Commodities

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UNREST IN EGYPT, LIBYA AND THE MIDDLE EAST

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The recent civil unrest and unexpected political changes in Tunisia and Egypt have now spread to Libya and are being felt in Bahrain, Yemen and other countries in the Middle East. Libya is the first major oil exporter to be affected, and has seen the most violent repression of public protests. The situation there is changing rapidly and the outcome remains uncertain.

Markets and investors, who had largely observed events in Tunisia and Egypt with interest, have shown real concern at the unrest in Libya. Whilst the quantities of oil produced by Libya - around 1.6 million barrels of oil per day - are not sufficient to create a supply shortage, the fear is that the unrest might spread to other countries in the Middle East, with a knock on effect on oil prices. If oil price rises are sufficiently steep, the effects on the global economy will be felt through rising fuel, transportation, construction and food costs, with a dampening effect on the long awaited global economic recovery.

For commodities traders doing business in Egypt or Libya, there are already a number of immediate practical difficulties to be faced, in particular relating to payment and delivery. In this article, we consider some of these difficulties and the legal issues which may arise from them. Many of these may be relevant in relation to other Middle Eastern countries experiencing unrest.

Disruption to the banking system

Trade with Egyptian and Libyan companies has been affected by concerns about receiving and making payment as the Egyptian and Libyan banking networks have been disrupted by the unrest. This presents difficulties for unpaid suppliers and shippers, particularly where the goods are already en route to their destination, and for buyers required to make prompt payments under their contracts.

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Sellers

Payment under letters of credit is proving particularly problematic. If the issuing/opening bank is in Egypt or Libya, sellers may not be able to present documents or obtain payment. In these circumstances, banks are likely to rely on the force majeure provision at Article 36 of the UCP 600, which states that banks assume no responsibility for the consequences of any interruption to their business services as a result of riots, civil commotion or any other cause beyond their control. Even after business resumes, banks will not honour or negotiate credits which have expired whilst their services have been interrupted. In these circumstances, if there is an advising bank outside Egypt and the seller presents documents to that bank on time, the issuing/opening bank will be obliged to honour the credit once the force majeure event has terminated.

If there is a confirming or negotiating bank outside Egypt or Libya, the seller should be able to obtain payment by presenting the documents to this bank. If the confirming or negotiating bank is in Egypt/Libya and the issuing/opening bank is outside, the seller may have the practical problem of not being able to present the documents. If possible, he can present them directly to the issuing/opening bank.

Buyers

Disruption to the banking system is also causing problems for those making payments where the timing of those payments is expressed to be of the essence of the contract. Force majeure clauses are unlikely to assist a buyer who fails to make payment in time. Unless the contract requires that payment is made from an Egyptian or Libyan bank, the buyer will be obliged to make suitable alternative arrangements for payment through a different bank.

Disruption and delays at ports

We understand that the port of Tripoli and many other ports in Libya are currently closed for all practical purposes. At the time of writing, it appears that the unrest and demonstrations are largely taking place away from the ports. However, it appears that no cargo operations are taking place. Sporadic delays at Egyptian ports are likely to continue until political stability returns.

Traders who have chartered ships to load at an affected export terminal may incur significant demurrage liabilities or even cancellations if the laycan period passes without loading. Even if their charterparty includes a force majeure clause, it may not interrupt the running of laytime or demurrage unless it uses clear words to that effect, both in the force majeure clause and in other clauses, such as laytime and non-weather working day clauses. In addition, the interruption of laytime or demurrage will only last whilst the specific force majeure circumstances apply.

Deviation

As was the case in relation to the unrest in Egypt, some major operators are now refusing to call at Libyan ports in an attempt to avoid the disruption, whilst others have re-routed services to avoid Egypt and Libya and/or have closed local offices. Where cargo is re-routed, shipping companies may decide to pass on any additional terminal handling charges, transshipment and freight costs to customers.

In the event of a deviation, parties will need to look carefully at the particular terms of the “liberty to deviate” clause in their contracts, as well as the applicable terms on war, riot and insurrection, to see whether they apply, especially in relation to calls at Egyptian ports, where the unrest is not countrywide and the UK’s Joint War Committee has adopted a very measured response. Deviation by a vessel must be a genuine attempt to deal with a danger, emergency or its consequences and must be exercised in good faith, not arbitrarily, capriciously or unreasonably.

War risks

Traders chartering vessels to Libya should check the terms of the war risk clause in their charterparties. The VOYWAR 2004 and CONWARTIME 2004 definition of “war risks” includes rebellion and civil commotion, and owners may legitimately refuse to follow charterers’ orders to proceed to a port where the vessel may be exposed to war risks if in the reasonable judgment of the master/owners there is or may be a danger to the vessel, cargo, crew or other persons on the vessel. Where charterers have the option to nominate a port within a range of ports, owners may in certain circumstances be entitled to discharge the cargo at any safe port of their choice, if charterers fail to nominate an alternative safe port. The additional costs or losses incurred by owners as a result of following charterers’ orders may also be recoverable under an express or implied indemnity or by way of damages.

Force majeure

Traders encountering difficulties in fulfilling a contract because of the unrest in Egypt and/or Libya should check whether their contracts contain a force majeure provision. Where a contract includes a force majeure provision, the parties may be freed from their obligations in extraordinary events or circumstances beyond their control. If there is no force majeure provision, English law will not imply one for the benefit of the affected party. In those circumstances, a party unable to perform its contractual obligations may be able to rely on the legal doctrine of frustration (see below).

If the contract does contain a force majeure clause, it is necessary to consider whether it covers the particular circumstances that are actually preventing performance. As force majeure clauses are exclusion clauses, they are interpreted strictly: A party seeking to rely on a force majeure clause will have to show that the circumstances on which they rely fall squarely within the circumstances identified in it. If the clause is ambiguous, the ambiguity will be resolved against the party seeking to rely on it.

It may be difficult to identify clearly the particular circumstances giving rise to difficulties in each case, since these may change as events develop. For example, they may include difficulties in production, transport problems, shortage of workforce, or state-imposed curfew. Whether any of these circumstances falls within the scope of a force majeure provision will depend on its specific terms.

Frustration

A contract may be discharged by frustration where an extraneous event occurs after the contract is agreed which is not caused by the fault of one of the parties and is not catered for in the contract (by a force majeure clause or otherwise), and where the event so fundamentally changes the nature (not merely the cost) of performing the contract that it would be unjust to require continued performance.

Frustration rarely occurs. A contract will only be discharged by frustration when it has become radically different or impossible to perform. For example, a contract for the sale of grain to an Egyptian buyer is unlikely to be frustrated just because transport or finance problems have made performance significantly more difficult or expensive. A closure of the Suez Canal might make a contract more difficult or expensive to perform, but it is very unlikely to be a frustrating event.

Insurance

Whilst cargo underwriters will have concerns about potential loss, damage or deterioration to goods transiting on land and stored in warehouses, it seems that - for the moment at least - the risk of damage by rioting is limited and the current situation is unlikely to have a major impact for cargo insurance. However, traders will need to ensure that their insurance is sufficient to cover the kind of risks likely to be encountered in Egypt and Libya, and for a sufficient period of time to allow for any delays.

Carriers are likely to seek to pass on any additional war risk insurance costs by way of surcharges, and some charterparties may allow owners to recover these costs from charterers.

Markets

Civil unrest in the Middle East has been good for commodities futures brokers: precious metals and crude oil futures have surged as unrest has spread from Tunisia to Egypt, Bahrain, Libya and Yemen. In times of uncertainty, concerns about unrest and economic instability drive investors to the perceived safety of bullion and other precious metals. However, it is rare for this trend to lead to a massive physical demand for the metals, as the rally in prices is too quick for any physical demand to take place.

Conversely, the prices of base metals are down amidst uncertainty over what will happen next after the latest protests in Libya and in Bahrain - an immediate neighbour of Saudi Arabia. If anything were to happen in Saudi Arabia, oil prices would be almost certain to rocket and hit both the burgeoning global recovery and demand for base metals.

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