decides to discharge the cargo and exercise the lien ashore, he must rely heavily on the trustworthiness of whoever is appointed to act as his agent to supervise the exercise of the lien. Furthermore, the warehouseman or other party that will store the cargo will normally look firstly to the shipowner for reimbursement of his storage charges. Unless the lien clause in the relevant contract of carriage expressly extends the ambit of the lien to include the storage charges<sup>18</sup> and/or provides the right to sell the cargo,<sup>19</sup> then, if the lien is not released,<sup>20</sup> the shipowner may have to apply to the local court for an order allowing the cargo to be sold to cover such charges. It should also be appreciated that when property is sold pursuant to a court order, the price that can normally be obtained for such property is lower than the price that could be achieved on the open market.

#### 24.3.1.6 Practical Difficulties

Even if the shipowner proves that the lien is legally effective both under the law that governs the contract of carriage and under the local law he may still be unable to exercise his right to lien because of practical difficulties at the place where the lien is being exercised. For example, the local authorities may not allow a lien to be exercised on board ship since the anchorage area is congested. Similarly, there may not be sufficient storage space to enable the lien to be exercised ashore. Therefore, the shipowner might prefer in some cases to try to exercise the lien before the voyage is completed. However, in normal circumstances, a shipowner must complete the voyage to the discharge port before he can exercise a lien and it is only in exceptional circumstances that he is entitled to do so before reaching the discharge port.<sup>21</sup>

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<sup>17</sup> For more detailed commentary see Chapter 4.4.3.2.1 (Charterparty Claims).

<sup>18</sup> A lien clause does not normally include the cost of storage. See paragraphs 17.37 to 17.38 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition, 2007.

<sup>19</sup> A lien clause does not normally allow the person exercising the lien to sell the cargo. See paragraphs 17.28 of *Voyage Charters* by Cooke, Young, Taylor, Kimball, Martowski and Lambert, Informa, 3rd edition, 2007.

<sup>20</sup> See Chapter 24.3.1.7.

<sup>21</sup> See paragraphs 30.14 to 30.16 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

### 24.3.1.7 Releasing a lien

If the lien is exercised in respect of a claim which is undisputed then the lien can be released by payment of the claim. However, if the merits and/or the quantum of the claim is disputed, there may be a reluctance on the part of the party that is subject to the lien to pay the claim. In such circumstances, the law of most countries provides a remedy in that the lien can be released by a payment of the sum claimed into court to await resolution of the dispute on its merits, i.e. the payment into court acts as alternative security to that provided by the lien. Alternatively, the lawyers of the respective parties are often instructed to pay the sum in dispute into an escrow account that has been opened in their joint names to await resolution of the dispute on its merits. This alternative usually has the advantage of less formality and the attraction that higher interest rates are normally paid on the joint escrow account.

### 24.3.2 Liens on Sub-Freights<sup>22</sup>

Many time charters purport to give the shipowner the right to lien 'all sub-freights'. However, this remedy is not a 'lien' in the strict sense of the word since the shipowner cannot have physical possession of the sub-freights; he is merely given the right to give notice to the party which is obliged to pay freight to the time charterers under a sub-charter, bill of lading, sea waybill etc., (i.e. sub-freight) that following receipt of the notice, the sub-freight should be paid to the shipowner not to the time charterers. Therefore, it is a form of self-help remedy which is not based on physical possession of any property.

The right to lien sub-freights is a purely contractual remedy which is normally allowed to shipowners by the express provisions of a time charter and is normally available when the time charterer has failed to pay hire or other sums due under the head time charter. Classic examples of sub-freights would be freight payable to the time charterers when they act as carriers under bills of lading (i.e. under charterers' bills)<sup>23</sup> or which is payable to the time charterers as disponent owners under a sub voyage charter.

A lien on sub-freights has been described as follows:

*"The lien operates as an equitable charge upon what is due from the shipper to the charterer, and in order to be effective requires an ability to intercept the sub-freight (by notice of claim) before it is paid by shipper to charterer."*<sup>24</sup>

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<sup>22</sup> For more detailed commentary see paragraphs 30.17 to 30.31 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

<sup>23</sup> See Chapter 3.2.4.1 (Cargo Claims).

<sup>24</sup> *The Nanfri*, [1979] 1 Lloyd's Rep. 201 at 210.

### 24.3.2.1 The Giving of Notice

The right of the shipowner to demand payment of sub-freights to him is triggered by the giving of notice to the party who is obliged to pay the sub-freight. The notice does not have to be in any particular form but it must make it clear that payment is to be made to the shipowner and not to the time charterers. So long as the notice is received by the party who is to pay the sub-freight before he has in fact done so then he is obliged to make payment to the shipowner. If he ignores the notice and pays the sub-freight to the time charterer he remains liable to pay the same sum to the shipowner, i.e. he may have to pay twice. However, if the party who is to make payment has already made payment to the time charterers before he receives the notice, then he is under no further duty to pay that sum to the shipowner, i.e. the notice is given too late.<sup>25</sup> A classic example is when the sub-freight has been prepaid.

The shipowner is entitled to give notice that the whole of the sub-freight should be paid to him even if the sub-freight is in fact in excess of the sums which are owed to him under the time charter. However, the shipowner is obliged in such circumstances to account to the charterer for any sums received by him which are in excess of the sums owed under the time charter.<sup>26</sup>

### 24.3.2.3 The Meaning of 'Sub-freights'

The right to exercise a lien on 'sub-freights' includes the right to intercept freight that is payable under a sub-sub-charter provided that there is a right to lien 'sub-freights' in both the head charter and the underlying sub-charter. For example, if a shipowner time charters his ship to A, who sub-charters to B, who sub-sub-charters to C, the shipowner is entitled to exercise a lien on the freight that is payable by C to B as well as the freight that is payable by B to A provided that there is a right to lien 'sub-freights' in both the head charter between the shipowner and A and in the sub-charter between A and B. However, if there is no right to lien 'sub-freights' in the sub-charter between A and B, the shipowner cannot exercise a lien on the freight that is payable by C to B.

It is unclear whether the right to lien 'sub-freights' includes the right to lien 'sub-hire', i.e. hire paid under a sub-time charter.<sup>27</sup> In order to avoid this difficulty the wording of some modern time charters has been extended to provide for a lien on 'all sub-freights and/or sub-hire'.

<sup>25</sup> See paragraph 30.29 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

<sup>26</sup> See paragraph 30.25 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008.

<sup>27</sup> See paragraph 30.31 of *Time Charters* by Coghlin, Baker, Kenny and Kimball, Informa, 6th edition, 2008 and *The Bulk Chile*, [2012] 2 Lloyd's Rep. 594.

#### 24.3.2.4 Legal and Practical Difficulties

A lien on sub-freights is a concept that is based on common law principles. Therefore, the shipowner may face practical problems in enforcing his right to receive the sub-freight if the cargo owner is resident in a foreign country which is not familiar with common law principles and concepts. If the cargo owner ignores the notice to pay, the shipowner may need the assistance of the foreign court in order to enforce the lien on sub-freights, and there is a significant risk that the court may refuse to order the cargo owner to make payment to the shipowner. However, the position may be different if the cargo owner is domiciled in the European Union since an order of the English court ordering payment of sub-freight to the shipowner may be enforceable in all other countries of the EU without any reconsideration of the merits of the judgment pursuant to the provision of the European Regulation (EC) 44/2001 of 22 December 2000 on Jurisdiction and Enforcement of Judgments in Civil and Commercial Matters (The EU Regulation).

#### 24.4 Maritime Liens

A maritime lien is not a self-help remedy in the true sense since it is a right that is given to certain claimants without the need for any action on their part. Furthermore, it is not a lien in the same sense as a possessory lien since it is not based on the physical possession of any property. Therefore, it does not provide the lienor with the means to enforce immediate payment of the claim or the provision of security. Nevertheless, it provides a claimant with some measure of security for the claim in the event that the defendant's ship or other property may subsequently be sold.

A maritime lien is a right to bring *in rem* proceedings<sup>28</sup> against a vessel, cargo, containers, bunkers etc., which attaches automatically as a matter of law at the time of the event which gives rise to the claim and which remains in force despite any subsequent sale or transfer of that property. It is a lien which creates a form of secured right in property that is owned by someone else and therefore, has important privileges which are not available in the case of other claims. For example, a party which incurs loss as a result of a collision acquires a maritime lien which will normally enable him to arrest and serve *in rem* proceedings on the offending vessel even though the ship may have been sold to a new owner between the time of the collision and the time of the arrest.

Consequently, a maritime lien 'follows the ship' and the new owner is bound by it even though he was not in fact the guilty party which caused the collision. Therefore, a maritime lien is a kind of interim measure which preserves the ability of the claimant to obtain security in due course even if the ship has changed ownership in the meantime. Consequently, a buyer acquires a vessel which is free of maritime liens only when the

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<sup>28</sup> For more detailed commentary see Chapter 19.4 (Law and Jurisdiction).

vessel has been sold by order of the court after an arrest. A private sale does not have that result. Therefore, a buyer of a ship otherwise than under a court sale should ask the seller to confirm that he is selling a vessel which is free of maritime liens and require an indemnity in the event that there is a subsequent breach of that representation. The most commonly used sale forms (such as the Norwegian Sale Form) contain an undertaking that the ship that is being sold is free from encumbrances and liens. However, the practical value of such a promise is questionable unless the promise is either given or supported by a worthwhile guarantor.

Not every type of claim gives rise to a maritime lien and, if the particular claim does not do so, then the claim gives no right *in rem* against the ship but merely a right *in personam*<sup>29</sup> against the party that caused the loss or damage. It follows that the claim will not 'follow the ship' in such circumstances, and that the claimant will not be able to arrest her and bring *in rem* proceedings against her in her new ownership since the new owner did not cause the loss.

The International Convention on Maritime Liens and Mortgages 1993 is not yet in force. Therefore, the question of what is or what is not a maritime lien depends on the local law of individual countries. It is not possible to state definitively what is or is not a maritime lien as different countries follow different approaches. The most common forms of claim which give rise to maritime liens are claims for:

- Salvage;
- Pilotage;
- Towage;
- Collision damage;
- Crew wages;
- Master's disbursements.

However, many countries consider that maritime liens also include claims for:

- Necessaries that have been provided to the vessel (e.g. bunkers, supplies, repairs etc.);
- Cargo damage;
- General average;
- Breaches of charterparties;
- Harbour dues;
- Wreck removal expenses.

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<sup>29</sup> For more detailed commentary see Chapter 19.4 (Law and Jurisdiction).

Therefore, it is very important that advice is sought before steps are taken to arrest a ship after she has changed ownership since, if the claim does not qualify as a maritime lien in the country of arrest, the party arresting may be liable in damages for wrongful arrest.<sup>30</sup>

Where, following the arrest of a ship, claims are made which exceed the value of the ship, it is necessary to consider which claims have priority over other claims since the proceeds of the sale of the ship will not be sufficient to satisfy all claims. Normally, maritime liens have priority over most but not all other claims but the ranking of maritime liens *inter se* varies as different countries follow different approaches.<sup>31</sup>

### 24.5 Statutory Liens

A statutory lien is similar to a maritime lien but with the difference that the right to bring *in rem* proceedings against a vessel, cargo, containers, bunkers etc., despite any subsequent sale or transfer of that property does not arise automatically on the occurrence of the event which gives rise to the claim. Statutory liens are created only when *in rem* proceedings are actually commenced. Therefore, if a ship has been sold before *in rem* proceedings have been commenced, the claim does not 'follow the ship' and the claimant cannot subsequently arrest the ship in respect of the claim. However, if *in rem* proceedings have been commenced before the change of ownership then the claim will normally 'follow the ship' as in the case of a maritime lien. Therefore, statutory liens do require some degree of court involvement since *in rem* proceedings require the consent of the court to commence the proceedings. However, they do not require any further formal court orders.

Statutory liens also do not normally have the same priority as maritime liens but rank ahead of other claims. However, it must be emphasised again that much depends on the local law of individual countries.<sup>32</sup>

Since statutory liens are created when *in rem* proceedings are commenced it follows that there can only be statutory liens for those claims which fall within the *in rem* jurisdiction of the courts of a particular country. Such courts do not have *in rem* jurisdiction to hear every type of claim that can be brought in respect of a maritime incident or dispute. Again, much depends on the local law of individual countries.<sup>33</sup>

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30 See Chapter 24.6.1.2 below.

31 See Chapter 24.6.1.3 below.

32 See Chapter 24.6.1.3 below.

33 See Chapter 24.4 above.



## 24.6 Interim Court Orders

The laws of most countries entitle claimants to apply to their courts for interim orders to attach a defendant's assets in order to enforce the provision of security. Such applications can normally be made even though the court in question may not consider that it has jurisdiction to determine the merits of the claim. Any order that the court may make will therefore be an interim measure in support of future proceedings on the merits which may take place either in the same court or in the courts of a foreign country. In the latter event, the court making the interim order will normally stay any further proceedings in that court pending resolution of the merits of the claim in the foreign court, but it may also hold the proceedings in abeyance in the event that the claimant may need to revert to the court to enforce the security in due course.

The most common forms of interim court orders are the following:

- Traditional arrest orders; and
- Freezing injunctions.

### 24.6.1 Traditional Arrest Orders<sup>34</sup>

It has been a traditional feature of maritime law for many centuries that certain claimants have the right to apply to the court of a country in whose territorial waters a ship or other property can be found for an order to arrest that ship or other property and, if necessary, to sell it by order of the court if the claim is not paid or security is not provided. Therefore, arrests normally serve two different functions – they establish the jurisdiction of the court and provide a means of enforcing the provision of security. An arrest is defined in Article 1(2) of the International Convention for the Unification of Certain Rules Relating to the Arrest of Sea-Going Ships 1952 (The 1952 Arrest Convention) as “... *the detention of a ship by judicial process to secure a maritime claim ...*”

#### 24.6.1.1 The Types of Claim that are Subject to Arrest Orders

Arrest is not normally available for all types of claim. The laws of most countries provide that a ship or other property can be arrested only if the claim is one which falls within the *in rem* jurisdiction of the courts of that country.

A reasonably successful attempt was made to unify international rules regulating the arrest of ships in the 1952 Arrest Convention. However, that convention has not been adopted by all countries and accordingly, there are still differences between the laws of different countries in this respect and a claimant should always check with local lawyers before seeking to arrest since an unlawful arrest may result in

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<sup>34</sup> See also Chapter 19.4 (Law and Jurisdiction).

substantial damages if the trading pattern of the ship has been affected by the arrest.<sup>35</sup> However, the right to arrest is normally available in relation to the following claims which are itemised in the 1952 Arrest Convention:

- Damage caused by a ship by collision or otherwise;
- Loss of life or personal injury;
- Salvage;
- Charterparty claims;
- Cargo claims;
- General average;
- Towage;
- Pilotage;
- Provision of supplies;
- Ship building or repair;
- Crew wages;
- Ship's disbursements;
- Ship mortgages;
- Ownership disputes.

The 1952 Arrest Convention has been criticised because of the somewhat restricted types of claims which entitle a claimant to arrest. An attempt to rectify that deficiency was made by the provisions of the 1999 Arrest Convention which came into force in September 2011. Under the 1999 Arrest Convention, ships may also be arrested for the following additional claims:

- Damage or threat of damage to the environment;
- Wreck removal;
- Port, canal and pilotage dues;
- Unpaid insurance premiums;
- Unpaid commissions, brokerages and agency fees;
- Disputes arising from contracts for sale of the ship.

The 1952 Arrest Convention also suffers from an important deficiency, namely that the claimant is allowed merely one opportunity to arrest. Consequently, if the arrest does not result in the production of sufficient security, the claimant cannot re-arrest that ship or arrest any other sistership to 'top-up' the security. However, the 1999 Arrest Convention allows ships to be re-arrested or sisterships to be arrested in the event that the security that was originally given to release the ship proves to be inadequate and there is sufficient equity in the ship or sisterships that is subsequently arrested to satisfy the increased security demand. For example, if a ship worth USD 5 million is initially arrested for a claim valued at USD 3 million, that ship or any other sistership may be re-arrested to obtain top-up security of a further

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<sup>35</sup> See section Chapter 24.6.1.2 below.

USD 2 million if the claim subsequently proves to be for USD 5 million rather than USD 3 million, provided that the ship which is subsequently arrested has a value of at least USD 2 million.

However, the 1999 Arrest Convention has only been adopted by a few countries to date and therefore, currently, has limited applicability.<sup>36</sup> Furthermore, there is some doubt as to whether it will ever be widely adopted.

In common law jurisdictions a claimant has the right to arrest a ship for claims relating to supplies only if it can be proved that the supplies were ordered for the account of the shipowner. If the supplies were ordered for the account of the charterers, then even though they were delivered to the ship, the claimant has no right to arrest the ship in relation to those supplies. Therefore, bunker suppliers would not normally have the right to arrest the ship for the value of bunkers delivered to the ship but ordered by time charterers for their own account if the charterers failed to pay for those bunkers. However, similar rules do not apply in all countries, and in some countries a party which provides supplies or bunkers 'on the credit of the vessel' is entitled to arrest the ship even though the bunkers were in fact ordered by the charterers for their own account.<sup>37</sup> Finally, although bunker suppliers may have the right to attach the bunkers rather than the ship, such claims are often fraught with difficulty.<sup>38</sup>

#### 24.6.1.2 Formalities

Because arrest can cause serious disruption to normal trading patterns the laws of most countries require a claimant to produce evidence supported by a sworn affidavit outlining the basis of the claim and the grounds for arrest. It is not normally necessary for the claimant to bring evidence sufficient to satisfy the court that the claim must inevitably succeed since not all the relevant evidence may be available at that time. However, the court will normally wish to be satisfied that the claimant has a firm basis for the claim. The test of sufficiency differs from country to country but normally courts will require the evidence to be the equivalent of the test that is required by the courts of common law countries, i.e. the claimant must prove that he has 'a good arguable case'.

In some countries the court will, as a condition of granting the right to arrest, impose a condition that the arrestor should put up counter security which can be enforced if it is subsequently proved that the arrest was unlawful. Claimants should always

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<sup>36</sup> A list of signatories to this and other international conventions can be accessed via the IMO website at: <http://www.imo.org/About/Conventions/StatusOfConventions/Pages/Default.aspx>.

<sup>37</sup> For more detailed commentary see Chapter 2.6 (Bunker Claims).

<sup>38</sup> See Chapter 2.6.2 (Bunker Claims).

check to see whether there is likely to be such a requirement in the country where the arrest is contemplated and the circumstances in which the owners of the arrested property can call upon this security. In common law countries an arrest is not considered unlawful if the court is satisfied that the claimant had 'a good arguable case' at the time of the arrest application even if subsequent events show that the claim must fail. However, other courts take the view that it is 'all or nothing' in the sense that if the claim fails, the arrest is deemed to be unlawful.

A ship or other property is normally arrested when a copy of the court order is served on the ship or other property. Thereafter, the ship or other arrested property must comply with the directions of the court which are normally conveyed by a court official such as the Admiralty Marshall or by a naval officer. Such officials have the authority to move the ship or property or to take any other action that they deem necessary to protect either the property itself or the rights of any other third parties that may be affected by the arrest. For example, the official might require the ship to be towed to another location to facilitate access to and from a particular berth. The arresting party is normally required to pay the cost of such action albeit that he is normally entitled to be reimbursed either by the owners of the arrested property or, failing that, out of the proceeds of sale of the property in due course. However, if an attempt is made by the owners of the ship or other property to remove the ship or other property from the territorial waters of that country without the consent of the court official, the attempt may be restrained by force since breach of the court order amounts to a contempt of court.

#### **24.6.1.3 Release of the Ship from Arrest**

Since the ship represents a security fund for a claim, the ship may be released if the claim plus interest and costs is paid or security is provided in a form and quantity that is considered satisfactory by the court.<sup>39</sup> Security is normally provided for the whole of the claim plus interest and costs. However, security may be provided for a lower limitation fund if the court is satisfied that the defendant is entitled to limit his liability. In this respect, there is an important difference between an arrest that is made in a country that applies the 1957 Limitation Convention and one which applies the 1976 Limitation Convention or the 1996 Protocol thereto (hereafter referred to jointly as the 1976 Limitation Convention).

Under the 1957 Limitation Convention the onus is on the party who seeks to limit to prove that he is entitled to do so, whilst under the 1976 Limitation Convention, it is presumed that the defendant has the right to limit and the onus is on the party contesting the right to limit to prove that the defendant is not entitled to do so. Consequently, if the ship is arrested in a 1957 Limitation Convention country,

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<sup>39</sup> See Chapter 24.7 below.

the court may not allow the ship to be released against provision of the relevant limitation fund unless and until the defendant proves to the satisfaction of the court that the defendant has produced sufficient evidence to prove his right to limit. However, if the ship is arrested in a 1976 Limitation Convention country, the court is likely to release the ship once a limitation fund has been established unless the party contesting the right to limit can produce convincing evidence that he is not entitled to do so. Since the right to limit is lost under the 1976 Limitation Convention only if the defendant is guilty of wilful intent or recklessness with knowledge that the loss or damage is likely to happen, it has been recognised that the right to release the ship on the establishment of a limitation fund under the 1976 Limitation Convention is almost automatic.

A defendant that establishes a limitation fund under the 1976 Limitation Convention also obtains a further benefit in that Article 13.2 of the convention states that any other ships or other property that may be owned by the defendant are protected against further arrest or attachment in any other country that has adopted the 1976 Limitation Convention.

#### **24.6.1.4 Sale of the Property**

If the owners of the arrested ship or other property do not offer security for the claim, the claimants may apply to the court for the sale of that ship or other property by the court. The purpose of the sale is to produce sufficient funds to satisfy the claim and any balance is thereafter released by the court to the owners of the arrested property. However, it should be appreciated that:

- Other claimants may also arrest the ship or claim against the proceeds of sale; and that
- The first arrestor does not automatically get priority over any subsequent arrestors; and that
- The proceeds of a forced sale through the courts are unlikely to be as high as the proceeds of a private sale.

Consequently, the sale may not produce sufficient proceeds to satisfy all the claims and the claims of other parties may have priority over the claimant's claim. The laws of most countries will normally establish the priority ranking of each claim according to the category of the particular claims. The priority ranking may differ from country to country but expenses incurred by the court officials will almost inevitably rank first, followed by claims for crew wages. Thereafter, claims will normally (but not always) rank as follows:

- Maritime liens;
- Claims which create a charge on the ship, e.g. a mortgage;
- Claims which have been enforced on the ship by action *in rem*.

### 24.6.2 Freezing Injunctions<sup>40</sup>

The Freezing Injunction (also known as the Mareva Injunction) is a relatively recent development, having originally been granted by the English court in the case of *Mareva Cia Nav. v International Bulkcarriers SA* in 1975,<sup>41</sup> and is intended to provide a remedy in circumstances where the traditional arrest order is not available and can be made in respect of both maritime and non-maritime disputes. The aim of the remedy is to ensure that assets are available to satisfy an award or judgement and the laws of most countries allow their courts to make such orders or similar orders if they consider it equitable to do so. Depending on the jurisdiction in which the injunction is made, the order can be made either before or after a judgement or an award on the merits has been made.

Traditionally, freezing orders were made only in respect of assets that were within the jurisdiction of the court making the order since the court considered that it would not be able to give extra-territorial effect to an order freezing assets outside the jurisdiction. However, in recent years, courts have been ready in some instances to make 'worldwide' freezing orders but only if they are satisfied that the courts of the country where the assets are located will be prepared to enforce the freezing order.

Since a freezing order is essentially equitable in nature, courts can be expected to periodically review the propriety of the remedy. For example, Rule B of the Supplemental Rules for Federal Admiralty and Maritime Claims of the US Federal Rules of Civil Procedure allows the US court to attach property that the defendant has in the USA if the defendant itself cannot be found there. This right to attach property (generally known as the Rule B Attachment) was used extensively in recent years to attach funds which passed momentarily through the US in the form of electronic fund transfers (EFTs). However, the sheer volume of attachment applications which followed made the orderly administration of banking business very difficult and the court has subsequently held that EFTs do not constitute property for the basis of Rule B.

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<sup>40</sup> See also Chapter 23.7 (Remedies).

<sup>41</sup> [1975] 2 Lloyd's Rep. 509.

The classic Freezing Injunction is normally made on an *ex parte* basis (that is to say, without prior notice to the defendant) when a claimant is able to prove to the satisfaction of the court that:

- he has 'a good arguable case' on the merits; and that
- there are reasonable grounds for believing that the defendant has assets either within the jurisdiction or in a jurisdiction which will enforce a freezing order when made; and that
- there is a realistic risk that the defendant will move his assets out of the relevant jurisdiction before any award or judgement can be enforced.

Therefore, the subject matter of the injunction is normally an asset other than real estate since the latter cannot be moved out of the jurisdiction. In the majority of cases the Freezing Injunction obliges the defendant and his agents to disclose the assets that are held in the relevant jurisdiction and to refrain from transferring those assets including bank deposits out of the jurisdiction. Any breach of the order amounts to contempt of court and can incur substantial penalties. However, Freezing Injunctions will normally be made subject to various ancillary orders designed to protect the interests of third parties. Therefore, the defendant will normally be entitled to pay out of the frozen funds sufficient monies to pay his legal fees and usual business and trading costs and expenses.

It must be emphasised that the Freezing Injunction does not give the claimant any particular proprietary interest or priority in the funds that have been attached. Therefore, the funds may have to be shared in due course with other claimants according to the customary priority rankings that apply in that country.

Finally, if it transpires that the injunction was wrongfully obtained, the applicant may be held liable to indemnify the defendant for any loss or damage that he has suffered as a result of the granting of the injunction and the court granting the injunction may require the claimant to put up counter-security sufficient to meet the defendant's losses should the claim not succeed in due course and any costs incurred by third parties such as banks in complying with the injunction. Therefore, an applicant must ensure that full and frank disclosure of all material facts and information is made to the court before the injunction is granted.

## 24.7 The Provision of Security

In the majority of cases the arrest or attachment of property or the threat of such arrest or attachment will persuade the defendant to offer security for the claim. Security can be provided in many different ways but is normally provided as a:

- P&I Club letter of undertaking; or
- Bank guarantee; or
- Bail bond; or
- Cash deposit.

In some cases, the liability of the property owner may be covered by P&I or similar insurance, whereas, in other cases, the property owner may either have no insurance cover, or may not have insurance cover for the claim itself but only for the costs of defending the claim (e.g. the claims which qualify for Defence cover).<sup>42</sup> This distinction is often material when considering the provision of security since, subject to the issues discussed below, the P&I insurer may be prepared and able to provide security on behalf of the assured in the case of an insured claim, whereas that facility is not normally available in the case of other claims. Consequently, if the claim is not covered by insurance, the property owner will normally be obliged to make his own arrangements to provide security.

### 24.7.1 P&I Insured Claims

In the majority of cases that involve insured claims, security is provided in the form of a P&I club letter of undertaking which is normally provided without charge and is given directly to a claimant rather than to a court, although it can sometimes be given directly to a court. Most claimants and courts around the world recognise and accept the sufficiency of this form of security when issued by an International Group P&I club. The main reason for this is the financial strength of the clubs, particularly in the case of large claims, since these clubs can rely on the protection of the pooling mechanism and collective market reinsurance. This security has also been recognised by a multitude of flag states which have for many years accepted the 'blue cards' that are issued by these clubs as certificates of financial responsibility under the compulsory insurance provisions of the CLC Convention,<sup>43</sup> and in more recent years, under similar provisions in the Bunker Convention.<sup>44</sup> Therefore, in the majority of cases, arrests and attachments are released in exchange for P&I club letters of undertaking if such security is offered in acceptable terms and for a sufficient amount.

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<sup>42</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV and Rule 65 (Defence Cover)).

<sup>43</sup> See Chapter 12.4.1.1.5 (Pollution Claims).

<sup>44</sup> See Chapter 12.4.1.1.2 (Pollution Claims).



The P&I clubs that are members of the International Group provide indemnity insurance to their members in accordance with the 'pay to be paid' principle.<sup>45</sup> Consequently, apart from certain important exceptions,<sup>46</sup> such P&I clubs are not legally obliged to provide security to a third party claimant.<sup>47</sup> However, such P&I clubs recognise the importance to their members of the ability to trade their ship without undue risk of arrest. Therefore, such P&I clubs will often agree to provide security to a claimant on a discretionary basis as a service to their member. However, such security will normally be provided only in respect of claims that are insured by the club. Furthermore, such P&I clubs will usually agree to provide security only in respect of claims that have already arisen, and in circumstances where the arrest or attachment of the member's ship or other property has either already occurred or is imminent. Finally, such P&I clubs may in some circumstances require the member to provide counter-security as a condition of providing security to a claimant on their behalf since the clubs will, by doing so, incur direct liability to the third party claimant.

If a P&I club agrees to provide security, it will, in most circumstances, offer its own letter of undertaking. There is no standard form of P&I club letter of undertaking since the form of security that is required will differ from case to case. However, before providing the security, the club will normally discuss with the member the terms on which it is prepared to offer the security. Should the local law or custom require security to be provided in some other form, a P&I club will normally strive to meet such a request, provided that the claim or matter for which security is requested falls within the P&I cover as of right. One form of security which is sometime requested is a bank guarantee. P&I clubs have established facilities in most countries for providing security in this form, although – in contrast to club LOUs, which can be provided very quickly – bank guarantees take longer, often several days, to provide and involve a cost to the club (for the service provided by the banks in question). Another, somewhat similar, form of security is a surety bond. This too can take time to put up and will involve a cost to the club. A cash deposit would be considered only in the most exceptional circumstances and, for the reasons discussed in Chapter 24.7.3 below, P&I clubs will normally agree to provide security in the form of a cash deposit only as a last resort.

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45 For more detailed commentary see Chapter 26.3.1.5 (The Structure of Marine Insurance).

46 For further commentary on the obligation of P&I clubs to provide compulsory insurance and to submit to direct actions from third party claimants see Chapter 12.4.1.1.1.5 (oil pollution from laden tankers), Chapter 12.4.1.1.2 (pollution from bunker spillages), Chapter 12.4.1.2 (pollution from hazardous and noxious substances) and Chapter 12.4.1.3.3 (pollution under the US OPA 90) and Chapters 11.3.2.4, 11.3.3.1 and 11.3.3.2 (legal liability to passengers).

47 See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 88 (Payments and undertakings to third parties)).

All these forms of security will be given only on terms which explicitly state that any payment that is made thereunder will be made only by agreement between the parties, or by the final unappealable judgment of the relevant court, or by a final unappealable arbitration award.

In cases where the claim or matter falls, or appears to fall, outside the P&I cover, clubs may exercise their discretion to assist the member by offering security. If this is done, the club will wish to ensure that it is adequately counter-secured by the member before agreeing to do so. What is considered to be 'adequate counter-security' is likely to vary, depending largely on the amount involved and the financial standing of the member.

#### **24.7.2 Claims Insured by Other Insurers**

In some instances, the particular event may give rise to claims which are either not insured by the P&I club or only partly insured by the club. For example, if a shipowner insures 3/4ths of his collision liability with hull and machinery insurers and 1/4ths with a P&I club, liability for the claims that may be made as a result of the collision will be shared between hull and machinery and P&I insurers. These situations can cause complications if a claimant threatens to arrest the ship, particularly since hull and machinery insurers cannot provide security for their proportion of the liability with the same facility as a P&I club. In such circumstances, the P&I club may be prepared to provide security for the full 100 per cent of liability if the club and the hull and machinery insurers have agreed in advance the terms on which security is to be provided to the claimant and the terms upon which the insurers will indemnify each other for doing so.

### 24.7.3 Uninsured Claims

If the claim is not covered by insurance, or if the local law or local custom requires security to be provided in the form of cash deposits, bail bonds or bank guarantees, the owner of the property that has been arrested or attached may have no alternative but to provide security in this form. The classic form of bail bond differs from a bank guarantee or a traditional form of P&I club letter of undertaking in that the bail bond is a form of security that is given to a court and is therefore, within the direct control of the court, whereas a bank guarantee or P&I club letter of undertaking is normally a purely personal form of security that is given directly to the claimant.

The party that is required to provide security in the form of a bank guarantee or bail bond should appreciate that the provision of such security will normally incur a financial charge. A bank or bail bond company will charge a commission for the provision of the security and will normally require some form of counter-security which may restrict the ability of the owner of the property that has been arrested or attached to have free use of its other assets. A cash deposit is even less attractive to a party that provides security in this form since it will usually attract less interest than other forms of deposits that may be commercially available and runs the risk of being irrecoverable even if the claim fails.

### 24.8 Claims Management and Insurance

The giving or obtaining of security can often have a fundamental impact on the merits of a claim or a defence to a claim. Therefore, parties should consider these issues at an early stage of any dispute and advice should be taken from knowledgeable lawyers in the relevant countries so that a considered assessment can be made and an agreed strategy can be reached as quickly as possible.

Contractual and non-contractual claims may involve both property insurers such as hull and machinery underwriters, cargo insurers, war risk insurers etc., and liability insurers such as P&I clubs, charterers' liability insurers etc. All such insurers will expect the assured to act prudently and take the appropriate steps to both minimise the insurers' liability and to preserve the insurers' rights in subrogation against third parties.<sup>48</sup> Therefore, the assured must also consult the relevant insurer as soon as possible since a failure to do so may prejudice his rights under the relevant insurance policy.<sup>49</sup>

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<sup>48</sup> For further commentary see Chapter 25.5 (The Fundamental Principles of Marine Insurance).

<sup>49</sup> See for example, the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV (Defence Cover) and to Rule 82 (Obligations with respect to claims)).

### 24.9 Case Study

A ship is time chartered by her owners A to B for a period of 12 months and B then sub-time charters the vessel to C for a shorter period but otherwise on back to back terms. Both charters include the following lien clause:-

*"That the Owners shall have a lien upon all cargoes, and all sub-freights for any amounts due under this Charter ..."*

A week later C sub-voyage charters the ship to D for the carriage of 5,000 metric tons of grain from Lake Charles, Louisiana, to Tema, Ghana. The head charter between A and B is due to end on completion of this voyage, after which A plans to sell the vessel.

The voyage charter provides that 90 per cent of freight is payable within three days of the issue of the bills of lading and that the balance is to be paid on delivery of the cargo. It also provides that:

*"Owners shall have a lien on all cargo for freight, deadfreight, demurrage and damages for detention."*

The vessel loads at Lake Charles and proceeds on her voyage. However, in the course of departing, she collides with the vessel SITTING DUCK which was anchored in the roads and caused damage to it in the order of USD 100,000.

In the meantime, A's agents have released bills of lading signed by the Master to D, who is named as shipper in the bills of lading. A printed clause on the reverse side of the bill of lading provides that:

*"all terms and conditions, liberties and exceptions of the charterparty dated overleaf are herewith incorporated."*

The relevant section on the face of the bill of lading confirms that freight is payable in accordance with the terms of the voyage charter between C and D.

One week after leaving Lake Charles B fails to pay a further hire instalment that is then due to A since B is in financial difficulties, and all subsequent demands from A for payment of the hire meet with no response.

A wishes to consider which, if any, remedies are available to it in relation to:

- a The claim for hire; and
- b The collision with the SITTING DUCK.

a The claim for hire

1 Can A refuse to complete the voyage?

Unless A terminates the charter it remains obliged to comply with B's employment orders. A will probably have the right under the head time charter to withdraw the vessel from B's service for non-payment of hire but this is unlikely to be commercially attractive for A if the time charter is due to end on completion of the current voyage. Furthermore, the bills of lading have been signed for and on behalf of the master, and therefore, even if it receives no hire from B, A is obliged as carrier under the bills to carry the cargo to destination for the benefit of the shippers and receivers and will incur liability to them under the quite separate bill of lading contract if it fails to do so. Therefore, there would seem to be little point in withdrawing the ship

2 Can A exercise a lien on the cargo at destination for the hire that is outstanding from B?

It is true that the lien clause in the head time charter gives A *"a lien upon all cargoes ... for any amounts due under this Charter ..."* However, the cargo receivers are not parties to that charter and there is no provision in the bill of lading (i.e. in the contract between them and A as carrier) which gives A the right to lien the cargo for hire. Therefore, the time charter lien clause on cargo is unlikely to provide A with a satisfactory remedy for unpaid hire.

3 Can A exercise a lien on the hire that is payable by C to B?

The lien clause in the head time charter with B also gives A *"a lien upon all sub-freights ... for any amounts due under this Charter ..."* However, A cannot exercise a lien over the hire that is payable by C to B under the sub-time charter since the clause gives a lien on *sub-freight* not sub-hire.

**4** Can A exercise a lien on the sub freight that is payable by D to C?

Since the lien clause in the head time charter with B gives A “a lien upon all sub-freights,” A has the right in principle to exercise a lien on the sub-freight that is payable by D to C. Provided that such notice is given before the freight is paid to C, the notice is effective under the common law and D is at risk if it ignores the notice since it will still remain liable to pay the freight to A. However, the problem that A has in this case is that 90 per cent of the freight has been paid before the giving of the notice which means that the lien is effective only in respect of the balance of 10 per cent that is payable on delivery of the cargo at the port of destination. Indeed, A may also face difficulty in securing payment of that proportion if D refuses to comply with the notice. In such circumstances, A may have the practical difficulty of enforcing the payment since the local courts in the country where D carries on business may not fully understand the common law concept and may refuse to enforce payment to A.

**b** The collision with the SITTING DUCK

A believes that the SITTING DUCK will inevitably bring a claim in due course and, since the SITTING DUCK was at anchor at the time of the collision, it is likely that A will be held to be solely to blame. Therefore, could this upset their plans to sell the vessel?

The seller of a vessel is usually required to give an undertaking at the time of the sale that the vessel is free of liens and encumbrances. The owners of SITTING DUCK are very likely to have a maritime lien over A's vessel, entitling them to enforce their claim against that vessel even when she has changed ownership as a result of the sale. Therefore, A will need to settle the claim before the sale if they wish to ensure that the incident does not disrupt their sale arrangements.<sup>50</sup>

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<sup>50</sup> For more detailed commentary see Chapter 1.1 (Building and Sale and Purchase Claims).

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Principles and Structure of Marine Insurance

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## Chapter 25

# The Fundamental Principles of Marine Insurance<sup>1</sup>

### 25.1 Introduction

It is not feasible to examine the minutiae of marine insurance law and policy in this brief overview.<sup>2</sup> However, there are a number of fundamental marine insurance principles that must be considered at all times as they apply to all aspects of cover in all countries.

Whilst the wording of national laws or insurance terms may differ to some extent the fundamental characteristics of marine insurance are as described in the following provisions of the English Marine Insurance Act 1906 (MIA).

Section 1 of the Act defines marine insurance as follows:

*“A contract of marine insurance is a contract whereby the insurer undertakes to indemnify the assured, in manner and to the extent thereby agreed, against marine losses, that is to say, the losses incident to a marine adventure.”*

Section 3 of the Act states that there is a *“marine adventure”* where:

*“any ship, goods or other moveables are exposed to maritime perils”.*

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<sup>1</sup> Further commentary can be found in Chapters 1-8 of the *Gard Handbook on P&I Insurance*, 5th edition.

<sup>2</sup> For more detailed commentary see *Arnould's Law of Marine Insurance and General Average* by Gilman Merkin, Blanchard, Cooke, Hopkins and Templeman, 18th edition, 2013, Sweet & Maxwell, *O'May on Marine Insurance* by Hill, 1993, Sweet & Maxwell, *MacGillivray on Insurance Law* by Birds, Lynch and Milnes, 12th edition, 2012, Sweet & Maxwell and *Marine Cargo Insurance* by Dunt, 2009, Informa.

Finally, Section 4 of the Act defines the phrase “*maritime perils*” as follows:

“ ‘*Maritime perils*’ means the perils consequent on, or incidental to the navigation of the sea, that is to say, perils of the seas, fire, war perils, pirates, rovers, thieves, captures, seizures, restraints and detainments of princes and people, jettisons, barratry and any other perils, either of the like kind of which may be designated by the policy.”

Such principles apply whether the policy protects against Hull & Machinery (H&M), P&I, Loss of Hire (LOH) or the other standard types of marine insurance.<sup>3</sup> However, different types of insurance policies will often provide cover in the event of additional perils provided that such perils have a maritime context.<sup>4</sup>

## **25.2 Disclosure and the Doctrine of Utmost Good Faith<sup>5</sup>**

Both parties to a marine insurance contract (i.e. the insured and the insurer) must observe the utmost good faith (*uberrimae fidei*) when negotiating the contract of insurance. This is a fundamental principle of the law of all countries and is enshrined in Section 17 of the English MIA which provides that:

“A contract of marine insurance is a contract based upon the utmost good faith, and, if the utmost good faith be not observed by either party, the contract may be avoided by the other party.”

The rationale that underpins the principle was explained as long ago as 1766 by Lord Mansfield in the English case of *Carter v Boehm*:

“... good faith forbids either party, by concealing what he privately knows, to draw the other into a bargain from his ignorance of that fact, and from his believing to the contrary.”

However, the duty to make full and frank disclosure is usually more relevant in the context of the information that should be disclosed by the assured to the insurer. The insurer must be able, when a contract is being negotiated, to rely on information provided by the assured since he cannot himself check and assess all the material facts that may be involved in the proposed risk. Furthermore, there may be facts that are known only to the party requesting cover. Accordingly, such a party is under a legal duty to disclose and represent all facts that are material to

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3 For more detailed commentary see Chapter 26 (The Structure of Marine Insurance).

4 See, for example, Chapters 5 (Claims for loss of, or damage to, ship) and 26 (The Structure of Marine Insurance).

5 For further commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 6 (The Member’s duty of disclosure)).

the proposed risk, i.e. every fact that would influence the judgment of the insurer in estimating the risk, or in assessing the premium, or the terms and conditions on which cover should be offered. The duty encompasses not only those factors that relate to physical hazards but also the personal standing of the assured (including details of dishonesty, breaches of regulations, prior claims history etc.). However, the party requesting cover need not disclose circumstances that diminish the risk, or factors that are known, or ought to be known, by the insurer in any event.

The duty of disclosure also encompasses all circumstances that are known to any officer or employee in the assured's organisation or to independent contractors, such as managers, to whom the assured has delegated important functions relating to the management and operation of the matter to be insured even if these circumstances are not known to the assured personally. It is also important to understand in this context that the broker who places the insurance on behalf of the assured is deemed to be the assured's representative and, therefore, any failure on the part of the broker to disclose material facts of which the broker was aware will be treated as a failure to disclose on the part of the assured even if the assured was not personally aware of those facts. Therefore, all those that act for, or represent, the party requesting cover have a duty to disclose all material facts and to ensure that what they tell the insurer during the pre-contract negotiation is true and correct.

If there is a failure to make a full and frank disclosure the insurer will normally have the option to avoid the contract of insurance and return the premium to the assured. However, if it is found that the assured has been acting fraudulently when doing so, the insurer is not normally obliged to return the premium.

In some cases, the particular insurance terms may also oblige the assured to notify the insurer of any material alteration in the nature or the extent of the risk which occurs after the policy has incepted but during the currency of the policy. The policy may also specify whether the insurer is entitled to terminate the policy in such circumstances. However, much depends on the terms of the particular policy.<sup>6</sup>

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<sup>6</sup> For more detailed commentary on this issue in the context of P&I insurance see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 7 (Alteration of risk)).

### 25.3 Warranties<sup>7</sup>

A warranty is a promise by the assured that some particular action will or will not be taken, or that some condition will be fulfilled. Similarly, the assured may warrant something if he affirms or denies some specific state of facts. Such a warranty may be express or implied and must be strictly complied with. Under the law of the United Kingdom and some other similar jurisdictions the warranty must be strictly complied with irrespective of whether it is material to the risk and, if it is not complied with, the insurer is discharged from all contractual obligations from the date of the breach.<sup>8</sup> For example, if the assured promises not to operate a vessel in ice-infested waters, or not to carry inflammable or explosive cargoes, or not to operate in areas that are subject to armed conflict or similar disturbances, he will be in breach of warranty once he breaks his promise.

Traditionally, a voyage policy has been considered to be subject to an implied warranty that the vessel shall be seaworthy at the commencement of the voyage for the purposes of the particular adventure.<sup>9</sup> However, this warranty has become of limited practical value in the case of cargo insurance since most policies contain a 'held covered' provision such as is found in Clause 5 of the Institute Cargo Clauses (ICC) A, B and C which provides that the cargo insurer waives any breach of the implied warranty unless the assured is "*privity to such unseaworthiness or unfitness at the time the subject-matter insured is loaded therein.*" Since the assured in the case of a cargo policy is likely to be the goods' owner rather than the shipowner, it is unlikely in most cases that the assured will be found to be privity to the unseaworthiness of the ship.

The position is somewhat similar in the case of a time policy. Whilst there is no such implied warranty in the case of a time policy, if the assured sends to sea a ship that he knows, or ought to know, to be unseaworthy, the insurer is not liable for any losses that can be attributed to the unseaworthy condition.<sup>10</sup> A ship is considered unseaworthy when she is not reasonably fit in all respects to encounter the ordinary perils of the seas for the venture insured.<sup>11</sup> Therefore, since shipowners are obliged to maintain a continuous programme of due diligence and to keep documentary

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7 It is important to remember that a warranty is construed differently in the context of contracts for the carriage of goods. In the context of a contract of insurance, a warranty is a term of the highest importance whereas in the context of a contract for the carriage of goods, a warranty is a term of lesser importance and is distinguishable from a term which is considered to be a condition (a term of great importance) and an intermediate term (a term which may be of the highest importance depending on the gravity of the breach and its consequences). See Chapter 23.4.2 (Remedies).

8 See Section 33 of the MIA.

9 See Section 39 (1) of the MIA.

10 See Section 39 (5) of the MIA.

11 For more detailed commentary see Chapter 4.4.1 (Charterparty Claims).

records in that regard,<sup>12</sup> insurers can be expected to require disclosure of such records if there is reasonable suspicion that an incident has been caused by the unseaworthy condition of the ship.

#### 25.4 Insurable Interest

One of the fundamental principles of marine insurance is that the assured must have an insurable interest in the subject matter of the insurance. The assured has such an interest if he has an equitable relationship to the marine venture or to any insurable property at risk in such a venture, so that the assured may either benefit by the safety or due arrival of such property, or may be prejudiced by its loss, damage or detention, or may incur liability arising from such occurrences.<sup>13</sup> The most obvious example of an insurable interest is the ownership of a vessel or cargo. However, a mortgagee of a ship also has an insurable interest in the ship since, pending repayment of the loan by the mortgagor, the ship is a source of security for the mortgagee who will, therefore, benefit by its continued well-being and will be prejudiced if it is lost or damaged. By way of contrast, a shipowner who claimed under a marine Loss of Hire insurance which provided cover in the event of *“the vessel being deprived of her earning capacity as a consequence of damage sustained”* was held to have no insurable interest in relation to loss of earnings incurred during the period that the vessel was obliged to undergo repairs following damage caused by an insured peril since it had been planned to drydock the vessel in any event as part of the shipowners’ periodic dry-docking schedule.<sup>14</sup>

If the ship or cargo is owned by a corporation, the owner of the property is the corporation rather than the shareholders and therefore, it is the corporation (rather than the shareholders) that has the insurable interest in the property. This is so even if a shareholder owns all of the shares in the owning company since a corporation is a legal entity that is separate from the shareholders.

Unlike other branches of insurance, a party who requests insurance cover need not have an insurable interest at the time that the insurance is effected, but must have such an interest by the time that the loss occurs. Therefore, a prospective buyer of a ship or cargo can conclude a contract of insurance and can recover under it if the relevant loss or damage occurs after the buyer has assumed ownership in due course. Finally, a marine cargo insurance policy is capable of being assigned, thereby enabling a CIF seller of goods to take out insurance which will protect

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<sup>12</sup> For more detailed commentary see Chapters 3.5.1.2 and 3.5.4 (Cargo Claims).

<sup>13</sup> See Section 5 of the MIA.

<sup>14</sup> See *The Capricorn*, [1995] 1 Lloyd’s Rep. 622.

the seller before, and the buyer after, transfer of the risk pursuant to the contract of sale.<sup>15</sup> However, insurers on other forms of marine insurance policies normally reserve the right to refuse to consent to an assignment.

### **25.5 The Measure of Indemnity<sup>16</sup>**

The insured is entitled to be indemnified only to the extent of the pecuniary loss that he has suffered as a result of an insured peril. However, it is a peculiarity of marine insurance that the assured and the insurer are entitled to agree the extent of the indemnity at the time of concluding the contract of insurance, i.e. to agree a valued policy. If the extent of the indemnity has been agreed in this manner, the indemnity is, in the absence of fraud, conclusive and binding between the parties although it may be less, or even more, than the actual pecuniary loss. In contrast, an unvalued policy has no specified value stated in the policy and the payment, if a loss occurs, will be the actual value, calculated under general insurance principles as set out in the relevant legislation. Most H&M, Total Loss Insurance, LOH and many cargo marine policies are valued policies.<sup>17</sup>

### **25.6 Subrogation**

Subrogation is the right that the insurer has to 'step into the shoes of the insured' when a loss has been paid and to take over all rights that the assured may have to claim against a third party that has caused the loss or damage.<sup>18</sup> For example, if a H&M insurer has settled a claim that has been brought by an assured shipowner for damage to the ship's hull as a result of a collision, the insurer is entitled to take over the right of the shipowner to bring a claim against the other colliding vessel to recover that proportion of the damage that can be attributed to the other ship's negligence.<sup>19</sup>

If it is necessary to pursue legal proceedings against such a third party the insurer is entitled, depending on the law of the country where the claim is being pursued, to either pursue legal proceedings himself in his own name<sup>20</sup> or in the name of the assured, or to call on the assured to pursue such proceedings on the insurer's behalf.

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15 For more detailed commentary see Chapter 4.1 (Charterparty Claims).

16 For more detailed commentary see Chapter 5 (Claims for loss of, or damage to, ship) and Chapter 26 (The Structure of Marine Insurance).

17 For further commentary see Chapters 26.3.1 and 26.3.3 (The Structure of Marine Insurance).

18 See Section 79 of the MIA.

19 For more detailed commentary see Chapter 6.8 (Collision Claims).

20 The insurer is normally obliged to pursue the claim in the jurisdiction where the assured would have been obliged to do so had the claim been brought by the assured. However, in the case of the *Front Comor*, the insurers brought the claim in a different jurisdiction leading to substantial, costly and complex multi-national litigation. See Chapter 19.12 (Law and Jurisdiction)

However, subrogation is a right and not an obligation. Therefore, there may be occasions when it is not in the interests of the insurer to do so, e.g. when the claim may attract substantial counter-claims.

### 25.7 Abandonment

The doctrine of subrogation is closely related to the doctrine of abandonment. Abandonment is a legal mechanism which enables the assured (usually on payment of a total loss or constructive total loss)<sup>21</sup> to give notice to the insurer that the insured property (or what remains of it) has been abandoned by the assured. If there is a justifiable abandonment, the insurer is entitled (but not obliged) not only to take over any rights that the assured may have to claim against a third party, but also to take over all proprietary rights and interests that the assured has in the abandoned property. However, insurers normally reject notices of abandonment in order to avoid any further liabilities that may still relate to the property, e.g. liabilities for wreck removal,<sup>22</sup> oil pollution clean-up,<sup>23</sup> disposal of damaged cargo etc.

### 25.8 Sue and Labour

The assured is obliged under marine insurance policies to 'sue and labour' (i.e. to use all reasonable efforts) to avert or minimise a loss that may be caused by an insured peril and which would give rise to a claim under the policy.<sup>24</sup> However, the assured is entitled to recover 'any expenses properly incurred' in so doing from the insurers. The insurers are obliged to pay such expenses even if they are also obliged to pay the total sum insured under the policy since the sue and labour obligation is a supplementary and separate obligation.

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21 For more detailed commentary see Chapter 26.2.1.1 (The Structure of Marine Insurance).

22 For more detailed commentary see Chapter 16 (Wreck Removal Claims).

23 For more detailed commentary see Chapter 12 (Pollution Claims).

24 See Section 78 (4) of the MIA and Section 4-7 of the Nordic Marine Insurance Plan (NMIP). See also the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 46 (Measures to avert or minimise loss)).





## Chapter 26

# The Structure of Marine Insurance

### 26.1 The International Nature of Marine Insurance

The scope of cover that is provided by many forms of insurance is restricted to a distinct and limited territorial area. However, ships cross all oceans and call at ports around the world and therefore, marine insurance needs to be truly global in scope to reflect the international nature of the maritime industry. Shipowners and insurers are also exposed to a wide variety of losses and liabilities that arise as a result of many different kinds of incidents in many different jurisdictions and which are, consequently, subject to many different rules of law. Therefore, the cover that they require, and which has developed over many centuries, must be sufficiently broad in scope to encompass this broad spectrum of risk.<sup>1</sup>

### 26.2 The Scope of Marine Risk

Normally, the owners, operators and charterers of ships and cargo interests will require insurance protection against the following:

- Loss of, or damage to, their own property;
- Loss of income;
- Liabilities to third parties (such as the owners of other ships or other property, or to cargo interests, or damage to the environment);
- Legal and other costs.

However, the mere fact that the assured has suffered loss, damage, liability or expenditure does not mean that the assured is inevitably entitled to recover under the relevant policy. Insurance policies provide protection only if the relevant loss etc., has been caused by an insured peril, i.e. a peril that the insurer has agreed will form the basis of compensation. In general, such a peril must, insofar as the assured

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<sup>1</sup> For commentary on the historical development of the marine insurance market see Chapter 1 of the *Gard Handbook on P&I Insurance*, 5th edition.

is concerned, be a fortuity or accident. Therefore, insurers do not provide cover for inevitable losses such as those that may be caused by inherent vice or ordinary wear and tear, or losses caused by the wilful misconduct of the assured.

However, even if the loss has resulted from a fortuity, it may be the result of many different types of events. For example, such losses etc., can arise as a result of a maritime peril<sup>2</sup> such as bad weather, collisions, groundings, fire, loss of or damage to cargo etc., or as a result of war risks including civil war, revolution and terrorism, or as a result of political risks such as governmental expropriation or other commercial risks such as frustration or repudiation of contracts, business interruption, inability to repatriate funds etc. Therefore, those that are engaged in maritime activity will normally require different types of insurance cover since the risks that arise as a result of these differing events differ in nature and require different risk evaluation. However, the issue can become complicated since certain risks are not necessarily covered by the same category of insurance and this can, therefore, affect the scope of cover that is available under such policies. For example, although 'piracy' is defined as a maritime peril for the purposes of the English Marine Insurance Act 1906 (MIA) and standard P&I insurance, the current market practice is for this risk to be excluded from standard H&M insurances and for it to be covered by war risks insurers. Therefore, it is important to check the specific risks that are covered under each form of insurance.

### **26.3 The Main Categories of Marine Insurance**

It is not possible to comment in detail in this publication on all the various forms of insurance that may affect those that are engaged in maritime activities. Therefore, the following commentary will concentrate only on those insurances that are most likely to be relevant in relation to the losses, liabilities and expenditures that have been itemised above. The terms 'marine insurance' and 'war insurance' will be used in the general sense described above but bearing in mind that the terms may cover the same or different risks in different policies.

Although there may be many subsidiary stakeholders that will normally have an interest in a maritime adventure (e.g. banks, ship managers, crewing agents etc.), the following commentary concentrates on the interests of the three major stakeholders, namely the owner of the ship, the charterer of the ship and the owner of the cargo.

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<sup>2</sup> Section 4 of the MIA defines 'maritime perils' as "... the perils consequent on, or incidental to the navigation of the sea, that is to say, perils of the seas, fire, war perils, pirates, rovers, thieves, captures, seizures, restraints and detentions of princes and people, jettisons, barratry and any other perils, either of the like kind of which may be designated by the policy."

### 26.3.1 Insurance for the Shipowner

A shipowner will normally require insurance cover for the loss of, or for damage to his own property, for loss of income and for his potential liabilities to other parties. Traditionally, a shipowner could choose whether or not to insure against these risks, and to choose the type and scope of insurance cover that he thought appropriate. However, the development of compulsory insurance requirements<sup>3</sup> allied to the rising cost of claims and higher asset values now means that a shipowner will find it almost impossible to operate the ship if he does not have adequate insurance cover. Therefore, no shipowner can afford to ignore the importance of ensuring that he is insured to the full extent that may be necessary.

#### 26.3.1.1 Hull and Machinery Insurance (H&M)

Hull and machinery insurance is insurance that a shipowner requires in order to protect his economic interest in 'the ship' which term includes:

- the ship's hull and its machinery;
- equipment and spare parts that are carried on board;<sup>4</sup>
- bunkers and lubricating oil that are carried on board.

These items are normally insured under the ship's H&M insurance if they are owned by the shipowner. However, containers are normally covered under separate container insurance even if they are owned by the shipowner.

Depending on the precise terms of the particular policy, H&M insurance may cover:

- physical damage to, or the loss of, the ship;<sup>5</sup>
- the shipowner's proportion of general average,<sup>6</sup> salvage<sup>7</sup> and sue and labour expenses;<sup>8</sup> and
- liability to third parties caused by collision with another ship<sup>9</sup> or by contact with other property.<sup>10</sup>

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3 For more detailed commentary see Chapters 11.3.2.4, 3.3.1, 11.3.3.2, and 11.5 (People Claims), Chapters 12.4.1.1.1.5, 12.4.1.1.2, 12.4.1.2, 12.4.1.3.3 and 12.7 (Pollution Claims) and Chapter 16.2.4.5 (Wreck Removal Claims).

4 However, not objects that are merely carried on board for a temporary period and are intended for consumption, e.g. paint supplies.

5 For more detailed commentary see Chapter 5 (Claims for the loss of, or damage to, the ship).

6 For more detailed commentary see Chapter 10.7 (General Average Claims).

7 For more detailed commentary see Chapter 14.5 (Salvage Claims).

8 For more detailed commentary see Chapter 25.7 (The Fundamental Principles of Marine Insurance).

9 For more detailed commentary see Chapter 6.8 (Collision Claims).

10 More detailed commentary see Chapter 9.3 (Fixed and Floating Objects (FFO) Claims).

#### **26.3.1.1.1 Hull and Machinery Insurance Providers**

H&M insurance is available from numerous insurance providers in all parts of the world, but the main hubs are in London (Lloyds), the Nordic countries and China. This form of insurance is provided both by commercial insurers that are owned by third parties and by mutual hull clubs that are owned and controlled by the shipowners/assureds themselves. However, the terms and conditions of cover, and the various levels of deductibles, that are provided by the Nordic Marine Insurance Plan (NMIP), the English ITC Hulls clauses, the German ADS/DTV clauses, and by the American, Japanese or French terms differ. Consequently, the scope of the H&M cover that is available is not standardised.<sup>11</sup>

However, the insurance is not normally placed with one insurer but with several insurers who each accept a proportion of the risk for each ship, and a policy for a fleet may be spread over different markets. Therefore, H&M insurance is usually placed by one or more brokers on behalf of the assured and sometimes in different markets. In many instances, one insurer may act as lead underwriter (or rating leader as he is sometimes called) and will have the authority to bind the following insurers in matters such as premium assessment, rating of additional vessels etc. Such a lead underwriter may also act as the claims leader who is authorised by the following insurers to handle claims and carry out claims adjustments on behalf of all insurers. Should the lead underwriter also happen to be the P&I insurer of the ship, experience has shown that this can facilitate the effective and efficient co-ordination and handling of claims for the mutual benefit of the assured and all other insurers and stakeholders.

#### **26.3.1.2 Separate Insurances against Total Loss (Total Loss Insurance)**

If a ship is totally lost the sum that is recoverable under the H&M policy may not be sufficient to provide the assured with a complete indemnity since the market value of the ship may be more than its insured value, particularly when the market price of ships is increasing. Furthermore, if the ship is a total loss, the shipowner will normally lose income from the time that the ship has been lost until it has been replaced by another ship. Consequently, shipowners will normally also wish to purchase Hull Interest and Freight Interest insurances (known as 'Disbursements' or Increased Value (IV) insurances) which provide additional cover in the event that the insured ship has become an actual or constructive total loss.

Hull Interest insurance is designed to cover the difference between the actual market value of the ship and its insured value under the H&M insurance, and any collision liabilities that exceed the sum that is insured under the H&M insurance. Freight Interest insurance is designed to cover the loss of income that the shipowner may

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<sup>11</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 36 (Collision with Ships) and Rule 37 (Damage to Fixed or Floating Objects)).

suffer when a ship has become a total loss and is, therefore, different from the cover that is provided by LOH insurance, which provides cover for the loss of income that is the result of physical damage that does not amount to a total loss (See Chapter 26.3.3 below).

Normally, the amount of Hull Interest and Freight Interest insurance is capped at a maximum of 25 per cent of the insurable value under the H&M policy, but this may vary depending on the underlying H&M conditions.

#### **26.3.1.2.1 Total Loss Insurance Providers**

Most H&M insurance providers also write Hull Interest and Freight Interest insurances but their ability to accept such risks for individual ships or fleets may be restricted by their capacity and attitude to cumulative risks.

#### **26.3.1.3 Loss of Hire Insurance (LOH)**

Traditionally, insurance policies have excluded cover for delay even if the delay has been caused by an insured peril. For example, Section 55 (2) (b) of the English Marine Insurance Act 1906 provides that:

*“Unless the policy otherwise provides, the insurer on ship or goods is not liable for any loss proximately caused by delay, although the delay be caused by a peril insured against.”*

Therefore, H&M policies do not normally provide cover for loss of time. However, there is no doubt that ‘time is money,’ and a shipowner will normally wish to be covered against such risk under Loss of Hire (LOH) Insurance. However, this type of insurance does not provide cover in all circumstances; it is normally designed to dovetail with other insurances and to provide cover in similar circumstances. Therefore, LOH insurance is normally designed to indemnify a shipowner against any loss of income that may arise as a result of an event that has caused physical damage to the ship which would be recoverable under H&M insurance irrespective of the level of the deductible. However, the terms of LOH policies can differ. Therefore, some LOH insurances may also offer cover in specified circumstances even when there is no physical damage to the ship, (e.g. when the ship is stranded, or has been hijacked by pirates).<sup>12</sup>

The amount of compensation that is payable under LOH insurances is normally based on the time that the assured has been deprived of income and on the amount of income that has been lost per day. In many cases, the amount of compensation will be agreed and based on a fixed daily amount that corresponds to the daily

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<sup>12</sup> This may also be covered by Strikes insurance – see Chapter 26.3.1.4 below.

hire that is payable under the ship's current charterparty. That daily sum is then multiplied by the number of whole and/or part days on which the ship is not able to trade, subject to a deduction of a pre-defined number of days (usually 14 days). Furthermore, the policy will normally specify that cover is restricted to a maximum number of days per incident, and to an aggregate number of days for the whole period of insurance regardless of the number of individual LOH incidents. Therefore, the LOH insurance policy may state, for example, that the insurance shall be subject to the term '14/90/90' which means that there is to be 14 days deductible, 90 days maximum recovery per incident and 90 days maximum recovery in the aggregate for the period of insurance. However, the LOH policy may also include an automatic reinstatement clause which has the effect of reinstating the full sum insured after a casualty, against payment of additional premium.

#### **26.3.1.3.1 LOH Insurance Providers**

Fewer insurers provide LOH insurance than H&M insurance although the LOH insurers of a vessel will sometimes also write a share of the H&M risk for the same vessel. Furthermore, the average proportion of the risk that is accepted by individual LOH insurers is usually higher than that which is accepted by H&M insurers and some providers may offer insurance on a 100 per cent basis. Collectively, the Scandinavian providers have a high share of the market whereas there are fewer providers in the United Kingdom or in Continental Europe.

#### **26.3.1.4 Strikes Insurance**

Strikes insurance provides cover for the daily costs of vessels delayed by *force majeure* situations on board or ashore that are outside the control of a shipowner or charterer. Therefore, strikes insurance is similar to some extent to the cover that is provided by LOH insurance but it is wider in scope and is intended to cover some of the gaps in LOH cover. For example, strikes insurance provides cover for periods of delay that fall within the excess period of LOH insurance and also for time lost in connection with incidents that do not give rise to a claim under H&M insurance. The following are typical examples of circumstances in which cover is available:

- Strikes, boycotts, actions by environmental objectors, industrial disputes;
- Collision, grounding, stranding, striking FFO's;
- Indirect effects of certain weather conditions;
- Fire, explosion, mechanical breakdown on land;
- Port closures, obstructions, or high levels of water;
- Illness, death or injury on board the vessel or caused by the vessel;
- Stowaways, saving life at sea, rescuing of refugees;
- Desertion of the crew;
- Presence of drugs onboard (actual or alleged);
- Pollution caused by the entered vessel (actual or alleged);
- Quarantine.

#### 26.3.1.4.1 Strike Insurance Providers

The major provider of Strikes Insurance is the Strike Club that provides cover on a mutual basis for some risks and on a fixed premium basis for extended cover.<sup>13</sup>

#### 26.3.1.5 Protection and Indemnity Insurance (P&I)<sup>14</sup>

P&I insurance has developed over the centuries in response to the increasing need that shipowners have had to obtain insurance cover for liabilities to third parties and for expenses that are not insured under standard H&M and other marine policies. Therefore, modern P&I insurers provide cover for a wide range of legal liability that the assured may have to third parties, and for expenditure arising as a result of:

- Loss of or damage to cargo;<sup>15</sup>
- Pollution from the ship, or its cargo;<sup>16</sup>
- Loss of life and injury to crew members, or passengers;<sup>17</sup>
- Removal of wreck;<sup>18</sup>
- Damage to fixed or floating objects;<sup>19</sup>
- Collisions with other ships.<sup>20</sup>

Most P&I insurers are P&I clubs that provide cover on a mutual basis. This means that each member of the club agrees to share the risks that affect the other members of the club and agrees to contribute the funds that are required to meet the claims that may be made against any member of the club during the policy year. Consequently, cover is made available only for those risks that are regularly and commonly encountered by the majority of the membership since these are the risks that each member has agreed to share. Therefore, cover is not normally available for unusual or excessively onerous liabilities. For example, if a member incurs a liability that arises solely as a result of contractual terms that are not commonly and regularly used by the majority of the membership, such risks would normally be excluded from cover unless they have first been approved by the club.<sup>21</sup> Similarly, members are expected and required to make full use of whatever rights they may have to exclude or limit their liability in order to protect the common funds of the club and

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13 Further details of the cover that is available can be accessed at:  
<http://www.thestrikeclub.com/HTML/default.htm>.

14 For more detailed commentary see the *Gard Guidance to the Statutes and Rules and P&I Club Law and Practice* by Stephen Hazlewood and David Semark, Informa, 4th edition, 2010.

15 For more detailed commentary see Chapter 3.7 (Cargo Claims).

16 For more detailed commentary see Chapter 12.7.1 (Pollution Claims).

17 For more detailed commentary see Chapter 11.5 (People Claims).

18 For more detailed commentary see Chapter 16.4.1 (Wreck Removal Claims).

19 For more detailed commentary see Chapter 9.3.3 (Fixed or Floating Objects (FFO) Claims).

20 For more detailed commentary see Chapter 6.8.2 (Collision Claims).

21 For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 55 (Terms of Contract)).

its membership.<sup>22</sup> Finally, clubs will also normally exclude risks that are preventable and which can give rise to very costly claims such as the liability that shipowners may face if they have delivered cargo without surrender of the original bills of lading to the wrong party<sup>23</sup> and the liability of cruise operators for personal injury to passengers incurred whilst on shore excursions.<sup>24</sup>

On the other hand, the mutual nature of P&I insurance enables clubs to be more flexible than profit-making market insurers in the manner in which they can provide cover. One important example is the 'Omnibus Rule' which gives the club the discretion to cover risks which do not fall expressly within the stipulated cover but which, in the opinion of the club, are incidental to the operation of an insured ship and which fall broadly within the scope of club cover.<sup>25</sup>

#### **26.3.1.5.1 P&I Insurance Providers**

##### *26.3.1.5.1.1 P&I cover provided by the P&I Clubs that are members of the International Group under the Pooling Agreement*

Traditionally, P&I insurance has been provided by the shipowners themselves on a mutual non-profit making basis through the medium of P&I clubs that insure legal liabilities, losses, costs and expenses incurred by the assured (i.e. a member of the club) in direct connection with the operation of ships that are entered in the club. Although P&I clubs maintain their independence, autonomy and competitiveness, most of them have agreed to co-operate with each other as members of the International Group of P&I Clubs (IG) in order to provide their individual members with very high levels of cover and to share ('pool') liabilities, losses, costs and expenses above a certain amount, currently USD 8 million any one claim. Currently, thirteen P&I clubs are members of the IG which collectively provides liability insurance for more than 90 per cent of the world's ocean-going tonnage and more than 95 per cent of the world's ocean-going tankers. The current members of the IG are:

- The American Steamship Owners Mutual Protection and Indemnity Association Inc.;
- Assuranceforeningen Skuld;
- Gard P&I (Bermuda) Ltd;
- The Britannia Steam Ship Insurance Association Ltd.;
- The Japan Ship Owners' Mutual Protection and Indemnity Association;

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<sup>22</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 51 (General Limitation of Liability)).

<sup>23</sup> For more detailed commentary see Chapter 3.2.9.2.3 (Cargo Claims).

<sup>24</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 57 a iii (Liability occurring during through transports)).

<sup>25</sup> For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Article 9.3 (b)).



- The London Steam-Ship Owners' Mutual Insurance Association Ltd.;
- The North of England Protecting and Indemnity Association Ltd.;
- The Shipowners' Mutual Protection and Indemnity Association (Luxembourg);
- The Standard Steamship Owners' Protection and Indemnity Association (Bermuda) Ltd.;
- The Steamship Mutual Underwriting Association (Bermuda) Ltd.;
- Sveriges Ångfartygs Assurans Forening (The Swedish Club) (Sweden);
- The United Kingdom Mutual Steam Ship Assurance Association (Bermuda) Ltd.;
- The West of England Ship Owners Mutual Insurance Association (Luxembourg).

Whilst the Rules of individual P&I clubs differ to some extent, the scope of cover that is provided by each club is broadly similar and is governed by the terms of the Pooling Agreement which is a claims-sharing arrangement between the IG clubs (the Pool) whereby such clubs agree to contribute to large claims that affect one or more of the clubs in certain layers according to pre-defined criteria. The arrangement also enables the IG clubs to buy on a collective basis commercial market reinsurance protection against claims that exceed the Pool limits and, therefore, enables these clubs to offer broader cover, higher limits and stronger security than other providers. The P&I insurance that is provided collectively by the IG clubs has very high limits of cover and is considered to be an extremely reliable form of security. Consequently, the so-called 'blue cards' that are issued by the IG clubs are accepted by contracting states (i.e. states that are parties to international liability conventions such as CLC 1992, The Bunker Convention 2001 and the Athens Convention 2002) as evidence that the 'insurance or other financial security' that is required by the compulsory insurance requirements of these conventions has been met. Therefore, in reliance upon these 'blue cards', contracting states are then prepared to issue the certificates that are acknowledged to be the formal evidence of the 'insurance or other financial security' that is required.

#### 26.3.1.5.1.2 Other Forms of P&I Cover

In recent years, some P&I clubs have started to offer extended cover for certain risks that are either not covered by, or are excluded from, the P&I cover that is subject to the Pooling Agreement, as an adjunct to such cover on a fixed premium basis.<sup>26</sup> However, such extended cover does not enjoy the reinsurance protection that is afforded by the IG reinsurance contract, although it may be reinsured elsewhere. The following are examples of such extended cover:

- Liability cover for vessels or units employed to carry out drilling or production operations in connection with oil or gas exploration or production;
- Liability cover for contractual cargo liabilities in excess of applicable limitation rights;
- Liability cover for vessels involved in specialist operations such as dredging and installation activities;
- Liability cover for personnel employed by the assured not forming part of ship's regular crew.

Differing forms and levels of cover may also be provided by a number of P&I clubs that are not members of the IG. Some of these clubs (such as China P&I Club or Islamic P&I Club) focus mainly on domestic or regional markets rather than on the wider international market. P&I cover may also be available from commercial market insurers such as the British Marine, the Navigators P&I, Osprey Underwriting Agency or the RaetsMarine which are owned by private investors and which offer P&I insurance on a fixed premium basis (i.e. there is no liability for additional calls) for significantly lower limits than those which are provided by the IG clubs. Several of these providers also have a niche focus in terms of tonnage types, size and trade.

#### 26.3.1.6 Defence Insurance (FD&D)

If the assured incurs legal and other costs in connection with a claim for which cover is available under the ship's H&M, P&I or other insurances, such insurances will normally provide the assured with protection not only for the claim itself, but also for the legal and other costs that are incurred by the assured in order to defend or pursue the claim. However, a shipowner may also incur legal and other costs in connection with claims that arise out of the operation of the ship but for which insurance cover is not available. In such circumstances, shipowners can be covered for such costs (but not for the claim that is the subject matter of the litigation) under the ship's Defence cover (or Freight, Demurrage and Defence (FD&D) cover as it is sometimes called).

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<sup>26</sup> Details of the extended cover that is provided by Gard can be accessed on the Gard website at: [www.gard.no](http://www.gard.no).

Defence cover is normally available not only for the costs of claims that may be made against the assured by third parties, but also for costs incurred by the assured in pursuing claims against third parties. The majority of such claims usually arise under contracts that govern the operation of the ship such as charterparties,<sup>27</sup> bills of lading<sup>28</sup> and insurance contracts, but defence cover may also be available for claims that do not arise in connection with a contract, e.g. for the defence of allegations that may be made by port authorities that the ship is in breach of local regulations.<sup>29</sup>

#### 26.3.1.6.1 Defence Cover Providers

Defence insurance is either written by P&I clubs as a separate class of insurance or by specialised Defence clubs that are owned and controlled by shipowners. Cover is normally limited in the sense that the member is often required to retain a share of the legal costs that are at risk in the form of a deductible. Almost all Defence insurance providers also limit their overall liability for such legal costs which currently ranges between USD 5 and USD 10 million. The main difference between these two categories of providers is that the specialised Defence clubs usually operate with less capital.

The Defence cover that is provided by P&I insurers normally gives the club the authority to exercise a wide discretion whether or not to cover legal and other costs that have already been incurred, or which can be expected to be incurred; to control and direct the handling of any case; and to withdraw cover at any stage if the nature or character of the case, or the manner in which the member wishes to pursue or defend it, is considered to be contrary to the best interests of the membership as a whole.<sup>30</sup> The in-house lawyers of the P&I club assess and monitor the merits of a case very closely, and Defence cover is made available, only if the officers are of the view that a prudent uninsured would have considered it worthwhile to pursue the matter even if insurance cover had not been available for the costs of doing so. The service aspect is a very important and integral component of Defence cover and many Defence cases are handled directly by the P&I club's in-house lawyers.

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27 For more detailed commentary see Chapter 4 (Charterparty Claims).

28 For more detailed commentary see Chapter 3 (Cargo Claims).

29 For more detailed commentary see Chapter 8 (Fines and Criminal Sanctions Claims).

30 For more detailed commentary see the *Gard Guidance to the Statutes and Rules* (Guidance to Part IV (Defence Cover)).

### 26.3.1.7 War Risk Insurance<sup>31</sup>

Most of the traditional marine policies expressly exclude cover for war risks. For example, Clause 23 of the Institute Time Clauses – Hulls 1.10.83 provides that:

*“23 War Exclusion*

*In no case shall this insurance cover loss damage liability or expense caused by*

*23.1 war civil war revolution rebellion insurrection or civil strife arising therefrom, or any hostile act by or against a belligerent power.*

*23.2 capture seizure arrest restraint or detainment (barratry and piracy excepted<sup>32</sup>), and the consequences thereof or any attempt thereat.*

*23.3 derelict mines, torpedoes bombs or other derelict weapons of war.”*

Similar exclusions are normally found in LOH and P&I policies<sup>33</sup> (other than for Defence cover). Consequently, shipowners normally take out a ‘package’ of war insurances that provide cover for claims that arise under H&M, LOH, P&I and Total Loss insurance as a result of war risks.

In common with other insurances, War Risks insurance does not provide cover for everything. Therefore, certain risks are excluded, including loss or damage caused by nuclear, chemical, bio-chemical, or electromagnetic weapons and, usually, deprivation of the ship by the act of the government or authority of the country in which the ship is registered or managed. Finally, a special feature of war risks insurance is the right that the insurer has to suspend or even cancel the cover in certain critical circumstances. For example, the policy could be cancelled in the event of the outbreak of war between major global powers. War Risks insurers also have the right to give notices that affect the trading limits of the ship during the currency of the policy. Depending on the particular policy, the insurers may consider a particular area to be an excluded area or a conditional area. In an excluded area the ship will usually have no cover for war risks, whilst in a conditional area, the ship may continue to be covered but only on payment of additional premium.<sup>34</sup>

#### 26.3.1.7.1 War Risks Insurance Providers

There is relatively limited overlap between the insurance providers that operate in the traditional war risk insurance market and those that operate in the marine insurance market. The war risk insurance market is a specialised segment and those that provide such insurance are typically organisations that have specialised competence and organisations. The two main categories of insurance providers

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<sup>31</sup> For more detailed commentary see *War, Terror and Carriage by Sea* by Keith Michel, LLP, 2004.

<sup>32</sup> In practise, the risk of barratry, piracy and violent theft is also transferred to the war risk policy.

<sup>33</sup> See the *Gard Guidance to the Statutes and Rules* (Guidance to Rule 58 (War Risks)).

<sup>34</sup> The relevant war risk areas are established by the members of the Joint War Committee which is based in London.

are: (a) the war risk mutual clubs that are owned and controlled by their shipowner members such as Den Norske Krigforsikring for Skib and the Hellenic War Association, and (b) commercial war risk insurance providers that are privately owned such as those that operate in the Lloyd's and company markets in London and which represent the largest provider of war risk capacity. However, cover for P&I war risks is placed by the International Group on behalf of the member shipowners of the IG clubs on a collective basis.<sup>35</sup>

### 26.3.2 Insurance for the Charterer

A distinction needs to be drawn for insurance purposes between bareboat charterers and other charterers.<sup>36</sup> Bareboat charterers are usually co-insured together with the shipowner under the same P&I and H&M insurance whereas other charterers, including time, voyage and slot charterers, are normally insured separately under different policies. Therefore, the following commentary is restricted to the insurance of charterers other than bareboat charterers.

Charterers are often 'caught in the middle' of various possible claim scenarios:

- They may be liable to the shipowners for the loss of or damage to the ship caused for example, by loading dangerous goods,<sup>37</sup> or by sending the ship to an unsafe port,<sup>38</sup> or by providing unsuitable bunkers;<sup>39</sup>
- They may be liable to cargo owners for cargo loss or damage if they are the carriers under the relevant contract of carriage;<sup>40</sup>
- They may be liable to third parties for personal injury,<sup>41</sup> property damage or for pollution;<sup>42</sup>
- They may, as owners of bunkers or containers, be obliged to contribute to general average<sup>43</sup> or salvage.<sup>44</sup>

In all the above scenarios, a charterer may face a liability to one party, but may wish to seek an indemnity for that liability from another party. Therefore, in many instances, the insurance that a charterer requires will be similar to the P&I insurance that is required by a shipowner, and for that reason, the P&I insurance that was

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35 The cover is currently limited to USD 500 million any one event each vessel in excess of the proper value of the entered ship or any amounts recoverable under any other P&I war risks cover which the member has arranged, whichever is greater. The minimum excess is the proper value of the ship or USD 100 million, whichever is the lesser.

36 For more detailed commentary see Chapter 4.2 (Charterparty Claims).

37 For more detailed commentary see Chapter 7 (Dangerous Goods Claims).

38 For more detailed commentary see Chapter 13 (Safe Ports Claims).

39 For more detailed commentary see Chapter 2 (Bunker Claims).

40 For more detailed commentary see Chapter 3.2.4.1 (Cargo Claims).

41 For more detailed commentary see Chapter 11 (People Claims).

42 For more detailed commentary see Chapter 12 (Pollution Claims).

43 For more detailed commentary see Chapter 10 (General Average Claims).

44 For more detailed commentary see Chapter 14 (Salvage Claims).

originally available for charterers was provided predominantly by P&I clubs on a mutual basis and was modelled on the P&I insurance that was provided for shipowners. However, over time, broader and more flexible covers have emerged that are better suited to meet all the insurance needs of the charterer, including the charterer's liability for damage to the ship. These covers are usually provided on a fixed premium basis.

However, charterers may also incur loss in their capacity as property owners if bunkers that have been supplied by, and owned by, them have been lost or contaminated. Cover for such loss is available in the form of a bunkers insurance that provides cover in the event of the loss or contamination of bunkers caused by marine or war risks.

Finally, charterers may also incur loss of income or profit following physical damage to, or loss of, the chartered ship and may also wish to purchase LOH or Total Loss insurance to protect their economic interest in the ship in such circumstances.

#### **26.3.2.1 Charterers' Liability Insurance Providers**

The market for charterers' liability insurance has grown considerably over the past two to three decades, reflecting the increased liability exposure that charterers now have under international conventions and domestic laws and regulations. Several of the P&I clubs that are members of the International Group now insure a substantial number of charterers for marine liabilities including those that arise as a result of war risks. However, in most cases, this is reinsured outside the terms of the Pooling Agreement.<sup>45</sup> Finally, other specialised clubs and fixed premium providers also provide differing levels of cover.

#### **26.3.3 Insurance for the Cargo Owner<sup>46</sup>**

Traditionally, the scope of cargo insurance has been more limited than the scope of ship insurance since, in most instances, the cargo owner is interested merely in the safe and timely delivery of the cargo at the end of the carrying voyage. This means that the provision of cargo insurance is an important element of contracts for the sale of the cargo the terms of which will determine who is to provide the insurance and for whose benefit it is to be provided. For example, it is the responsibility of the buyer to obtain cargo insurance in the case of FOB sales, whilst it is the responsibility of the seller to obtain insurance for the benefit of the buyers in the case of CIF sales. It is also the responsibility of the CIF seller to provide the buyer

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<sup>45</sup> For example, Gard currently offer a Comprehensive Charterers' Liability Cover which expressly includes liability for damage to the ship and which is subject to a limit per incident or occurrence. Full details of this cover can be accessed on the Gard website: [www.gard.no](http://www.gard.no) and follow the links to Covering Risks and Comp Charterers' liability.

<sup>46</sup> For more detailed commentary see *International Cargo Insurance* by John Dunt, Informa, 2012.

with documentary evidence that he has provided such insurance, and therefore, payment of the CIF price of the goods is made against documents including the insurance certificate. Consequently, if the agreed certificate is not provided, or not provided in the correct form, the seller may not be able to secure payment from his buyer.<sup>47</sup>

### 26.3.3.1 Protection against Damage to, or Loss of, Cargo

The most common forms of cargo insurance are based on standard conditions such as the Institute Cargo Clauses (ICC) A, B and C.<sup>48</sup> The level of cover that is available differs depending on the particular version of the ICC clauses that is chosen. The A clauses provide cover for all risks, the B clauses for only specifically nominated risks whilst the C clauses provide cover only for catastrophic risks.

Furthermore, it should be appreciated that 'all risks' cover is not the same as 'all losses' cover. Cover is available only for loss or damage that has been caused by a fortuity or accident and, therefore, loss or damage that is inevitable, or arises as a result of inherent vice or the natural behaviour of the subject-matter is excluded. However, provided that the loss or damage has been caused by a peril that is covered by the particular version of the ICC clauses that is being used in any particular case, the cargo interests are normally insured against the following:

- a Loss of or damage to cargo;
- b Salvage charges;<sup>49</sup>
- c General average charges;<sup>50</sup>
- d Forwarding charges;
- e Charges incurred in averting or minimising loss (sue and labour expenses);<sup>51</sup>
- f Charges incurred in preserving the subrogated rights of the insurer.

Other standard clauses provide more or less the same scope of cover as that which is provided by the ICC clauses with some variations.

War and strikes risks are excluded from the cover that is provided by the ICC clauses. However, it is possible for additional clauses such as Institute War Clauses (Cargo) and Institute Strikes Clause (Cargo), to be added to the policy to provide cover for loss, damage or expense caused by such risks.

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47 For more detailed commentary see Chapters 4.1 (Charterparty Claims) and 3.2.2 (Cargo Claims).

48 However, because some cargoes are vulnerable to risks which do not affect cargo in general, specific cargo insurance clauses are available for the carriage of such specific cargoes. For example, there are specific clauses available to insure the carriage of frozen foods, bulk oil, coal etc. Many of these clauses have been developed in collaboration with a specific body such as the Federation of Oils, Seeds and Fats Associations (FOSFA).

49 See footnote 44.

50 See footnote 43.

51 See footnote 8.

Most modern cargo policies provide expressly that the cover is not prejudiced by any deviation of the carrying vessel or by the unseaworthiness of the carrying vessel unless the assured cargo owner is privy to such unseaworthiness at the time that the cargo is loaded.

#### **26.3.3.2 Protection against Loss or Damage Caused by Delay**

Cover is not available for loss or damage resulting from delay except in limited circumstances. Therefore, if the delivery of a cargo is delayed by a marine peril and, consequently, the value of the cargo is materially diminished as a result of missing an important market, no cover is available under the ordinary form of cargo policy. Similarly, if a cargo of rice is damaged by sea water, cover is normally available under the cargo policy, but if the cargo deteriorates further as a result of delay in removing or segregating the cargo, cover is not available for any additional losses that are thereby incurred. However, special insurances that provide cover for losses caused by delay are available on the market.

#### **26.3.3.3 Protection against Liability to Third Parties**

Cargo owners may incur liabilities to third parties and may, therefore, require insurance cover for such liability. Therefore, the ICC clauses indemnify the assured cargo owners against their liability to contribute in general average or salvage. However, liability may also arise in other circumstances. For example, if a ship is damaged as a result of the carriage of dangerous cargo,<sup>52</sup> the cargo owner may become liable for very substantial sums both for loss of or damage to the ship and for personal injury and may require liability cover in such circumstances. Such liability is not covered under the ICC clauses but there is currently a growing market for the provision of liability insurance for cargo owners and traders.

#### **26.3.3.4 Subrogation<sup>53</sup>**

In the event that a cargo is lost or damaged in transit the cargo owner is likely to claim under his cargo insurance rather than pursuing a claim against the carrier since the former is usually a quicker and better route to recovery. When the cargo insurer indemnifies the cargo owner for his loss the insurer becomes subrogated to (i.e. 'steps into the shoes of') the cargo owner and assumes whichever rights the cargo owner would have had to bring claims against third parties, e.g. the contractual carrier. Therefore, in the majority of cases, it is cargo insurers (or special recovery agents or lawyers on their behalf) who bring cargo claims against carriers.

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<sup>52</sup> See footnote 37.

<sup>53</sup> For more detailed commentary see Chapter 25.5 (The Fundamental Principles of Marine Insurance).



### 26.3.3.5 Cargo Insurance Providers

Unlike some other forms of marine insurance, cargo insurance is provided by an evenly spread worldwide cross-section of insurers. However, in some cases, this is the result of local regulations which require importers or exporters to insure with local insurers and, in a number of such cases, the risk may be reinsured with companies in one of the recognised insurance hubs around the world. In any event, notwithstanding the insurer, the scope of cover is predominantly similar reflecting the need for cargo insurance to comply with the accepted international norms for different types of cargo sale.

## 26.4 Ship Builders' Risks<sup>54</sup>

The prospective owners of a new ship are normally obliged to make various payments to the builder by installments at various stages of the ship's construction and to provide the builder with various items of equipment for installation on the ship.<sup>55</sup> Therefore, if the ship is damaged during the construction, the prospective owners run the risk that the builder may not be able to complete the construction.

Builders will normally be contractually bound under the terms of the shipbuilding contract to take out insurance cover on terms such as the Institute Clauses for Builders' Risks 1/6/88 which insures the structure that is being built:

*"against all risks of loss of or damage ... caused and discovered during the period of this insurance including the cost of repairing replacing or renewing any defective part condemned solely in consequence of the discovery therein during the period of this insurance of a latent defect."*

Such insurance is normally taken out by the builder but it is good policy for the prospective shipowner to require the builder to include the prospective owner as a co-insured, and to apply any amounts that may be recoverable under the insurance to the cost of repair and the replacement of the buyer's equipment.

The launching of newly built ships is also sometimes delayed by incidents that occur during the course of construction at the shipbuilders' yard. This can cause considerable financial loss to the shipowner if he is contractually obliged to deliver the ship for service under a charterparty or contract of carriage by a certain date. Some insurers provide cover in such circumstances on terms that are similar to those that are provided by Loss of Hire insurers.<sup>56</sup>

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<sup>54</sup> For more detailed commentary see *The law of Shipbuilding Contracts* by Simon Curtis, Informa, 4th edition, 2012.

<sup>55</sup> For more detailed commentary see Chapter 1 (Building and Sale and Purchase Claims).

<sup>56</sup> See Chapter 26.3.1.3 above.

### 26.4.1 Shipbuilders' Risks Insurance Providers

Shipbuilders risk insurance is provided in most cases by insurers that operate in the marine markets in Norway, London, Europe and Singapore and companies that write H&M insurance will often provide cover for builders' risks as part of their overall profile. However, local insurers that are based in the shipbuilding countries also play an active role particularly when there is a regulatory requirement that local companies must be used. However, in many such cases, the risk is often reinsured with companies that operate in one of the established marine insurance centres mentioned above.

In most cases, the insurance is based on the Institute Clauses for Builders Risks 1/6/88 (ICBR) but may also be arranged on the basis of other clauses such as the Nordic Marine Insurance Plan (NMIP) or the American Institute Builder's Risk Clauses (8 February 1979). However, the standard policies do not provide cover in all circumstances and care should be taken to ensure that the cover that is actually placed is wide enough to protect against the risks that are likely to be encountered during the building. For example, whilst the standard ICBR clauses exclude "*loss damage liability or expense caused by earthquake or volcanic eruption*"<sup>57</sup> (and similar exclusions including earthquakes and tsunamis are included in the standard Japanese terms), insurers will often agree to delete or amend such exclusions.

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<sup>57</sup> Clause 6.

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## Claims Management

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## Chapter 27

# Claims Management

### 27.1 Introduction

It cannot be said that every small claim is straightforward or that every large claim is complex, but it can be said with considerable certainty that most large claims are complex. This is especially true of 'casualties' that involve a sinking, a collision, a grounding, or a serious problem such as a fire which affects the vessel, the cargo and possibly the crew. Most casualties are likely to involve some or all of the following factors:

- an immediate concern for People, the Environment and Property (PEP);
- several different areas of potential liability with commercial, financial and other consequences;
- several, competing legal systems and jurisdictions;
- several different insurance covers;
- the involvement of local and national authorities;
- the involvement of the media and the general public.

The most complex cases involve all of these factors, and consequently, virtually all shipowners plan and prepare for such an event, but relatively few shipowners actually experience one. Although many casualties have similarities, no two casualties are the same and regardless of their size, those unfortunate shipowners who have to deal with such a casualty are likely to have limited previous experience to guide them. It might be said that dealing with such an incident is like putting together the pieces of a jigsaw puzzle – but without the benefit of the final picture and, sometimes, seeing the pieces changing shape and size as the drama unfolds. One important source of support and assistance for shipowners in such cases is their insurers, especially their P&I club. In normal circumstances, P&I cover will be available for most and possibly all of the liabilities which a shipowner is likely to face. Clubs have extensive experience in working with shipowners to respond to such cases, whenever and wherever they may happen and it is very much in the mutual interest of these parties to work together closely.

This chapter contains a fictional example of a major casualty. It suggests how such an incident might develop and discusses some of the many complex questions which shipowners are likely to face. It comments on the parties to whom shipowners can look for advice and support, and on how shipowners might plan for, and respond to, some of the problems that they are likely to face. It also offers suggestions about the slightly longer-term, tactical and strategic thinking that may be necessary for the resolution of the claims and disputes that are likely to arise. However, it does not – and cannot – provide complete answers to all issues since each case is different, and numerous events can alter needs and priorities overnight. No two shipowners will respond to a particular scenario in exactly the same way and each case must be dealt with strictly on its own merits.

Nevertheless, good planning and preparation is essential for an effective response to a casualty. Planning ranges from the purely practical, (such as ensuring that there are enough telephone lines in the crisis room to ensure effective communication), to the more strategic, (such as the appointment of appropriate staff members to the crisis or emergency response team). Preparation also means ensuring that the crisis team not only has the appropriate knowledge, but also the ability and experience to translate that theory into practise. Training is important, because it develops the necessary knowledge and understanding and, consequently, the confidence of team members. However, it is important to appreciate that no emergency response plan should be too rigid. Structure is important, but so is the ability to be flexible, because no plan will – or can – cover every possible eventuality. Clearly, not every real-life, maritime casualty will occur when everyone is in the office at 10.00 on a Monday morning. It is far more likely that such a casualty will occur outside office hours. In many cases, shipowners have had to deal with a casualty on a public holiday, or when key members of staff are away from the office, or even in the middle of an emergency drill; hence the need to be prepared at all times.

One immediate challenge that faces a shipowner is how to balance and deal with the numerous competing issues and parties who are, will, or may become involved. To whom – and to what – does a shipowner give priority, and when does he do so? What form of external advice and assistance can a shipowner expect, and what should he ask for? Who does he need to notify about the casualty? What steps should be taken to try to deal with the problem and in what order? These are merely some of the relevant issues.

## 27.2 Stage 1 of the Casualty

The first few hours of a fictional example of a serious casualty are outlined below.

*“The vessel is a bulk carrier of some 17,500 gt, built in 2001. She is on a voyage from the Far East to South-East Africa with a full cargo (around 33,250 mt) of fertiliser.*

*She is owned by a one-ship company, but there are 10 other vessels of similar size, age and value in the same management which are all separately owned by one-ship companies and which are all registered in the same country. The vessel is on time charter to a large trading house and the crew consists of officers from Eastern Europe and Filipino ratings. The vessel carries 310 m/t of IFO and 80 m/t of MDO as bunkers. The IFO is located in several tanks, one of which is a double-bottom tank beneath no. 3 hold.*

*The vessel's voyage is uneventful until, late one evening, she makes contact at full speed (14.5 knots) with a reef just off a tropical island that is well-known as a popular holiday destination. The weather at the time is rough (winds of Force 8, with a heavy swell and poor visibility). Initial reports from the vessel indicate that, in trying to avoid the reef, she has grounded on rocks nearby, that she is aground up to the aft part of no. 2 hold, and is taking in water in the forepeak tank and holds 1 and 2. The after part of the vessel is floating freely and the vessel is working heavily on the rocks.*

*Attempts by the master to contact the shipowners are unsuccessful. It is very early in the morning in the city where the shipowners carry on business and all their senior executives are flying back from the capital city after meeting senior figures in the government and are therefore, out of mobile telephone contact. The shipowners only hear about the incident from the chief officer some six hours after the grounding. He reports that the master was thrown down a flight of stairs and hit his head when the vessel grounded, and that one crewman, an AB, suffered a serious leg injury (a possible broken leg) as a result of the grounding.”*

### 27.2.1 Immediate Issues

The person in the shipowners' office who receives this report has some important and immediate decisions to make. The most important immediate decision relates to internal notification, and almost all shipowners will have their own emergency response plans that have been prepared for just such an eventuality. These plans will normally list those people within the company, often called the emergency response team (ERT), who should be notified. This team will usually include people with whatever legal, technical, operational, commercial, and often, media-related, backgrounds that may be available.

If the emergency response plan has been properly established it should be possible to assemble the ERT with the minimum of delay in order to formulate and implement the shipowners' response to the incident. Experience suggests there are two main areas on which the ERT should focus at this stage: firstly, the assessment of those facts and issues that require urgent action; and secondly, the need to notify and (in most cases) request help and advice from external parties.

All serious casualties involve a complex amalgam of legal, technical and commercial issues. One of the greatest challenges which shipowners and their insurers face is how best to take all such advice into account in their overall strategic decision-making. This requires an understanding of how each individual piece of advice affects the various other issues that may be relevant, some of which may appear at the time to be unrelated, and the manner in which one particular course of action is likely to have an impact on future events. There is a great deal of information that needs to be obtained, shared, considered and disseminated to those who need it, and an urgent need for co-ordinated management, decision-making and action. All of this needs to be done whilst, at the same time, monitoring actions that have already been taken, and evaluating those that, consequently, will need to be taken in future. In a nutshell, there is a need for 'kaleidoscopic eyesight' that must focus simultaneously on shorter and longer term issues.

Let us consider, by way of example, one issue that is likely to arise in our fictional case. Given the seriousness of the incident, the shipowners may decide to send a senior executive to the scene. Such a step is often taken because it demonstrates how seriously shipowners regard the situation, and because it evidences their wish to take part in face to face discussions with the decision-makers at the scene of the incident. Such motives are laudable, but it is important to consider the background, experience and skills of the person that is to be sent, and to establish and agree his/her role beforehand. Furthermore, it is important to assess the situation in its overall context. Will he/she be the best person to assist in relation to technical issues that affect the vessel, a role for which a senior superintendent might be more appropriate? Will he/she be required to take part in discussions with the local/national authorities, a role for which a more 'corporate' individual might be appropriate? Will this person be able to adequately represent the shipowners in media interviews and briefings? Indeed, will it actually be helpful to send anyone to the scene or could it merely expose that person to pressure and threats from local individuals, organisations, politicians or authorities, any or all of whom may be extremely upset at what they consider to be the irreparable damage that has been caused to their environment and jobs? Is there a risk that the person may be



detained and become a 'hostage' to be released only if and when certain demands have been satisfied? Shipowners may have already identified the relevant person in their emergency response plan, but before taking a decision, it is important to consider whether the circumstances of the incident require the plan to be reconsidered and, perhaps, changed.

In most cases, details of the casualty will initially be given exclusively to the shipowners by those on board. However, within twelve hours and possibly sooner, news of the incident is likely to be more widely available, and the location and seriousness of the casualty will probably influence how widely such news is broadcast and the prominence that will be given to it. Numerous other parties will then try to establish the facts and assess the implications of such facts. Therefore, it is essential that shipowners, together with their insurers, should use the 'head start' that they may have before the news becomes publicly available in a productive manner in order to convene the ERT and to assess the implications of the incident. The acronym 'PEP' (People, Environment and Property) can often serve as a helpful guide to the issues to which priority should be given. However, this may not always be the case, and the particular facts will dictate which issues should, or should not, be addressed immediately.

#### **27.2.1.1 People<sup>1</sup>**

Two injuries have been reported. The leg injury to the AB seems serious but the degree of seriousness that should be attributed to the injury to the master is unknown. However, the injury to the AB will require medical assistance and probably a medical evacuation in any event. Such an evacuation will almost certainly need the assistance of the local authorities who will, therefore, need to be informed about the incident.

The injury to the master may also require medical evacuation but, if this were to occur, this would mean that the vessel would be without the services of her master for an indeterminate period of time. Therefore, the important decision of whether or not to evacuate the master may have to be taken with incomplete information.

#### **27.2.1.2 Environment<sup>2</sup>**

The vessel has run aground on a reef and it is likely that the reef has suffered damage as a result of the grounding. Furthermore, even if the vessel can be, and is, refloated, further damage may be caused to the reef. If the reef is a coral reef, this could give rise to a substantial claim, especially if the reef is important for the

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<sup>1</sup> For comment on personal injury issues see Chapter 11 (People Claims).

<sup>2</sup> For comment on pollution issues see Chapter 12 (Pollution Claims).

holiday/leisure activities which provide the island with significant income. Whilst an early assessment of the physical damage caused by the grounding would be helpful, this will probably have to be postponed until the vessel has been refloated. Although it appears that the vessel is hard aground there are no reports that the bunker tanks have yet been damaged. However, the weather is bad and the vessel is at risk of suffering further structural damage if she continues to 'work' on the rocks. Therefore, the potential for damage to, and leakage from, one or more bunkers tanks is clear.

### **27.2.1.3 Property<sup>3</sup>**

The vessel has suffered serious damage and whilst it appears that the cargo is presently undamaged, the precise picture is unclear and may be changing rapidly. Therefore, the crew would normally be expected to do what they can to conduct damage assessment tests by visually checking holds and sounding tanks for leakages.

It seems extremely unlikely that the vessel can refloat herself and therefore, salvage assistance is likely to be urgently required. Some shipowners may feel competent to engage salvage assistance themselves but in most cases, this would be done in liaison with (and, in many cases, by) the vessel's Hull and Machinery (H&M) insurers.

## **27.2.2 External Advisers**

The shipowners will also need to involve numerous external parties in order to provide the necessary support and advice and, most importantly, to ensure that the shipowner acts in accordance with the requirements of his insurance cover, particularly his P&I and H&M insurance. Shipowners and their insurers will also wish to involve other external service providers such as lawyers, technical experts, salvors, and possibly, media advisers. Each service provider will need to receive full information and full and regular updates from the shipowners, and will need to be kept fully and regularly briefed about the work that is being done by the other service providers in order to ensure that they can carry out their own investigation in the most constructive manner. Therefore, the early establishment of a team of external advisers is essential.

### **27.2.2.1 Lawyers**

Instructing the appropriate lawyers is important for a number of reasons. Many owners and insurers have a list of their preferred firms, but it is important to choose a firm and a person, or group of persons, within a firm, with the necessary competence and experience. Shipowners should also be aware that the information

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<sup>3</sup> For comment on salvage issues see Chapter 14 (Salvage Claims) and for comment on hull and P&I claims see Chapter 26 (The Structure of Marine Insurance).

gathered by lawyers, and the advice that they give, is frequently the subject of legal privilege, i.e. it cannot be disclosed to other parties.<sup>4</sup> It is likely that lawyers will need to be appointed in at least two different jurisdictions – the jurisdiction where the incident has occurred and the jurisdiction(s) provided for in the contract(s) of carriage, charterparty and/or crew contracts.<sup>5</sup>

Lawyers are often instructed not merely to give legal advice, but also to assist in ascertaining the facts of the incident by taking statements from the relevant crew members and collecting evidence from the vessel. The appointed lawyers should be familiar with the numerous electronic data recording devices with which ships are equipped and may need to act swiftly with experts and/or device manufacturers in order to save data before it is lost. The timely collection of such evidence will help shipowners and their insurers in the handling of claims which are likely to be made against the shipowners, and to make an early assessment of their potential liability for such claims. Furthermore, important issues such as the possible application of limitation of liability principles, and the applicable and/or favourable law and jurisdiction(s) will also need to be considered.

#### 27.2.2.2 Salvors<sup>6</sup>

Securing salvage assistance is likely to be a priority given the difficult situation in which the vessel finds herself. It is customary for shipowners to liaise with their H&M insurers in order to identify those salvors who are willing and able to assist. This is usually done either by direct contact with the salvors, or through one of the well-known salvage brokers that will act as a link between the shipowners/insurers and the salvors. Whichever method is adopted, it is likely that the shipowners and their insurers should have sufficient information available to them within a short space of time to enable them to identify the firm of salvors with whom they will enter into a contract, and the likely terms of the salvage contract.<sup>7</sup> Speed is important since the authorities will be eager to see an immediate response to the casualty. Indeed, most coastal states have laws regulating the speed of response times. If the authorities are not satisfied with both the speed and the extent of the shipowners' response, they may take matters into their own hands and require the shipowners to pay the cost thereafter.<sup>8</sup> This is unsatisfactory, because it can often mean that the shipowners have little or no control over the decisions that are being made, but are, nevertheless, expected to pay all bills as and when they are subsequently presented.

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4 For more detailed commentary see Chapter 3.5.4 (Cargo Claims).

5 For more detailed commentary on jurisdiction issues see Chapter 19 (Law and Jurisdiction).

6 See Chapter 14 (Salvage Claims).

7 The most common and well-known form of salvage contract is the Lloyds Standard Form of Salvage Agreement, usually referred to as LOF, but other options, such as a fixed price agreement, or a daily rate agreement, are sometimes considered. For more details of the LOF contract see Chapter 14.1 (Salvage Claims).

8 See Chapter 26.2.3 below.

Once the salvage contract has been agreed, the shipowners and their insurers may wish to appoint their own salvage consultant. If the salvage agreement incorporates the SCOPIC Clause,<sup>9</sup> the shipowners and their P&I club will almost certainly appoint a Special Casualty Representative (SCR) in accordance with Clause 12 of the SCOPIC provisions and Clause 13 gives the H&M insurers a similar right to appoint a Special Hull Representative to “*observe and report on the salvage operation ...*” However, even if the SCOPIC Clause is not incorporated into the salvage agreement, shipowners and their insurers (both P&I and H&M) are nevertheless, likely to appoint a salvage expert to provide them with technical advice and comment on the salvors’ plans and work.

### 27.2.2.3 Environmental Experts

It may also be prudent for the shipowners and their P&I club to appoint, or at least consider appointing, experts who can assist in the event that the ship’s bunkers cause pollution and there is consequent damage to the (coral) reefs and a need to consider various clean-up methods. Experience suggests that salvage operations often take longer than expected to mobilise, sometimes because of bad weather, and sometimes because of other unexpected delays, such as customs or immigration problems in the country in question. Consequently, pollution can occur in the meantime. Indeed, even if the salvage operation were to be successful, it is possible that there may still be damage to the reef. Therefore, it might well be sensible, even at this early stage, to instruct an organisation such as the International Tanker Owners’ Pollution Federation (ITOPF)<sup>10</sup> if only to identify the oil spill response equipment and resources that may be available in case oil does start to spill from the vessel.

### 27.2.2.4 Media Consultants

A casualty such as this is likely to generate considerable media attention, especially in the country where the incident has occurred. Media attention may also be generated in the shipowners’ flag state or in the country where the shipowners’ carry on business or, even more generally, in industry circles. Indeed, should the vessel break up and thereby cause environmental damage, this may generate even more widespread media interest. Modern communication systems mean that news of such an incident is then likely to be made public within a few hours of the occurrence with photographs and film being posted on the internet for all to see. Past experience

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9 The Special Compensation P&I Club (SCOPIC) Clause sets out *inter alia* the basis on which the special compensation for environmental salvage that is payable under Article 14 of the International Convention on Salvage 1989 is to be assessed. For more details see Chapter 14.3 (Salvage Claims).

10 The International Tanker Owners Pollution Federation Limited (ITOPF) acts as an independent technical adviser for non-tanker owners as well as tanker owners and attend many spills of bunker fuel from non-tank vessels worldwide.

makes it clear that the adoption of a 'no comment' policy is unlikely to be an effective strategy in such circumstances, particularly in the event of serious pollution, and it must be assumed that there will be unfavourable media comment.

Therefore, the shipowners will almost certainly need to prepare their own media response. This is usually best done by appointing a specialist shipping media consultant, although some shipowners may have already nominated a particular firm in their emergency response plan.

If time permits, media releases should be discussed and coordinated with the shipowners' lawyers and insurers before release in order to ensure that all parties adopt a consistent approach. Shipowners can often feel pressurised to make promises which may meet the immediate demands of certain parties but which may, nevertheless, be impossible to achieve in practice, and may be inconsistent with the shipowners' legal obligations and liabilities. In this regard, shipowners must keep in mind that their insurers afford cover only for *legal* liabilities. Therefore, if time permits, the issue of cover for the cost of media advisers should be discussed between the shipowners and their insurers before instructions are given.

#### **27.2.2.5 Local Representation**

Inevitably, the shipowners will need to be represented locally in the country where the incident has taken place. In most cases, this can best be done by the P&I club's local correspondents who are effectively the 'eyes and ears' of the club in that country. They provide local knowledge and contacts and can provide any assistance that may be necessary to enable those that are instructed by or on behalf of the shipowners to travel to the scene of the incident, and to carry out the tasks with which they have been entrusted. Such assistance is of particular help to any P&I club (or H&M) representative that may need to attend 'on-site'. The attendance on site of such a representative can often provide valuable support both for the local correspondents and for any shipowners' representative(s) that may also be attending on site, and can facilitate quick decision making and the orderly transfer of detailed information back to the insurers and all other interested parties. The attendance of such a representative also provides a visible link between the insurers (normally the ultimate paying party) and the local authorities, and can facilitate the negotiation of any requests for financial security that may be made by claimants.

All these people will need to work closely together to provide the shipowners and their insurers with the information and advice that will be necessary to enable them to take the decisions that will be required to respond promptly and satisfactorily to the various issues which have arisen and which will continue to arise.

### 27.2.3 Response Action

#### 27.2.3.1 People

There is no doubt that the local authorities will have to be notified of the incident and the authorities should be asked to allow the injured AB to be medically evacuated as soon as possible. If the shipowners have no local agent, the local P&I club correspondent may be able to assist in this respect. However, the shipowners should appreciate that they may be required to guarantee the cost of the evacuation and/or any medical treatment.

It is also necessary to consider whether the master should be medically evacuated. It is unlikely that his injury can be properly assessed on board but it may be wise, in any event, to seek the opinion of a doctor before taking any decision. If the doctor advises that he should be evacuated, this will leave the vessel without a master at a critical time. Therefore, it will be necessary to consider whether the chief officer can take over the master's responsibilities or whether it is necessary (and possible) to fly out a replacement master.

#### 27.2.3.2 Environment

There is probably relatively little that can be done at the scene of the incident at this stage but the local authorities may, nevertheless, take what they consider to be prudent anti-pollution measures (e.g. the deployment of a boom around the vessel) or call upon the shipowners to do so. It may also be appropriate to transfer bunkers to a (more) protected location on board provided that this does not affect the vessel's stability. However, weather conditions may have a bearing on what is or is not possible. Finally, since prevention is always better than cure, the most effective anti-pollution measure that can probably be taken at this stage is the engagement of expert salvage assistance.

#### 27.2.3.3 Property

Based on current information, it seems that the cargo has not yet been affected, and it is unlikely that much can be done at this stage about any damage that has already been sustained by the vessel. If the vessel can be refloated in due course, the extent of the damage will have to be assessed at a later date. In the meantime, the engagement of expert salvage assistance is also probably the best measure that can be taken at this stage in order to prevent or minimise further property loss or damage. Since salvage assistance is required urgently, the shipowners do not have the luxury of being able to negotiate the most favourable salvage terms, but is likely in any event that the salvors will only be prepared to offer assistance on the basis of Lloyds Open Form (LOF) terms.

#### 27.2.3.4 Information and Documents

The salvors and the vessel's classification society may need to be provided with relevant technical information to enable them to make a technical assessment of the vessel's damaged condition and stability. The shipowners' lawyers and P&I club will also need essential documents such as the contracts of carriage (charterparty, bills of lading etc.) to enable them to make a realistic assessment of the shipowner's potential legal liability. The media will also be hungry for information. Therefore, details of the vessel, the amount and type of bunkers on board, her classification society and flag, and other relevant facts, will need to be gathered for the purpose of press statements.

There is much information and documentation that the shipowners should either have available already or, if not, which they should start to collect immediately. It may also be wise to identify at an early stage the person in the shipowners' office who is to be responsible internally for document retention and collection.

#### 27.2.3.5 The Notification of Other Parties

Most shipowners will wish to notify their insurers first since they are the people whom the shipowners believe will be able to give them the best help to deal with such a complex matter. However, it must be remembered that many other governmental and other bodies will also need to be notified promptly, and that a failure to do so may not only hamper the shipowners' subsequent response plans, but may also subject them to sanctions.

##### 27.2.3.5.1 Governmental Authorities<sup>11</sup>

Many countries in which a casualty has occurred have strict rules identifying the parties or bodies in that country that must be notified promptly, the form and type of information that is required, and the time scale in which notification must be given.<sup>12</sup> Furthermore, the flag state is likely to wish to carry out its own investigation

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<sup>11</sup> For more detailed commentary on maritime regulation and compliance issues see Chapter 22 (Maritime Regulation and Compliance).

<sup>12</sup> For example, US federal laws require an oil spill to be reported to the National Response Centre (NRC), or if this is not possible, then to the local US Coast Guard or the local office of the US Environmental Protection Agency 'immediately', 'promptly', or 'as soon as possible' after the shipowners are aware of the discharge and individual states have their own state law which requires similar notification to be given to local state authorities. There is a duty to report even if no spill has actually occurred but there is a 'substantial threat of discharge'. Australia, China, South Africa and Singapore have similar requirements. Furthermore, shipowners who wish to send their ships to the USA must conclude beforehand a contract with a recognised salvage company or similar private organisation (Oil Spill Response Contractors (OSRO)) to organise, manage and actually carry out any pollution clean-up operations that may be required whilst the vessel is in that country. A similar system is also now in force in China. Nevertheless, despite such appointments, the shipowners and OSROs will almost certainly have to discuss their intentions with, and obtain approval for their plans from, the relevant governmental authorities.

into the incident and will require full and prompt notification. Therefore, care must be taken by shipowners to report the relevant facts to the relevant authorities within the required time scale.

Shipowners should also appreciate, particularly if there is a risk of pollution, that almost all countries that have a seaboard have wide powers of intervention and compulsion, either under international conventions or under national legislation,<sup>13</sup> which they will not hesitate to use if they consider that the shipowners and their advisers are not responding properly or sufficiently to the situation. Therefore, local authorities will invariably demand to be kept fully and regularly informed of the condition of the vessel and the progress of the salvage operation. This can cause problems or delay since decisions may be taken by a combination of private and governmental or quasi-governmental bodies, some of whom may have competing interests. There is no doubt that a good level of co-operation enables effective, sensible and reasonable decisions to be taken for the benefit of all concerned.

#### **27.2.3.5.2 Contractual Partners<sup>14</sup>**

Parties with whom the owners have a commercial relationship will also wish to be notified and kept informed. For example, the time charterers will be concerned about the length of any off-hire, and voyage charterers will be concerned to know when, or indeed, if, their cargo is likely to be delivered. The vessel's 'next' charterer may also have a significant interest if the current charter is about to come to an end at the time of the incident. If a major oil company is involved, it is likely to want to issue its own press releases and may well seek to influence the decision-making process.

#### **27.2.3.6 The Need to Take Care**

The duty to notify may often oblige the shipowners to report the cause of the incident. In some cases, the immediate cause may be obvious (e.g. "the vessel's hose came away from the manifold, causing oil to be lost into the sea"), but the underlying cause(s) is (are) likely to require further investigation. In other cases, the immediate cause may not be obvious, in which case early speculation is unwise as it can lead to wrong assumptions and wrong decisions. It should also be remembered that other parties will be seeking to protect their own interests which may be different from those of the shipowners, and that such parties may well bring claims against the shipowners in due course. Therefore, shipowners would be wise to remember that, whilst it may be mutually beneficial in the short run to seek to establish a common interest with some of these parties, they should take the

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<sup>13</sup> See Chapter 14.7 (Salvage Claims).

<sup>14</sup> For commentary on chartering issues see Chapter 4 (Charterparty Claims).



appropriate measures to ensure that their interests (and those of their insurers) are properly protected. Therefore, it is important that information provided to any or all of these parties is released in a consistent manner.

#### **27.2.4 Potential Claims**

Even at this very early stage the shipowners and their advisers should endeavour to make a preliminary assessment of the claims that are likely to arise. Using the PEP acronym, the following claims seem likely:

##### **27.2.4.1 People**

The injured AB may well bring a claim for loss of wages and for any disability (temporary or permanent) that he or she may suffer, and it is likely that the shipowners will be responsible for the cost of medical treatment and repatriation. Depending partly on the severity of his injury, the master may also bring a similar claim, and other crew members may claim for loss of personal effects and for loss of their employment.

Most claims of this type are brought on a contractual basis under the relevant contract of employment which is likely to include the terms of a collective bargaining agreement (CBA) entered into between the shipowners' association and the crew member's union. A concurrent claim could also be brought in tort for negligence unless the terms of the contract of employment preclude the crew members from making such a claim. The shipowners are likely to incur strict liability under the terms of the contract of employment (i.e. the shipowner will be liable irrespective of fault) whereas their liability in tort will depend on whether the accident can be attributed to the negligence of the ship owners (or one of their other employees).

The shipowners may also incur additional expenditure if the vessel is not refloated but breaks up and becomes a total loss since the entire crew will then have to be repatriated. Even if the vessel is refloated, an exchange of some crew members may be appropriate, particularly those crew members who may have suffered stress and who may have been obliged to work longer hours as a result of the casualty and the salvage operation.

##### **27.2.4.2 Environment**

It appears that damage has already been caused to the reef and claims may be brought against the shipowners by local holiday companies, hotel owners, recreational activity providers, fishermen and the local authorities for loss of business and amenities. Indeed, salvage activity and/or refloating attempts may cause yet further damage, in which case, notwithstanding the fact that the further damage has been caused by the salvors, claims are likely to be brought against the shipowners. In such circumstances, the shipowners are likely to face difficulties in obtaining

an indemnity from the salvors unless the latter can clearly be seen to have acted negligently. Whilst salvors are expected to conduct their work in a professional manner, courts and arbitration tribunals realise that such work is challenging and risky and do not easily conclude that damage caused in the course of the salvage operations is due to the negligence of the salvor.

If the vessel cannot be salvaged, her cargo and her bunkers are likely to be lost to the sea. In such circumstances, careful consideration will have to be given to whether the cargo is a pollutant and/or whether it can be 'cleaned up' in any meaningful and effective manner. In any event, it will be necessary to try to contain and/or clean up the bunker spillage and the shipowners can expect to receive claims for contamination damage to the environment and to private and public property.

#### **27.2.4.3 Property**

There is clearly some physical damage to the ship, and the ship could become a total loss if the salvage operations are not successful. If the ship is saved, then the shipowners will incur a liability to the salvors pursuant to the salvage award and will wish to claim that sum and the cost of repairing the ship from the vessel's H&M insurers. If the ship becomes a total loss, then the shipowners will wish to claim the insured value of the ship from the H&M insurers. Furthermore, if the ship cannot be salvaged, it is likely that the local authority will order the wreck to be removed at the shipowners' cost although in practice, such removal is normally carried out and financed by the ship's P&I insurers.

Should the cargo be damaged,<sup>15</sup> or should bunkers be lost, the shipowners are likely to face claims in due course from the cargo owners and the time charterers (as owners of the bunkers). In the meantime, it is likely that the shipowners will wish to declare General Average so that the cost of any future salvage award can be apportioned following the completion of the salvage operation in accordance with the values of the property at risk at the time of redelivery by the salvors.<sup>16</sup> However, the shipowners must assume that the cargo owners and the time charterers are likely to refuse to pay their contribution in due course if they conclude that the incident resulted from the shipowners' breach of the charterparty or the contract of carriage. For example, shipowners will often be faced with allegations that they have not exercised due diligence to make the vessel seaworthy.

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<sup>15</sup> For commentary on cargo claims see Chapter 3 (Cargo Claims).

<sup>16</sup> For further commentary see Chapter 14.2 (Salvage Claims).

Finally, it is likely that the charterers will put the vessel off hire. Therefore, the shipowners should notify and involve their Defence insurers promptly to ensure that the charterers are indeed, entitled to place the ship off-hire, and that cover for legal costs for any future disputes is safeguarded.

### 27.2.5 Resume

The shipowners, their insurers and their advisers will be focussing on all of these issues during the first few days after the incident, but the list is not exhaustive. In almost every major incident, issues will arise that are unique to that incident and which have, therefore, not been considered in any previously-prepared emergency response plan. Some issues may require immediate action, whereas others can be deferred, but all will require careful consideration and discussion with the shipowners' insurers and advisers. The greatest challenge for shipowners is how best to give the right priority to the right issue(s) at the right time.

## 27.3 Stage 2 of the Casualty

Three days have passed since the occurrence of the casualty and the situation is now as follows:

*"A contract on LOF terms incorporating the SCOPIC Clause (which has not yet been invoked) has been agreed with a firm of professional salvors. The salvors have advised that one of their salvage tugs is approximately three days' sailing time from the casualty and that a salvage master and some other personnel whose attendance they consider necessary have flown out to the scene.*

*Following consultation with a doctor specialising in head injuries, the shipowners have agreed with the master that he should remain on board until a replacement master can relieve him. A replacement master is sent out the following day, but has been unable to obtain a visa on his arrival and, notwithstanding the assistance that has been provided by the local club correspondent, has been detained by immigration officials over night. His visa is issued locally the following day, but he was unable to relieve the existing master until late on day 2. Following a de-brief meeting between the two masters on board, the original master was taken ashore for a medical examination early on day 3. He was diagnosed to be suffering from severe concussion and was kept in hospital overnight for observation. The hospital advised that it intended to carry out further tests, but was not equipped to deal with serious head injuries.*

*Unfortunately, due to continued bad weather, the salvage tug has been delayed. Despite the fact that there has been relatively little tidal rise or fall in the vicinity of the grounding, and despite the fact that the vessel has been 'ballasted down' as much as possible, the vessel has 'worked' on the reef. Consequently, a transverse*

crack has developed in the deck just forward of no. 3 hold. Further pounding on the rocks caused this crack to propagate and by the time that the salvage tug arrived, the two parts of the vessel were connected only by a small amount of steelwork. The salvors invoked SCOPIC immediately and demanded security for the customary USD 3 million specified in the SCOPIC Clause. Up to that time, there had been no spillage of bunkers, but the initial advice from the salvors was that it was only a question of time before the double bottom tank beneath hold no. 3 would be breached. The salvors also advised that the vessel could not be refloated in one piece and that she would break into two pieces very shortly.

By this time, the local authorities have been informed of the problem. They have issued an order that the pollutants on the vessel must be removed as soon as possible and that the vessel herself must also be removed. However, whilst the salvors were preparing their pollutant removal plan for approval by the authorities, the vessel broke in two. As a result, fuel oil was lost from the bottom tank beneath no. 3 hold.

The fore part of the vessel remains aground. The salvors succeeded in securing a line to the aft part but the aft part started to sink before they could tow it into deeper water.

When the vessel broke in two, the crew abandoned her. They were rescued without any injuries and taken ashore, where the senior officers, including the replacement master, were detained (in a hotel) and their passports confiscated, pending an official enquiry and possible criminal charges.

The incident is the main item of news locally and is featured in shipping media worldwide. Furthermore, some passengers on a cruise ship that happened to be visiting the island at the time took photographs and a video film of the incident and these have been published on the internet. Before long, there is increased media focus on what is described as an 'environmental catastrophe' from several mainstream media outlets in the USA and Europe."

Clearly, a serious incident has now developed into a major casualty. Intense media interest inevitably means that the shipowners will need assistance from an organisation that has experience on how best to deal with media enquiries in such cases. Nevertheless, it is important that the shipowners should remain focussed on the PEP approach and that they and their insurers and advisers should continue to concentrate on the action that is required in relation to each of these issues.

## 27.3.1 Current Needs

### 27.3.1.1 People<sup>17</sup>

The following issues now require urgent attention:

- The crew members will need food, clothing and accommodation, and it will probably be best to accommodate them in the same hotel if possible;
- Whilst there will, undoubtedly, be considerable media interest in the crew, it is probably inappropriate to expose crew members who have just experienced the trauma of a shipwreck to the attentions of the media;
- Those crew members that are allowed to leave will require repatriation;
- Some crew members may require medical attention, particularly the master and the injured AB.

The master may prove to be a particular problem since he is a key witness to the events leading to the grounding and may be requested by the local authorities to remain within the jurisdiction pending completion of their investigations. It is also possible that he may face criminal charges. However, the hospital where he is being treated is not equipped to deal with serious head injuries and, if the local authorities will not allow the master to be flown to a location where the required medical facilities and competence are available, the shipowners may need to fly a doctor who specialises in head injuries to the hospital to assist the local hospital staff.

It may also be necessary, in view of the detention of the senior officers and the looming threat of criminal action against them and the shipowners, to instruct local criminal lawyers to represent them both. However, it may be necessary to consider whether one firm of criminal lawyers can represent both the officers and the shipowners. It is also probably wise to investigate whether it is possible to put up bail to ensure the repatriation of the officers, and if so, to investigate the means of doing so.<sup>18</sup>

Since the crew members are the main witnesses to the events leading to the casualty, it is essential that the relevant crew members are interviewed by the lawyers and experts that have been instructed by the shipowners, and that statements are taken from them before they are repatriated since, although considerable evidence is likely to remain on board the vessel in both electronic and paper form, it may be difficult if not impossible to gain access to any part of the vessel at this time. Whilst it may be difficult in the circumstances to gain access to all the relevant crew members, an attempt should be made in the light of local law and practice since

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<sup>17</sup> For commentary on the shipowner's responsibilities to crew members see Chapter 22.5 (Maritime Regulation and Compliance).

<sup>18</sup> For comment on the possibility of criminal action against crew member see Chapter 12.4.2.2 (Pollution Claims).

much may depend on the evidence that crew members are able to give, and on the documentation that they were able to bring with them when they left the vessel. Whilst the safety of life is paramount, the securing of as much evidence as possible is also vital, and the shipowners should have this issue firmly in mind from the start.

### **27.3.1.2 Environment**

The worst has happened. The vessel has broken in two and heavy fuel oil (bunkers) and possibly some cargo has been spilled into a pristine, tropical marine environment. Consequently, the shipowners face two major difficulties.

Firstly, there is a risk that the spill will cause significant damage to a locality that obtains much of its income from tourism and the fishing industry, and which is home to a colony of rare turtles. The risk to the turtles is immediately identified by both local and international wildlife organisations and considerable publicity is given to a 'Save the Turtles' campaign. A local wildlife organisation offers its services to the shipowners to protect the turtles and some overseas organisations offer to travel to the island to help. The shipowners will need to consider how best to respond to such offers and it may be better to focus on efforts to prevent any oil reaching the turtle colony since this should also, at least to some extent, mitigate the losses which are likely to be sustained by the tourism and fishing industries.

Secondly, the island does not have the equipment or personnel that is necessary to clean up the spill but the shipowners have nevertheless, been instructed by the local authorities to take all necessary measures to clean up the spill and prevent any further spillage. Consequently, the necessary equipment will have to be brought from overseas, which will take time even if everything goes well. Much depends on where such equipment can be found, whether it is available immediately, and the weather both locally and during the transit of such equipment.

It has often proved to be more effective to train local personnel rather than import a large team of people who have no local knowledge and who place an additional strain on the local environment. Knowledge of local conditions is important and, therefore, it may be advantageous to hire some of the local fishermen to assist with the clean-up operation particularly since it will provide the fishermen with an income at a time when the authorities may impose a ban on fishing. Nevertheless, it will still probably be necessary to fly in a small number of experts called spill managers.

The clean-up plans and procedures are likely to be supervised by an ITOPF representative who will normally attend at the scene as soon as possible after the event. The ITOPF representative may be accompanied by a senior person from the

shipowner's P&I club and will normally draft a clean-up response plan for submission to the local authorities which will identify appropriate local resources and spill managers, and any other equipment or personnel that may need to be imported.

### **27.3.1.3 Property**

The vessel has broken in two and at least some of the cargo has been damaged. Therefore, the shipowners and the salvors will need to discuss urgently whether any part of the ship and/or cargo can be saved. In any event, the local authorities have ordered that the ship and any pollutants that there may be on her must be removed. Therefore, if the salvage of the ship and/or cargo is not commercially viable, the shipowners and their P&I insurers will have to investigate the possibility and cost of wreck removal.<sup>19</sup> The cargo in the fore part – which is currently aground – can potentially be saved, but this is likely to require discussion with the H&M insurers, who may feel that the continuation of LOF services in circumstances where, at best, only a part of the vessel may be recovered is inappropriate. Therefore, the shipowners and their insurers will have to decide how best – technically and contractually – to remove the fore part of the vessel and the cargo that is contained therein.

## **27.3.2 Potential Claims**

Whilst the shipowners' attention must be focussed in the initial aftermath of a casualty on how best to respond to the numerous practical problems that arise, the passage of time should enable the shipowners to consider matters from a broader perspective. The shipowners are likely to have already spent, and are likely to have to continue to spend, very large amounts of money to investigate the cause of the casualty and to control and minimise further damage to people, the environment and property. Nevertheless, there is no doubt that, despite these efforts, the shipowners will have to deal with many substantial claims from many of the parties involved.

### **27.3.2.1 People**

Most of the relevant claims have been identified in Chapter 27.2.4 above. The shipowners will also appreciate that the families of the two injured crew members may request the shipowners to fly them to the scene of the casualty at the shipowners' cost.

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<sup>19</sup> For commentary on wreck removal see Chapter 16 (Wreck Removal Claims).

### 27.3.2.2 Environment

Claims may be brought against the shipowners by:

- holiday companies, hotel owners, recreational activity providers, fishermen etc., for loss of business; and by
- national and local governments for clean-up costs and for loss of amenities.

Criminal sanctions may also be brought against both shore based and ship based personnel.

### 27.3.2.3 Property

#### 27.3.2.3.1 Cargo<sup>20</sup>

It is now clear that at least some of the cargo – that contained in the aft part of the vessel – will be a total loss and the owners of that cargo are likely to bring a claim against the shipowners for the value of that cargo.

If attempts to salvage the cargo that remains in the fore part of the ship are successful, the owners of that cargo are likely to have to contribute to the amount that is awarded to salvors under the salvage contract. However, if such attempts are not successful, the cargo in the fore part may also be a total loss. In either case, the cargo owners are likely to bring claims against the shipowner either for payments made by them to the salvors or for the full value of the lost cargo.

#### 27.3.2.3.2 Bunkers

The identification of the whereabouts of any bunkers that are on board is normally a question that the shipowners should address urgently. The aft part of the vessel is likely to contain the greatest quantity of bunkers and there is a good chance that this quantity will leak out over time. However, the fore part may also contain some bunkers (and other possible pollutants, such as paint). The time charterers (as owners of the bunkers) will almost certainly claim the value of their (lost) property from the shipowners.

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<sup>20</sup> See Chapter 3 (Cargo Claims).



#### 27.3.2.3.3 *Charterparty Claims*<sup>21</sup>

Since the vessel has now broken in two she is likely to be treated as a total loss or will, at the very least, not be available for future service for some considerable time. Therefore, the time charterers are likely, not only to continue to treat the vessel as off-hire, but also to claim damages for loss of profits during any remaining period of the charter when they do not have the use of the vessel.

**NB!** It is likely that the cargo interests and charterers will each require security for their claims. Such demands are unlikely to be made at this early stage, but the shipowners should bear this in mind when they consider more general tactical and strategic issues, such as the possible limitation of liability and the relevance of law and jurisdiction (See Chapter 27.3.4 below).

#### 27.3.2.3.4 *Special Compensation Claim*<sup>22</sup>

It looks increasingly likely that the vessel and cargo will become a total loss and that consequently, the salvors will probably not receive a traditional 'no cure no pay' salvage award. The salvors may, therefore, claim Special Compensation payments under the SCOPIC Clause for their successful work in preventing or minimising pollution.

### 27.3.3 Potential Liability

On first impression it would appear that the owners of a vessel which has ran aground on a chartered reef are likely to find it difficult in most jurisdictions, and under most legal systems, to defend these various claims. However, it must not be assumed that the shipowners have no means to defend themselves or to minimise their liability.

#### 27.3.3.1 Defences

It is unlikely that the shipowners will be able to successfully defend the personal injury and other claims that may be brought by the crew members pursuant to their contracts of employment. Similarly, the shipowners are unlikely to have any defence to any salvage or Special Compensation award that may be made in favour of the salvors under the LOF and SCOPIC agreements. However, whilst the shipowners may not have a defence for pollution and clean-up claims resulting from the bunker spillage (or from the spillage of the cargo if the cargo is considered to be a hazardous and noxious substance) in the country where the incident occurred, there is usually scope to negotiate the quantum of such claims.

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<sup>21</sup> See Chapter 4 (Charterparty Claims).

<sup>22</sup> For more detailed commentary see Chapter 14.3 (Salvage Claims).

By way of contrast, the shipowners may have a defence to claims that may be brought for the loss of, or for damage to, the cargo or bunkers. The cargo claims will probably be brought pursuant to the terms of a contract of carriage such as a bill of lading, and the claim for the loss of the bunkers and the loss of use of the vessel will probably be brought under the terms of the time charterparty, both of which are likely to be subject either compulsorily or by agreement to the provisions of the Hague-Visby Rules, Article III Rule 2 (a) of which provides that:

*“Neither the Carrier nor the ship shall be responsible for loss or damage arising or resulting from*

*a) Act, neglect or default of the master, mariner, pilot, or the servants of the Carrier in the navigation or in the management of the ship.”<sup>23</sup>*

#### **27.3.3.2 The Limitation of Liability<sup>24</sup>**

If the shipowners are not able to exclude their liability completely they may, nevertheless, have the right to limit that liability, and if they are able to do so, this may reduce the amount of compensation that they are obliged to pay by a considerable amount. Shipowners should also remember in this regard that their liability insurers are obliged to indemnify them only for those amounts to which they are entitled to limit their liability.

The right to limit liability exists only to the extent that it is allowed by international convention or national law. Whilst most countries are parties to international conventions, not all conventions are enforced by all countries. Therefore, it is necessary to investigate which conventions are enforced in which countries and, if the relevant convention is not enforced in the particular country, whether the right to limit liability is given by the national law of that country.

Since the ship that has been involved in the casualty described above is not carrying oil as cargo the various CLC and Fund Conventions are not relevant. However, if the cargo is considered to be a hazardous or noxious substance then the shipowners may be able to limit their liability for pollution caused by the cargo pursuant to the HNS Convention should this have come into force and be enforceable in the country in question. In any event, the spillage of the bunkers will probably be regulated by the Bunker Convention which entitles a shipowner to limit his liability in accordance with the 1957 or 1976 Limitation Conventions or the 1996 Protocol to the 1976 Convention (whichever is in force in the relevant country). Similarly, claims for the loss of, or damage to, the cargo, or for personal injury, are also subject to limitation under the 1957 or 1976 Limitation Conventions or the 1996 Protocol.

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<sup>23</sup> For more detailed commentary see of Chapter 3.2.9.3.1 (Cargo Claims).

<sup>24</sup> For further commentary see Chapter 21 (Limitation of Liability).

However, the shipowners are not entitled to limit their liability for any sums that may be payable by them to salvors by way of a traditional 'no cure no pay' salvage award or by way of Special Compensation for pollution prevention services. Similarly, if the ship cannot be salvaged and becomes a wreck, the shipowners may not be able to limit their liability for wreck removal costs that may have been incurred by, or at the order of, the local government. Whilst the 1957 and 1976 Limitation Conventions and the 1996 Protocol all allow limitation for wreck removal in principle, many countries have, nevertheless, exercised the right that is given to them by these conventions to exclude the right to limit liability for wreck removal.

Therefore, the shipowners' liability for many of these various claims could be substantially reduced pursuant to these conventions unless they are found to be guilty of certain conduct. Under the 1976 Limitation Convention and the 1996 Protocol there is a presumption that the shipowners are entitled to limit their liability, and they are denied this right only if the claimant proves that *"the loss resulted from (the) personal act or omission (of a senior officer of the ship owning company), committed with the intent to cause such loss, or recklessly and with knowledge that such loss would probably occur."* Such conduct is normally very difficult for a claimant to prove. However, the position is different under the 1957 Limitation Convention. The shipowners are entitled to limit their liability under this convention only if they prove that the incident occurred without the 'actual fault or privity' of a senior officer of the shipowning company. This test normally makes it more difficult for shipowners to prove their right to limit their liability.

### 27.3.3.3 Jurisdiction<sup>25</sup>

Since different countries have different laws, the ability of the shipowners to either exclude or limit their liability depends very largely on the country that has jurisdiction to determine the particular issue. The issue is complicated since the claims that are likely to be brought against the shipowners may be brought in contract, or in tort or pursuant to international conventions or national laws, and it cannot be assumed that all claims will be brought, and all issues determined, in the same jurisdiction.

The claims that are brought in contract (such as the cargo claim, the claims for loss of the bunkers and the use of the vessel, the crew claims and the salvage claim) would normally be resolved subject to the law and jurisdiction stipulated in the particular contract(s). However, whilst the time charterparty, the bill of lading and the salvage contract may be subject to English law and jurisdiction, the crew employment contracts are likely to be subject to the law and jurisdiction of the country of origin of the crew. Furthermore, whilst the bill of lading, the time charter and the salvage contract may all be subject to English law and jurisdiction, the particular forum for

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<sup>25</sup> For further commentary see Chapter 19 (Law and Jurisdiction).

dispute resolution may be different. For example, the bill of lading may be subject to the jurisdiction of the English High Court, the time charter may be subject to arbitration in London by London Maritime Arbitrators Association (LMAA) arbitrators and the salvage contract may be subject to arbitration in London by a Lloyds salvage arbitrator.

The claims for pollution damage will not be brought pursuant to contract, and will probably be brought in the local jurisdiction where the loss or damage was caused pursuant either to international conventions (such as the Bunker or HNS Conventions if ratified by the country in question) or the national law.

Therefore, it is very likely that the shipowners will be faced with claims in at least two different jurisdictions. Indeed, there could be even greater diversity if (for example) cargo interests were to believe that they may obtain a more favourable decision in another court and therefore, ignore the law and jurisdiction clause in the contract of carriage. In such circumstances, the shipowners might wish to consider the possibility of seeking an anti-suit injunction from a court in the contractually agreed jurisdiction.

#### **27.3.4 Response Action**

Therefore, it is important that a detailed analysis be made as soon as practically possible of the circumstances of the grounding, the basis on which the various claims are made and the likelihood of being able to either successfully defend the claims or to limit liability for the claims, so that a strategic assessment of owners' exposure can be made, and a collective decision can be taken as to the general approach that is to be adopted vis-a-vis claimants. Such an analysis will encompass not only the events on board in the hours and days leading up to the grounding, but also wider issues relating to the due diligence of the shipowners in relation to the seaworthiness of the ship, and the recruitment, training and supervision of the officers over the prior months and even years. All relevant records will have to be examined minutely by lawyers and experts, so that the shipowners need to ensure that all relevant information and documentation relating to these issues are made available promptly for such examination.

Even if the analysis concludes that the shipowners have substantial exposure to the claims, the exercise is, nevertheless, normally useful as it will indicate that the shipowners should investigate and take advantage of whatever possibilities there may be to settle claims on the best terms possible. It will also establish the proactive steps that the shipowners and their advisers should consider taking in order to improve the shipowners' overall standing. For example, the owners of ships that may be involved in a casualty such as the one described in this scenario can normally be expected to adopt a strategy based on the following principles:

- All claims should, insofar as possible, be determined pursuant to the same law by the same forum in the same jurisdiction;
- All claims should be resolved on the basis of legal liability;
- The shipowners should seek to limit their liability in accordance with any applicable international convention or national law; and
- Claims which can be shown to have merit and which are properly supported by evidence should be resolved as quickly as possible.

However, the successful implementation of these aims will normally require the shipowners and their advisers to consider the following questions:

- What law and jurisdiction governs the claim in question?
- What (if any) potential defence(s) are the shipowners likely to have to the various claims in that jurisdiction?
- Which claims are subject to limitation in that jurisdiction?
- Is the law and jurisdiction specified in the first question (the most) favourable law and jurisdiction for the shipowners?

Very often, this last question may produce a negative answer, in which case, it will then be necessary to consider whether there is anything which the shipowners can do to ensure that the claims are resolved in, and pursuant to the law of, the country that is considered by them and their advisers to be (the most) favourable for the shipowners.

However, this is not an exhaustive list. Shipowners should 'expect the unexpected' in such matters and should, whilst keeping their strategic aim(s) in mind, retain the flexibility which may be necessary to deal with unexpected and unusual issues or developments.

## 27.4 Conclusion

A casualty such as this will test most shipowners to the limit. Not only will substantial sums of money be at stake, but the shipowners' reputation may also be 'on the line'. Therefore, commercial considerations will inevitably play a part in the shipowners' thinking and it can often be a challenge to ensure that these issues are managed in a manner that is consistent with the shipowners' legal liabilities. Shipowners need to plan, prepare and practise internally for such incidents, always remembering that it is often the little things that are missed (e.g. 'our Designated Person is on holiday in the mountains where there is no mobile phone signal and we have nobody who can deputise for him'), but which can have a significant impact. However, shipowners should also ensure that they are aware of the various sources of assistance and support that is available to them outside their offices. They should be aware, in particular, of the extent of the insurance cover that they have and of the assistance and support that they can expect from their insurers. The successful control and resolution of complex casualties depends very heavily on the prompt establishment of capable internal and external teams, and on the effective manner in which these teams can work smoothly together and with other parties who might be viewed as 'opponents.' In most cases, open and regular contact, often face to face, with others that have a part to play in relation to the incident response is essential.

Whilst the owners of any ship that is involved in a casualty will, understandably, wish to focus in the early stages on immediate issues, it is important that they should also focus, even at that early stage, on the wider perspective. Early decisions will have a major impact on subsequent issues, and it is important to keep that in mind when dealing with immediate issues. Decisions need to be taken in a strategic manner.

Last – but definitely not least – it is important to be in the driving seat, not the back seat!

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Help Centre

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## Chapter 28

# Help Centre

### A Relevant Organisations

It is not possible to provide details of all relevant organisations and websites. Therefore, the following sections merely include sources that are commonly used. Website addresses are not included since such addresses may change from time to time. However, such organisations can be readily accessed by internet searches.

Reference is also made to the website of The International Maritime Organisation (IMO) which keeps a directory of Maritime Links according to Subject/Category or Country/Region at:

<http://www.imo.org/KnowledgeCentre/Pages/IMOLinksDirectory.aspx>

### 1 Maritime Safety Authorities/Safety Boards/Coast Guards

- Australian Transport Safety Bureau (ATSB) – <http://www.atsb.gov.au/>
- China Maritime Safety Administration – <http://www.msa.gov.cn/>
- European Maritime Safety Agency <http://www.msa.gov.cn/>
- Hong Kong Marine Dept – <http://www.mardep.gov.hk/>
- Hong Kong Port – [http://www.pmb.gov.hk/pmb/&Maritime Board](http://www.pmb.gov.hk/pmb/&MaritimeBoard)
- Japan Coast Guard – [http://www.kaiho.motnet.go.jp/e/index\\_e.htm](http://www.kaiho.motnet.go.jp/e/index_e.htm)
- Marine Accidents Inquiry Agency, Japan – <http://www.motnet.go.jp/maia/english.htm>
- Maritime Safety Authority of New Zealand – <http://www.msa.govt.nz/>
- Marine Accident Investigators International Forum – <http://www.maiif.net/>
- The Maritime Industry Foundation – <http://www.themaritimefoundation.com/>
- US Coast Guard – <http://www.uscg.mil/>
- UK Marine Accident Investigation Branch (MAIB) – <http://www.open.gov.uk/maib/maibhome.htm>
- UK Maritime and Coastguard Agency (MCA) – <http://www.mcga.gov.uk/>
- Transportation Safety Board of Canada – <http://www.bst-tsb.gc.ca/marinelist.html>
- Transport Accident Investigation Commission, New Zealand – <http://www.taic.org.nz/>
- The National Transportation Safety Board, USA (NTSB) – <http://www.ntsb.gov/>

## 2 Classification Societies

**IACS** International Association of Classification Societies Ltd: <http://www.iacs.org.uk/>

- **ABS\*** American Bureau of Shipping
- **BV\*** Bureau Veritas
- **CBS** Cyprus Bureau of Shipping
- **CCS\*** China Classification Society
- **CRS\*** Croatian Register of Shipping
- **DNV\*** Det Norske Veritas
- **GL\*** Germanischer Lloyd
- **HRS** Hellenic Register of Shipping
- **INSB** International Naval Surveys Bureau
- **IRS\*** Indian Register of Shipping
- **KRS\*** Korean Register of Shipping
- **LRS\*** Lloyd's Register of Shipping
- **NKK\*** Nippon Kaiji Kyokai
- **PRS\*** Polski Rejestr Statkow
- **RINA\*** Registro Italiano Navale
- **RINAVE** Registro Internacional Naval (Portugal)
- **RS\*** Russian Maritime Register of Shipping
- **TL** Turkish Lloyd

The Classification Societies that are designated with an asterisk are members of IACS at the time that this publication goes to print.

## 3 Ship Registers<sup>1</sup>

- Antigua and Barbuda
- Bahamas
- Belgium
- Bermuda
- Cayman Islands
- China
- Cyprus
- Denmark
- Finland
- Germany
- Greece
- Hong Kong
- Isle of Man

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1 Detailed requirements for ship registration in different jurisdictions can be found in the Hill Dickinson publication "International Ship Registration Requirements" which can be accessed at: <http://www.hilldickinson.com/pdf/International%20ship%20registration%20requirements.pdf>

- Italy
- Liberia
- Luxembourg
- Malaysia
- Malta
- Marshall Islands
- Netherlands
- Netherlands Antilles
- Norway
- Panama
- Singapore
- Sweden
- United Kingdom
- United States
- Vanuatu

#### **4 International Associations for Ship Operations**

- BIMCO
- European Community Ship owners' Association (ECSA)
- International Chamber of Shipping (ICS)
- Intercargo
- International Association of Ports and Harbors (IAPH)
- International Bunker Industry Association – <http://www.ibia.net/index.asp>
- International Council of Cruise Lines (ICCL)
- InterManager
- International Maritime Pilots' Association (MPA)
- The International Navigation Association (PIANC)
- International Parcel Tankers Association (IPTA)
- International Shipping Federation (ISF)
- International Tugmasters' Association
- Intertanko
- Oil Companies International Marine Forum (OCIMF)
- Society of International Gas Tanker & Terminal Operators (SIGTTO)
- Vessel Operators Hazardous Materials Association (IVODGA) – <http://www.vohma.com/>

## 5 International Governmental or Quasi-governmental Organisations

- Equasis
- European Commission Directorate for Maritime Affairs and Fisheries (DG Mare)
- European Maritime Safety Agency (EMSA)
- European Shippers' Council (ESC)
- International Hydrographic Organisation (IHO)
- International Labour Organisation (ILO)
- International Maritime Organisation (IMO)
- United Nations Conference on Trade and Development (UNCTAD)
- United Nations Commission on International Trade Law (UNCITRAL)
- World Customs Organization (WCO)
- World Meteorological Organization (WMO) –
- International Transportation Safety Association (ITSA) – <http://www.itsasafety.org/>

The National Oceanic and Atmospheric Administration (NOAA) of the United States also has much extra-territorial influence.

## 6 Organisations Representing Sectors of the Shipping Industry

- American Petroleum Institute (API)
- Association of Average Adjusters
- Baltic Exchange
- Central Union of Marine Underwriters Norway (CEFOR) – <http://www.cefor.no/>
- Chemical Distribution Institute – <http://www.cdi.org.uk/>
- Comite Maritime International (CMI)
- Federation of Oils, Seeds and Fats Association (FOSFA)
- Federation of National Associations of Ship Brokers and Agents (FONASBA)
- GDV Cargo Information Service – [http://www.tis-gdv.de/tis\\_e/inhalt.html](http://www.tis-gdv.de/tis_e/inhalt.html)
- Grain and Feed Trade Association (GAFTA)
- Hazardous Materials Advisory Council – <http://www.hmac.org/>
- Honourable Company of Master Mariners – <http://www.hcmm.org.uk/>
- ICC International Maritime Bureau (IMB)
- International Cargo Handling Co-ordination Association (ICHCA)
- Institute of Chartered Shipbrokers
- International Association of Oil and Gas Producer (OGP)
- International Chamber of Commerce (ICC)
- International Federation of Freight Forwarders Associations (FIATA)
- International Group of P&I Clubs
- International Maritime Mobile Satellite Organisation (INMARSAT)
- International Ship Suppliers' Association (ISSA)
- International Underwriting Association of London
- International Union of Marine Insurance (IUMI)

## 7 International Pollution Organisations

Contact details for many relevant organisations can be accessed via the website of the International Tanker Owners' Pollution Federation Limited (ITOPF) (Useful Links)

- Advisory Committee on Protection of the Sea (ACOPS) – <http://www.acops.org/>
- Aquatic Nuisance Species Task Force – <http://anstaskforce.gov/>
- Center of Documentation, Research and Experimentation on Accidental Water Pollution (CEDRE) – <http://www.ifremer.fr/cedre/>
- Chemical Distribution Institute – <http://www.cdi.org.uk/>
- International Marine Environment Protection Association (INTERMEPA)
- European Environment Agency – [http://www.eea.eu.int/main\\_html](http://www.eea.eu.int/main_html)
- International Oil Pollution Compensation Funds (IOPC Funds) – <http://www.iopcfund.org/>
- International Petroleum Industry Environmental Conservation Association – <http://www.ipieca.org/>

## 8 Health and Social Welfare Organisations

- EU Personal Injuries Assessment Board
- International Association of Shipmasters' Federations (IFSMA)
- International Committee on Seafarers' Welfare (ICSW)
- International Federation of Shipmasters' Associations (IIFSMA)
- International Maritime Employers' Council (IMEC) – <http://www.marisec.org/IMEC/index.htm>
- International Radio Medical Centre (CIRM)
- International Shipping Federation
- International Transport Workers Federation (ITF)
- Maritime Rescue Co-ordination Centre (MRCC)
- Seafarers' International Research Centre – <http://www.sirc.cf.ac.uk/index.html>
- World Health Organisation (WHO)

## 9 Professional Bodies

### a Arbitration and Conciliation Bodies

- Centre for Effective Dispute Resolution (CEDR)
- London Maritime Arbitrators Association (LMAA) – <http://www.lmaa.org.uk/>
- Maritime Arbitrators Association of the United States (MAA)
- Maritime Solicitors Mediation Services (MSMS)
- Singapore Chamber of Maritime Arbitration (SCMA)
- Singapore International Arbitration Centre (SIAC)
- Society of Maritime Arbitrators (SMA) – <http://www.smany.org/>

### b Salvage Organisations

- International Salvage Union (ISU) – <http://www.marine-salvage.com/>
- Lloyd's Salvage Arbitration Branch – <http://www.lloyds.com/the-market/tools-and-resources/lloyds-agency-department/salvage-arbitration-branch>
- The Salvage Association

### c Technical Organisations

- Association of Certified Marine Surveyors – <http://www.acms-usa.com/>
- Institute of Marine Engineering, Science and Technology – <http://www.imarest.org/>
- International Institute of Marine Surveying – <http://www.iims.org.uk/>
- National Association of Marine Surveyors – <http://www.nams-cms.org/>
- Society of Accredited Marine Surveyors – <http://www.marinesurvey.org/>
- Society of Consulting Marine Engineers and Ship Surveyors – <http://www.scmsHQ.org>
- Society of Naval Architects and Marine Engineers – <http://www.sname.org/>

### d Security Associations

- Maritime Liaison Office (MARLO) – <http://www.cusnc.navy.mil/marlo/>
- Maritime Security Centre – Horn of Africa (MSCHOA) – <http://www.mschoa.org/Pages/About.aspx>
- NATO Shipping Centre (NSC) – <http://www.shipping.nato.int/Pages/default.aspx>

## **B Written Material**

### **1 Legal Text-books**

**Admiralty Jurisdiction and Practice** by Meeson and Kimball, 4th ed., 2011, Informa  
**A New convention for the Carriage of Goods by Sea – The Rotterdam Rules** by Thomas and others, 2009, Lawtext Publishing

**Arnould's Law of Marine Insurance and Average (Volumes 1-3)** by Gilman, 17th ed., 2010, Thomson Reuters

**Bareboat Charters** by Davis, 2nd ed., 2005, LLP

**Bills of Lading** by Aikens, Lord and Bools, 2006, Informa

**Brice: The Maritime Law of Salvage** by Reeder, 5th ed., 2012, Sweet & Maxwell

**Check Before Fixing** by BIMCO Informatique A/S

**Chitty on Contracts**, 31st ed., 2012, Sweet & Maxwell

**Clerk & Lindsell on Torts**, 20th ed., 2010, Sweet & Maxwell

**Dictionary of Shipping Terms** by Brodie, 5th ed., 2007, Informa

**International Cargo Insurance** by Dunt, 2012, Informa

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**P&I Club Law and Practice** by Hazelwood and Semark 4th ed., 2010, Informa

**Port State Control** by Oezcayir, 2nd ed., 2004, LLP

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**Scrutton on Charterparties** by Eder, Bennet, Berry, Foxtton and Smith, 22nd ed., 2011, Sweet & Maxwell

**Shipbroking and Chartering Practice** by Gorton, 7th ed., 2009, Informa

**Shipping and the Environment** by de la Rue and Anderson, 2nd ed., 2009, Informa

**The Carriage of Goods by Sea** by Wilson, 7th ed., 2010, Pearson Longman

**The Law of Shipbuilding Contracts** by Curtis, 4th ed., 2012, Informa

**The Law of Tug and Tow and Offshore Contracts** by Rainey, 3rd ed., 2011, Informa

**The Law of Shipbuilding Contracts** by Curtis, 4th ed., 2012, Informa

**The Maritime Labour Convention 2006** by Mc Connell, Devlin and Doumbia-Henry, 2011. Martinus Nijhoff Publishers

**Time Charters** by Coghlin, Baker, Kenny and Kimball, 6th ed., 2008, Informa

**Voyage Charters** by Cooke, Young, Taylor, Kimball, Martowski and Lambert, 3rd ed., 2007, Informa

**War, Terror and Carriage by Sea** by Michel, 2004, LLP

## 2 Technical textbooks

It is not possible in this publication to provide an up-to-date list of the very many technical books that deal both with general and specific shipping issues. However, details of publications that may be available from time to time can be found at the following websites:

**The Nautical Institute Publications List and Services:**

[www.nautinst.org/download.cfm?docid=14E77439-4B0A-410B](http://www.nautinst.org/download.cfm?docid=14E77439-4B0A-410B)

**Ship Knowledge series:** [www.dokmar.com](http://www.dokmar.com)

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**Brown, Son and Ferguson Ltd:** [www.skipper.co.uk/](http://www.skipper.co.uk/)

**Institute of Marine Engineering, Science & Technology (IMAREST):**

<http://www.imarest.org/>

**The Institute of Chartered Shipbrokers:** [www.mandibooks.com](http://www.mandibooks.com)

**Kelvin Hughes:** [www.bookharbour.com](http://www.bookharbour.com)

**Witherby:** [www.witherbyseamanship.com](http://www.witherbyseamanship.com)



### 3 Periodic information sources

Please note that in some instances access requires ID and password

**BIMCO** – <https://www.bimco.org/>

**BIMCO Bulletin**: [https://www.bimco.org/en/Products/BIMCO\\_Bulletins.aspx](https://www.bimco.org/en/Products/BIMCO_Bulletins.aspx)

**Bunkerworld** – <http://www.bunkerworld.com/>

**CEFOR** – <http://www.cefor.no/>

**Containerisation International**: [www.ci-online.co.uk](http://www.ci-online.co.uk)

**Digital Ship**: [www.thedigitalship.com](http://www.thedigitalship.com)

**DNVPS** – <http://www.dnvps.com/services/home.htm>

**Fairplay/AIS live** – <http://www.aislive.com/>

**Fleetview online** – <http://www.fleetviewonline.com/services/Content/tracking/Default.aspx> (requires user ID and password)

**FOSFA international** – <http://www.fosfa.org/>

**Gard News**: [www.gard.no/ikbViewer/page/news-and-publications](http://www.gard.no/ikbViewer/page/news-and-publications)

**IMO Vega** – <https://vp.imo.org/Login.aspx?ReturnUrl=%2f>

**Insurance Day** – <https://www.insuranceday.com/>

**Intercargo** – <http://www.intercargo.org/>

**Intertanko** – <http://www.intertanko.com/>

**ISU – LOF** – <http://www.lof-at-isu.com/secure/index.asp>

**Lloyd's Informa i-law portal** – <http://www.i-law.com/ilaw/index.htm;jsessionid=FB0368601344A3DE86C007882CFEB429.wa2>

**Lloyd's List** – <http://www.lloydslist.com/ll/>

**Seatrade**: [www.seatrade-global.com](http://www.seatrade-global.com)

**Sea-Web** – [http://www.sea-web.com/seaweb\\_welcome.aspx](http://www.sea-web.com/seaweb_welcome.aspx)

**Seasearcher** – <http://www.lloydslistintelligence.com/llint/index.htm;jsessionid=A21ED2D3FB646A81C15A72C9FD6F1152>

**Ship2Yard** – <http://www.ship2yard.com/>

**Tradewinds** – <http://www.tradewindsnews.com/>

**Upstream** – <http://www.upstreamonline.com/>

**World Cargo News**: <http://www.worldcargonews.com/>



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