HFW

DECEMBER 2020

COA PACK

By HFW in association with Barristers from

ESSEX COURT CHAMBERS
BARRISTERS

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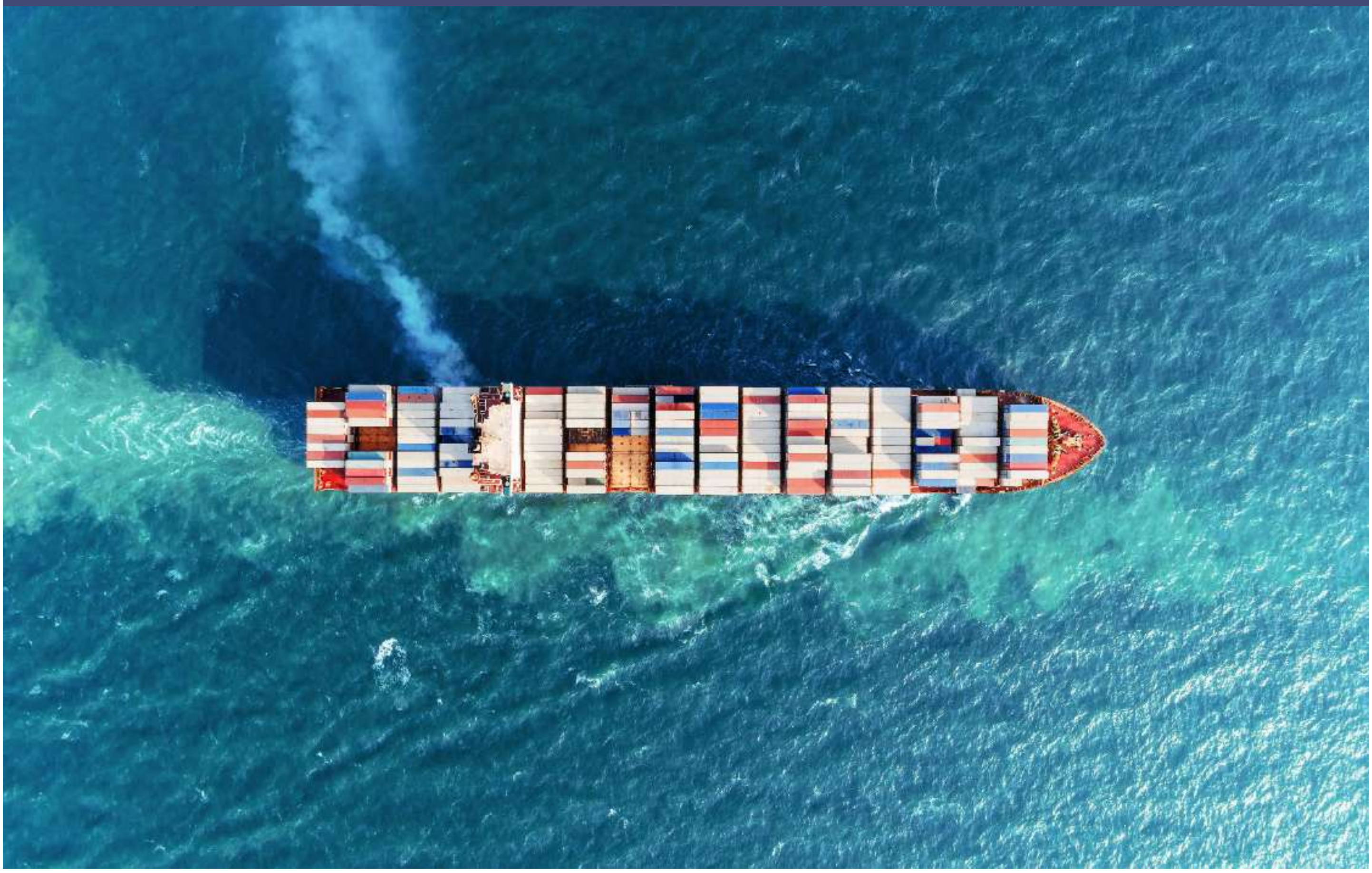
INTRODUCTION



1. INTRODUCTION

Dear Reader

Welcome to the first edition of our "COA Pack".

Surprisingly, notwithstanding their importance, a certain “legal mystery” surrounds Contracts of Affreightment (or "COAs" as they will be referred to in this Pack).

The primary purpose of this pack is therefore to shine a light on these important maritime contracts and bring to your attention some features of real importance.

The last freight crash saw several COA disputes erupt and, in due course, be resolved. We were involved in a number of them. This COA pack, where possible, is informed by these previous experiences.

Any discussion of COAs would be incomplete without looking to the future and in our final section, we address some matters that should be considered when fixing COAs. These are intended to be food for thought. Cyber risk allocation, protection against insolvency, environmental and human considerations are all included and where possible, these should be the subject of express clauses leaving less room to chance or implication.

We hope you find our collective thoughts helpful.

02

RIGHTS AND OBLIGATIONS

2. RIGHTS AND OBLIGATIONS

The rights and obligations of an owner and a charterer in a COA are on one level similar to those in a standard voyage charterparty. The owner will earn and the charterer will pay freight and the owner will carry the charterer's cargo from one destination to another.

There are however certain subtle differences which we consider in this section and further in this Pack.

a. A COA is for more than one voyage

   Although there is no strict, technical definition, a COA is generally a contract for the carriage of cargo by sea, in which the parties agree for the performance of more than one voyage – for example, a COA for 4 voyages from Brazil to China over 1 year. The benefit of this is that the owner can lock in 4 voyages to one contract and control its schedule / income accordingly; and the charterer has the certainty of knowing that it will have a carrying vessel, and may also (depending on the contract) get a measure of certainty over the costs of carriage.

   The multiplicity of voyages is usually reflected in the form of a COA. Most COAs comprise a “framework” agreement, containing terms which are intended to apply to all voyages, and a series of individual charters which relate to the individual voyages. Although there are standard forms of “framework” COA in use – notably BIMCO’s GENCOA, VOLCOA and INTERCOA 80 forms – parties just as often draft bespoke agreements. The terms of, and level of detail in, a framework COA can vary greatly.

b. Voyages usually have an agreed "spread"

   Whether this is by reference to a fixed schedule or to terms such as "evenly spread" or "fairly evenly spread" ("ES" and "FES" discussed further in this Pack), the gaps between the voyages are also usually agreed. This is partly so that the parties can anticipate when they will be required to perform their respective obligations (to provide a vessel / load cargo), though nomination and notice provisions also help with this. But it is also about trying to ensure that each party’s obligation to perform comes at a time that is reasonably convenient: other things being equal, regular and evenly spaced obligations are generally easier to meet than irregular highs and lows of demand, at least for an owner and sometimes also for a charterer.

c. The freight is often not fixed

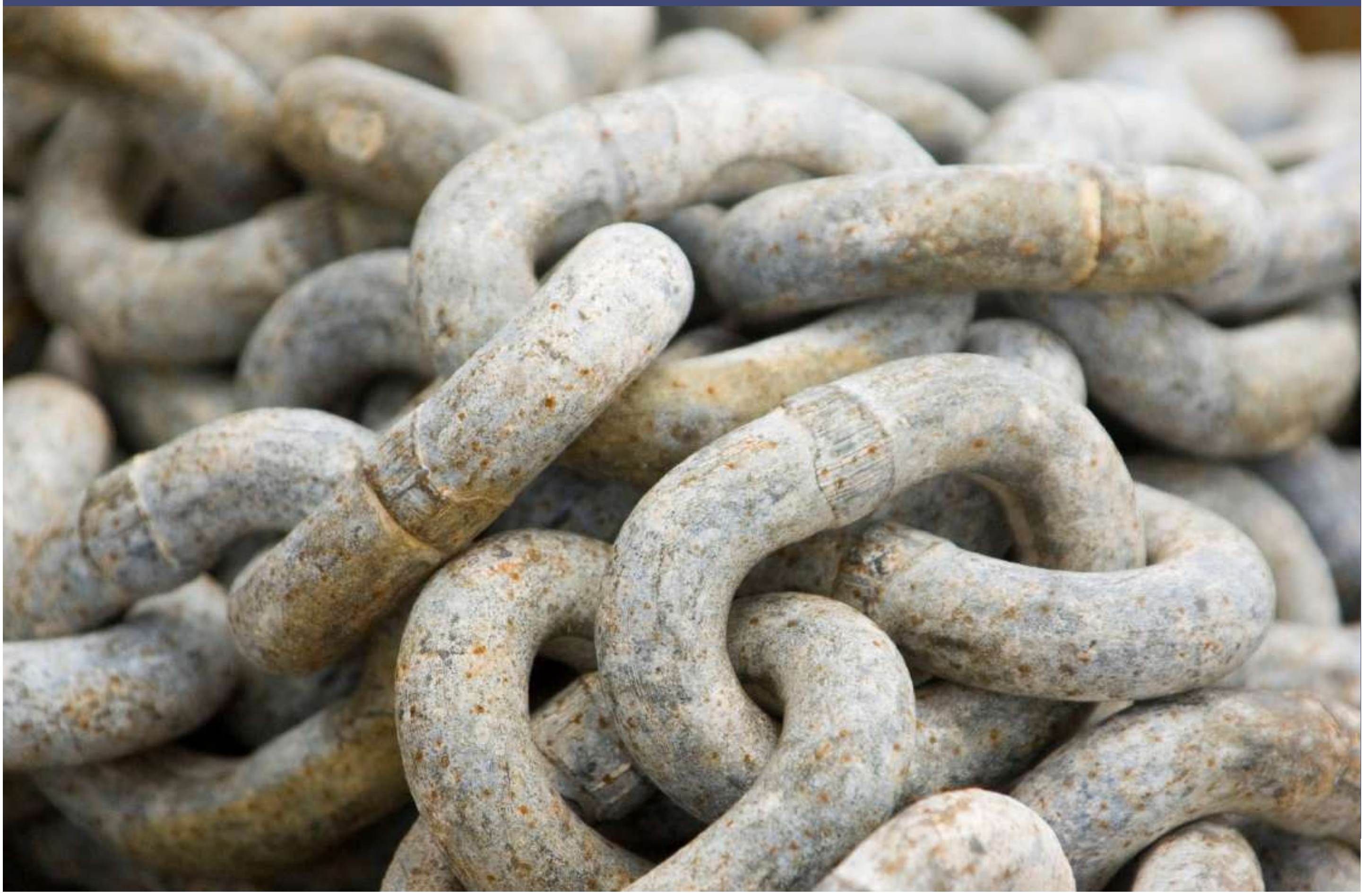
   Unlike standard, one-voyage charterparties, COAs often do not have fixed freight rates. This is because, especially in long-term COAs, it is difficult to know what the market rate will be like at the time of the voyage; and both owners and charters generally prefer that the individual voyages should be undertaken at around market price, rather than to set a fixed price. We consider some of the potential issues that this gives rise to later in the Pack.

d. The dispute resolution clauses are more complex

   As there are multiple voyages, the parties would not normally want minor issues arising under one voyage (e.g. a small demurrage dispute) to affect the remainder of their long-term COA. Therefore the dispute resolution clauses are often drafted in a way to ensure that the COA can (and should) continue without disruption.

03

NOMINATION AND MEANING OF "ES" AND "FES"



3. NOMINATION AND MEANING OF "ES" AND "FES"

(1) Introduction

Under a COA, the owner and the charterer have agreed to a certain number of voyages to be performed across a certain period of time. But what also needs to be defined in the COA is the spread across that period of time. A charterer will often want maximum flexibility so that they can utilise the voyages in accordance with their often changing and price-sensitive trading schedules. Conversely, an owner will want dates that are fixed as much as possible, so that they can schedule their vessels.

The parties may well decide to have a fixed schedule within the COA. For example, in the case of a 4 voyage COA which is to last 4 months, you could expressly state that a voyage is to be performed in the first week of each month.

Another alternative is to use terms such as "*evenly spread*" or "*fairly evenly spread*" to define how the voyages need to be performed across the time period of the COA. These two terms can cause perhaps the most contentious issues which are specific to COAs.

(2) "*Evenly Spread*" and "*Fairly Evenly Spread*"

So what do these terms actually mean? Although there are few authorities under English law, those that have discussed the terms "*evenly spread*" and "*fairly evenly spread*" provide some useful guidance.

In an unreported London arbitration, in which HFW acted for owners, the arbitrators provided some guidance on the definitions of these terms as follows (our emphasis):

> *"Contracts of this kind (i.e. for the shipment of quantities of a particular commodity over a particular period) contain varying provisions specifying when shipments are to take place. At one extreme, a contract might spell out precise dates. At the other, there might be an extremely loose arrangement.* ***In between lie contracts that require shipments to be "fairly evenly spread", "evenly spread", or which provide for a particular quantity within particular periods at the charterers' option,*** *or one shipment per quarter, etc…* ***"fairly evenly spread" is more favourable to a charterer than a requirement to ship a particular quantity within a year; and "evenly spread"… is more or less the same as having a fixed schedule."***
>
> *"… we have no hesitation in saying that* ***"evenly spread" means precisely what it appears to say,*** *and that subject to de minimis exceptions,* ***there is no justification for allowing any margin"***[1].

The focus of the findings in the award was a consideration of the even "spread" between shipments.

It seems, therefore, that "*evenly spread*" means simple and exact mathematical division, without a margin. What about the term "*fairly evenly spread*"? The natural and obvious meaning of the word "*fairly*" would be as a qualification, to import some margin of tolerance around the dates that would otherwise be produced by an exact mathematical division. Consistent with that, in another arbitration in which HFW acted and where the term "*fairly evenly spread*" was under consideration, it was argued that this meant a 10% margin of tolerance. The arbitration settled before an award was issued, so the point was not adjudicated.

[1] Confidentiality beyond this quote is fully maintained.

The words "*fairly evenly spread*" received some very limited consideration in *Aquavita v Ashapura*,[2] a decision of the English High Court. The case concerned a COA under which the charterer was obliged to ship 250k MT (+/- charterers' option) in 40k MT shipments between November 2011 and March 2012 "*fairly evenly spread*". Mr Justice Burton held that the meaning of these words was "*fairly clear*", and simply divided the number of days available (151 days) by the number of shipments (6), holding as follows (our emphasis):

> *"The contractual provision in relation to those six laycans was that the shipments be 'fairly evenly spread'. Although [counsel] has not been able to find any legal or other authority as to the meaning of those words, they would appear to me to be fairly clear, and in any event, I have had the benefit of Mr Goodall's evidence, which is that he has come across these words very often in COAs and other similar contracts of affreightment; and that it is a standard and perfectly well understood term in the trade, which means that* ***there must be regularity where there is provision for "fairly evenly spread" over a defined period****, so as to avoid the imposing of prejudice on the shipping party by reference to freight risks, if all of the shipments are clustered towards the end of the period; and that his understanding of the practice,* ***which I accept, is that what it in fact means is that the total amount of the shipments is split, and divided by the number of shipments and spread evenly over such a period. In this case, that would be every 25 days.***"[3]

Although the final sentence might be thought to imply that there was no difference between "*evenly spread*" and "*fairly evenly spread*", with both requiring a more-or-less exact mathematical division, on a fuller analysis the case does not support that reading. The meaning of the clause was not really in issue: it was common ground that the charterers had only loaded 132,000 MT out of the required 250,000 MT of the COA period, and it made little difference when precisely the remaining 118,000 MT should have been lifted. The charterer was unrepresented, so the case would have limited precedent value in any case. But, more importantly, Mr Justice Burton treated it as being common ground that (as stated in the charterer's witness statement) shipments had to be nominated "*roughly once every four weeks*." Quite what "*roughly*" meant did not have to be determined.

While this is to give the decision closer analysis than it can properly justify, it can be argued that as the difference between 25 days and 28 days (i.e. 4 weeks), "*roughly*" must have meant at least 3 days, and therefore something slightly more than 10%. *Aquavita v Ashapura* is ultimately, therefore, consistent with the unreported arbitration referred to above.

(3) Concluding comments

The limited authorities available therefore show that the charterer cannot cluster the shipments together in a short period of time where specific wording such as "*evenly spread*" or "*fairly evenly spread*" is used. "*Evenly spread*" is likely to be interpreted as requiring a strict mathematical division with little or no margin around the resulting dates. "*Fairly evenly spread*" does imply a margin of some sort, perhaps in the order of 10% though it is not possible to be definitive.

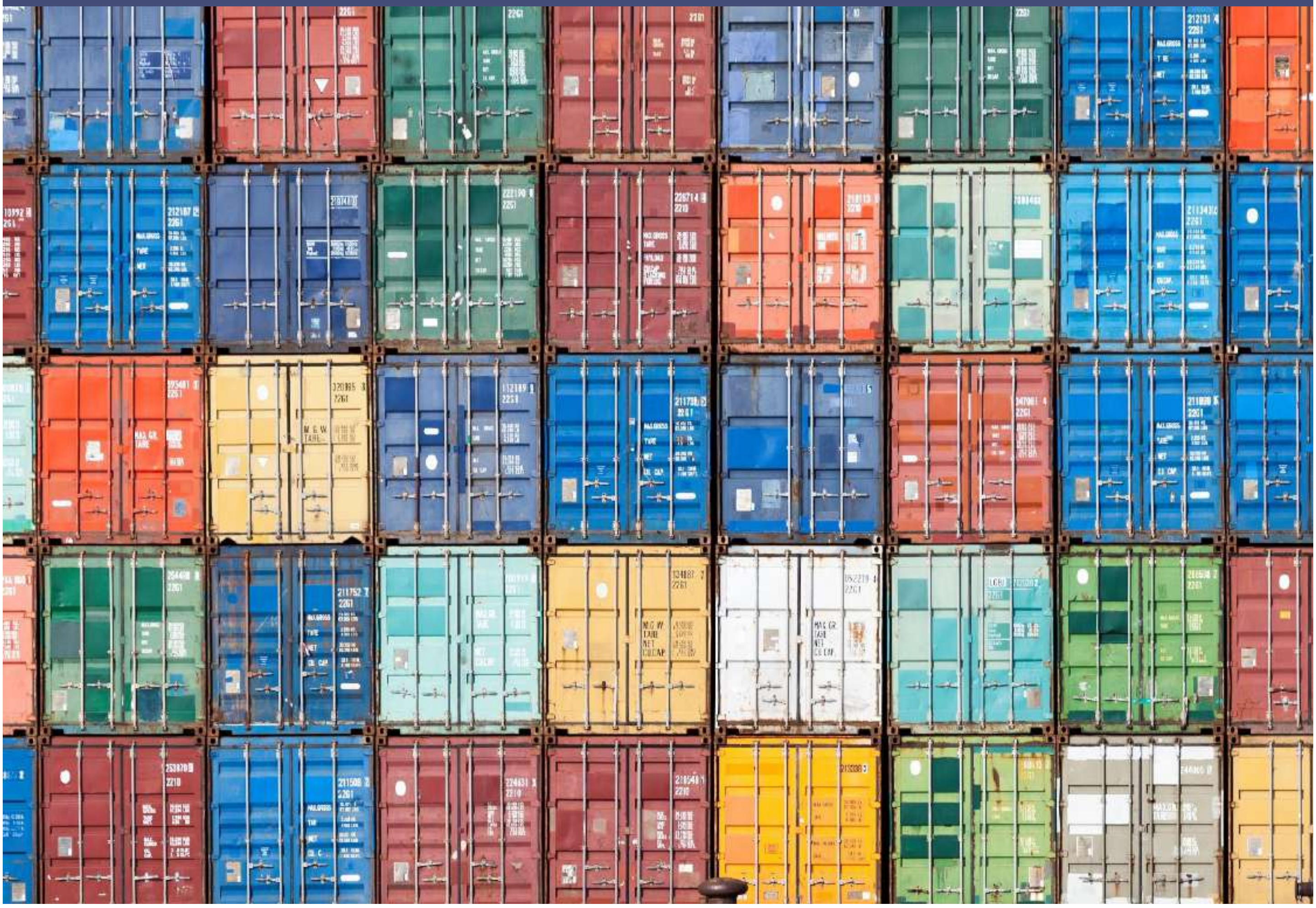
What is also clear from this analysis is that there is limited commentary on the topic. It is therefore much better to state expressly when the voyages are to be performed within your COA, and not to rely on these terms whose meaning has not yet (unlike many shipping law expressions) been pinned down by years of authority.

[2] *Aquavita International SA, Glendive Enterprises Limited v Ashapura Minechem Limited* [2015] EWHC 2807

[3] ibid., at [45].

04

INDEX LINKED FREIGHT



4. INDEX LINKED FREIGHT

(1) Introduction

As COAs are often long-term and fixed for multiple voyages which are to take place at some point in the future, it is common for the freight rates to be fixed based on an index rate (often plus / minus a certain percentage). The specific date of the index rate would then usually be fixed on a certain point of the voyage (e.g. first or last day of the laycan). The indices used are commonly from the Baltic Exchange.

A typical clause may therefore look like this: "*THE AVERAGE OF [INDEX] 6% (LESS SIX PERCENT) [X] DAYS PRIOR TO 1ST DAY OF LAYCAN FIOST BASIS [LOADPORT]*".

Fixing a price based on an index is common not only with COAs but in commodities trading, where, for example, metals are traded based on LME prices and certain soft commodities traded based on Chicago Board of Trade prices.

However, there are potential problems with fixing a price in this way.

(2) Changes in the index

COAs may be for a long period of time, and in those periods it is possible that the index to which they refer could cease to exist or undergo some fundamental change in nature. For example, there were calls this year for the Baltic Exchange to update their indices to take into account the impact of the new 2020 sulphur regulations.[4]

As a result, it is imperative that a COA contain clauses which account for this sort of scenario. Such a clause should state what is to happen in the event there is a change in the way an index is determined and/or if the index ceases to be published altogether.

Usually the parties opt for a resolution whereby the owner and charterer are to discuss in good faith to try and agree a solution. This however raises the problem that "agreements to agree" are not enforceable under English law. Therefore it is good practice to include a second tier in the dispute resolution clause which refers the matter to a particular forum where the issue can be resolved if the parties cannot agree it between themselves. This may be the overall dispute resolution clause in the COA (e.g. High Court or arbitration), or a specific dispute resolution clause to resolve any dispute with regards to changes in the index. This type of clause is considered in the following sub-section.

(3) Dispute resolution

Where a specific dispute resolution clause is included to resolve a dispute with regard to changes to an index, some COAs also call on various members of the index producers' management to be appointed to resolve the dispute – for example, the President of the Baltic Exchange. This is akin to an expert determination clause.

Although this can offer a sensible solution (where the named person is well qualified to determine this precise type of dispute), parties should bear in mind that naming someone in a COA in this way does not confer on that person an obligation to take on the role.

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[4] https://www.reuters.com/article/shipping-imo-balticexchange/baltic-exchange-keeps-shipping-indices-unchanged-ahead-of-imo-changes-idUSL8N21D56W

It is therefore advisable not to identify a specific individual or office-holder within the dispute resolution clause unless it has been agreed in advance with that person that they can be called upon in any dispute, with terms such as fees, conflicts and the determination process to be decided in advance.

For a comprehensive approach to what is admittedly a rare problem, the clause could specify a fall-back in the event that the primary named expert is unwilling or unable to act – for example, that the dispute would then be resolved by three experts, one to be appointed by each side and the third to be appointed between the experts.

(4) Interim payment, pending dispute resolution

If the parties are in a dispute about which index is to apply, the owner will still wish to be paid freight in the meantime. To address this, an interim payment clause can be included in the COA, whereby while the dispute is being resolved, the owner will be paid based on an expressly chosen index rate, with such payment to be adjusted based on the ultimate outcome of the dispute.

05

BUNKER ADJUSTMENT FACTOR (BAF) CLAUSES

5. BUNKER ADJUSTMENT FACTOR (BAF) CLAUSES

As stated in *CMA v European Commission*,[5] a Bunker Adjustment Factor (or "BAF" clause) is a clause which allows for a "*price adjustment made by a carrier to reflect the difference between the current cost of ship's fuel and a base level incorporated in the freight rate*."

A simple BAF clause may look like this:

"*Reference price: Platts Bunkerwire Mean Price at Japan of VLSFO 0.5%*
Basis Price: US$[ ]mt
Factor: [ ]/$/t (both ways i.e for bunker prices increase of decrease)

The Bunker Adjustment Factor to apply shall be [   ] for every dollar increase (payable to Owners) or decrease (payable to Charterers), calculated as the difference between the Bunker Price on the first day of loading and US$[ ] per metric ton. If the Bunker Price on the first day of loading is not available, then the nearest available previous day's Bunker Price to apply".

Similar to index-linked freight rates, long-term COAs can account for any dramatic changes in bunkers by including such BAF clauses. Bear in mind that these clauses are not solely for the benefit of owners – they can also benefit charterers.

[5] *CMA CGM and others v European Commission (Case T-213/00)* [2003] All ER (D) 277 at [31]

06

SAFE PORT OBLIGATIONS

6. SAFE PORT OBLIGATIONS

(1) Express safe port or berth warranties

It is open to parties to a COA to include an express warranty as to the safety of a port or berth. Such a warranty can be found in the terms of the COA framework agreement, or in the charter terms applicable to the individual shipments. Neither the GENCOA nor VOLCOA standard forms for COAs published by BIMCO contain an express warranty as to the safety of ports or berths, but INTERCOA 80 does, as do some bespoke forms. [6]

(2) Implied safe port or berth warranties?

Where a charterparty contains no express provision by which the charterer warrants the safety of a port or berth, it is possible for there to be an implied term to that effect. In the context of a time charter, it is not unusual for such a warranty to be implied, at least where the charterer has a choice from a range of unnamed ports (The "*Evaggelos Th*" [1971] 2 Lloyd's Rep. 200). The usual rules as to the implication of terms will apply – the term sought to be implied must be necessary, must be reasonable, and must not conflict with the express terms of the contract. This has the result that in the voyage charter context, a term is far less likely to be implied. Such a warranty is thought to be unnecessary, at least where there is a named port or ports, because the owner, having agreed to proceed to a named port, is taken to have considered and accepted the risks of doing so (*The "APJ Priti"* [1987] 2 Lloyd's Rep. 37). Where the charterparty provides for a range of ports, particularly if they are not named, it is more likely that a warranty will be implied. As Sir Anthony Clarke MR said in *The* "*Reborn*" [2009] 2 Lloyd's Rep 639, "*whether such a warranty will be implied will be influenced greatly by the degree of liberty which the charterers enjoy under the terms of the charter to choose the port or place where the ship is to load or discharge*".

What does that mean in the context of COAs where there is no express safe port or berth warranty? If the COA provides for carriage to or from named ports (even if there is a choice amongst those named ports) or a small and easily identifiable range, it is unlikely that any safe port warranty will be implied. But where the charterer has a good deal of choice, it is possible that there might be such an implied term in the COA, so that the charterer must nominate a safe port, and the nomination of an unsafe port is invalid.

Where in a COA there is no express or implied warranty of safety of the port, and no express warranty of the berth, it is most unlikely that a warranty of safety of the berth will be implied: see *The "Reborn*", above.

(3) The content of the safe port or berth obligation

Where there is an express or implied warranty in relation to the safety of the port, the berth(s) must also be safe. But the converse is not true: a charterer who warrants the safety of a berth within the port does not warrant the safety of the port as a whole.

What does "*safety*" mean in this context? The test is set out in *The* "*Eastern City*" [1958] 2 Lloyd's Rep 127 : "*…a port will not be safe unless, in the relevant period of 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*

[6] Some standard form voyage charter agreements contain safe port or berth warranties – the NORGRAIN form, for instance - but many, such as GENCON, do not.

cannot be avoided by good navigation and seamanship…". So if at the time of nomination, a port (or berth) has a particular characteristic making it unsafe, the warranty will be breached. That characteristic could be physical (e.g. ice, a hidden sandbank) but need not be: it could be a blockade, or the risk of detention by the authorities, or the risk of being fired on by fighter jets. But if what makes it unsafe is an "*abnormal occurrence*", the warranty will not be breached. In *The "Ocean Victory*" [2017] 1 WLR 1793, the Supreme Court suggested that an abnormal occurrence was "*…something rare and unexpected… [not] something which was normal for the particular port for the particular ship's visit at the particular time of year*".

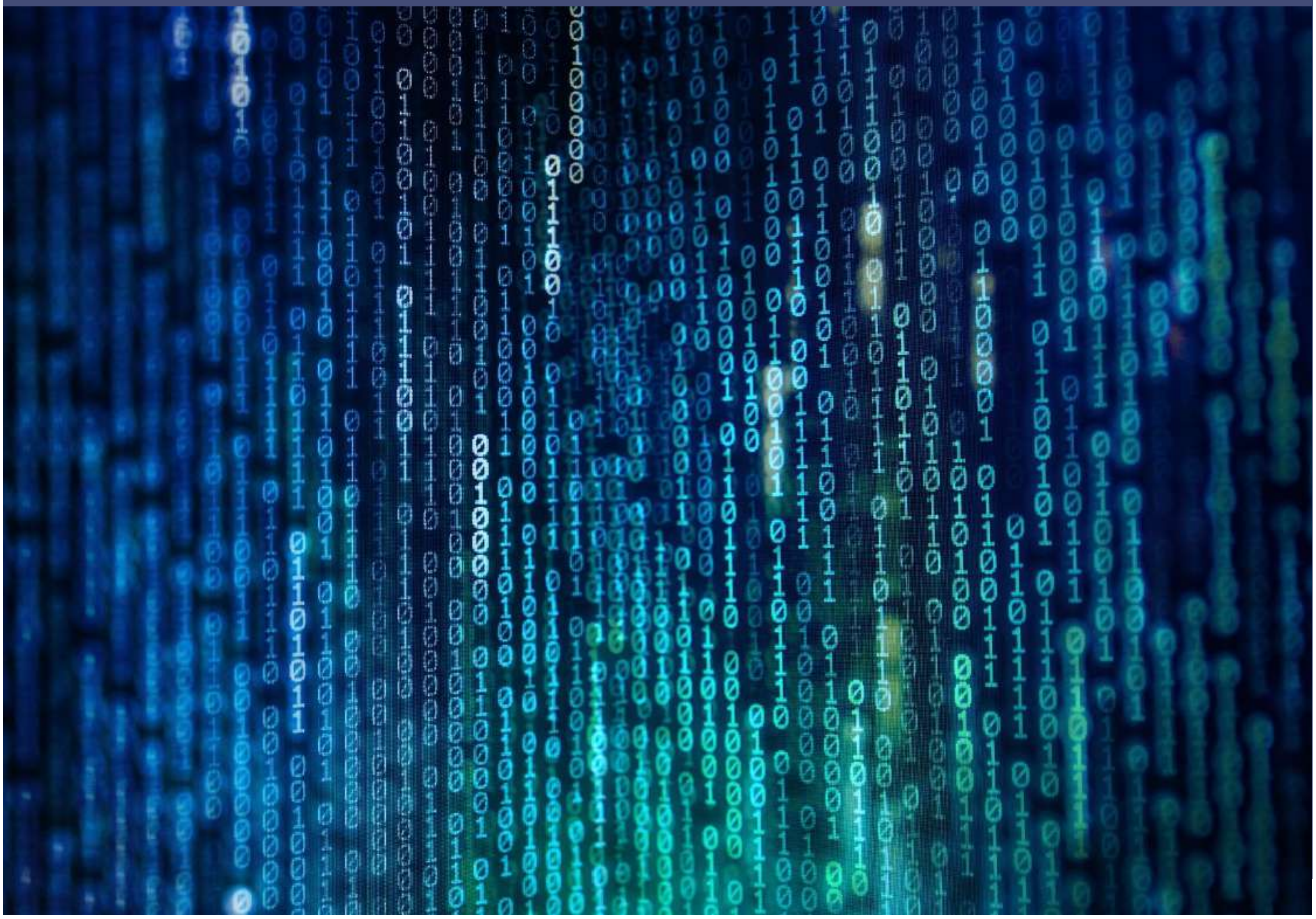
(4) Obligation to re-nominate?

A safe port warranty is strict, but it is prospective rather than continuing. The port must be safe at the time of nomination.

In time charters, if the port becomes unsafe whilst the vessel is *en route*, charterers come under a secondary obligation to cancel their order and order the vessel to a different, safe port: The "*Evia*" *(No. 2)* [1982] 2 Lloyd's Rep. 307. Does that obligation to re-nominate apply in the context of COAs? The position is not crystal clear, but the answer is probably "No". Once a port is nominated, it is treated as "written in" to a voyage charter, and it is generally thought that this prevents the obligation to re nominate from arising under a voyage charter. That is probably equally true in the case of a voyage charter concluded under the umbrella of a COA.

07

CYBER SECURITY



7. CYBER SECURITY

This is the subject of a separate HFW Cyber Pack. The evidence is that cyber attacks are continuing to increase, and are a particular concern in the maritime and trade industries. We recommend that cyber security ought to be considered in any substantial shipping contract, and COAs are no exception. We therefore touch briefly on this issue below.

Parties to a COA should consider making specific provision for what will happen if one or other (and particularly the owner) is affected by a cyber-attack.

A first challenge will be to define a "*Cyber Attack*". Here is a possible definition, focused on the position of an owner:

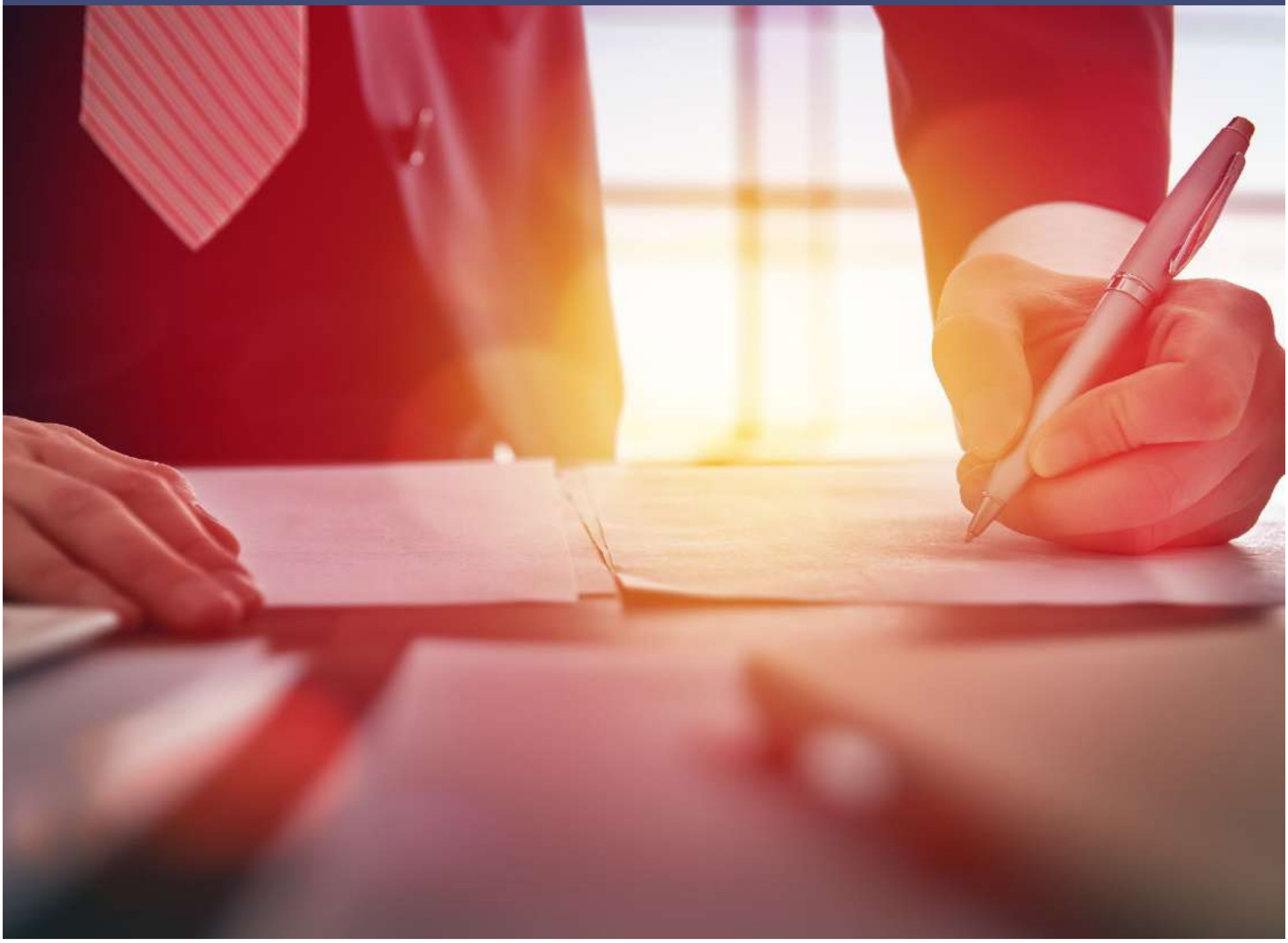
> *"Cyber Attack" means any act by a third party which affects the vessel's on-board computers, computer systems or computer software through or by the use of code, computer virus, process or any other electronic means whatsoever, without the consent of the owners.*

Thereafter, the parties should consider addressing the following key points:

- Laytime and demurrage: a "Cyber Attack" (as defined) can be included as an exception to laytime and demurrage.
- Payment: the charterer could include appropriate wording so that if its bank or other payment mechanisms suffer from a Cyber Attack, it is afforded more time to make payments under the COA.
- Seaworthiness: the charterer may wish to require that the owner takes "*prudent and reasonable measures to prevent and/or mitigate Cyber Attack(s) in relation to the vessel*".
- Safe port: an owner may wish to state expressly that a port will be unsafe (discussed further above) in the event that it has not taken "*prudent and reasonable measures to prevent and/or mitigate Cyber Attack(s)*".

08

FORCE MAJEURE



8. FORCE MAJEURE

(1) Introduction: types of clause

Given the long-term relationship embodied in a COA, issues as to one or other party's ability to perform their obligations as a result of external events will often arise. So it is unsurprising that many parties will seek to protect themselves by the insertion of suitable language into their COA.

The expression "force majeure" (literally: "superior force") is often used loosely to describe contractual clauses that address events arising through neither party's fault that prevent or hinder performance. In fact, the nature and effect of those clauses varies.

Some clauses operate as "contractual frustration" clauses: they provide that if a particular event occurs, the parties are automatically discharged from further performance under the contract.

Others provide for the suspension of performance by one or both parties during the period of the relevant external event, but do not bring the contract to an end. Sometimes that suspension is coupled with a right afforded to one party, or to both parties, to cancel the contract if the suspension continues for an identified period. That mechanism is familiar from shipbuilding contracts, but appears in COAs too.

More general exceptions clauses are also sometimes described as force majeure clauses: they relieve one or other party from liability where it is unable to perform because of some external circumstance. A good example of such a clause in a COA is afforded by the recent decision of the Court of Appeal in *Classic Maritime Inc. v. Limbungan Makmur Sdn Bhd* [2019] EWCA Civ 1102.

(2) Labels, and the approach to construction

In *Classic Maritime*, Limbungan, the charterers, tried to rely on a wide-ranging exceptions clause in a COA to excuse their failure to provide cargoes for shipment. They sought to label the clause a "force majeure" clause and contended that particular consequences – more fully discussed below – followed from that labelling. The Court of Appeal disagreed, holding that the manner in which a particular clause operates is a question of construction in every case.

It follows that describing a clause as a "force majeure" clause (as opposed to an exemption clause, or an exceptions clause, or something else) is not especially helpful. How the particular clause works depends not on the label given to it, but on the words used, read in the context of the COA as a whole.

(3) Getting within the clause

Where one party wishes to rely on an external event as excusing it from performance (or suspending performance, or to entitle it to cancel a COA) it must show that the event relied on falls squarely within the terms of the relevant clause, and that it does in fact prevent performance. Thus, and whilst all depends on what the clause actually says, usually it will be necessary to show that the strike, or embargo, or pandemic, or whatever it is, does prevent performance altogether. In particular, if the non-performing party could have taken reasonable steps to avoid or mitigate the force majeure event, but did not do so, it will normally not be entitled to rely on the clause: see *Channel Island Ferries Ltd. v. Sealink UK Ltd*. [1988] 1 Lloyd's Rep. 323.

Many COA clauses identify a list of specific events that can be relied on as force majeure. GENCOA is an example: clause 15, entitled "I*nterruption of Performance*", sets out a list of exceptions which will excuse the parties from liability for a failure to perform. But others are far more general. Clause 19.1 of the VOLCOA form, for example, provides that:

"*If the performance of this contract or part of it is interrupted through any event whatsoever which cannot be avoided or guarded against by either party, the performance affected shall be suspended until the hindrance ceases to have effect. Quantities not carried by reason of such an interruption of performance cannot be demanded to be shipped nor to be carried afterwards*."

This broad wording potentially gives both charterers and owners the right to rely on a very wide – indeed, unlimited – range of events, but subject always to the caveat that the event could not have been avoided by either party. The effect of the *Channel Island Ferries* decision, however, is that that limit would probably have been implied into the clause even if it were not express.

(4) But-for causation issues

The particular issue in *Classic Maritime* was whether Limbungan had to show that their inability to provide cargoes was in fact caused by the extraneous event relied on, in the sense that they would have been able to perform but for that event. A dam burst had resulted in the closure at one of the iron ore mines from which they sourced product. This was, on any view, an "*accident at the mine*" – one of the events identified in the exceptions clause in the COA. However, the Court found that even if the dam burst had not occurred, Limbungan would not have been able to supply cargoes.

The Court of Appeal held that on its proper construction, the exceptions clause in the COA did require Limbungan to show that it would have been able to perform, were it not for the excepted event (the dam burst). Since it could not do so, it was unable to rely on the exceptions clause and was liable in damages to the shipowners.

This does not mean that *all* "force majeure" clauses operate in this way. As the Court of Appeal made clear, it depends on the clause. There will be other clauses where it is enough for the party seeking to rely on the clause to show that the event has occurred, and that the event would prevent performance, without it being necessary to show that performance would otherwise have occurred. Such a construction is more likely where the clause is a "*contractual frustration clause*", i.e. the clause operates by cancelling the contract for both parties. Males LJ observed that: "*…where the effect of a clause is to discharge the parties from an obligation to perform in the future, as distinct from to relieve them from liability to pay damages for a past breach, that may well have at least a bearing on the nature of the causative effect on a party's performance which an event is required to have. In such a case, both parties need to know at once when the event occurs whether they are under any continuing obligation. There is, therefore, much to be said for a simple and straightforward causation requirement (an embargo which makes it impossible for any goods to be shipped) without requiring investigation of matters known only to one party, such as whether it was able and willing to perform if the event had not occurred*". But all depends on what the clause says.

The author's view is that both the GENCOA and VOLCOA general exceptions/force majeure clauses include a "but for" causation requirement of this kind. An example, however, of a clause that does not do so is the BIMCO War Cancellation Clause, also included in both forms, and in INTERCOA 80. That clause gives either party the right to cancel in the very limited circumstances identified in that clause, and it is unnecessary to show that the outbreak of war will in fact have any impact on performance.

(5) How many shipments?

Under a COA, a question may also arise as to whether a force majeure event impacts only on a single shipment, or on a number, or even the entirety, of the shipments yet to be fulfilled. Once again, the answer is "*it depends*": on the event in question (its nature, severity and so on) and on the terms of the clause relied on.

(6) Notice requirements?

Lastly, some clauses include requirements that notice be given of the intention to rely on an event as force majeure. It may be necessary to give notice in writing; it may be that notice must be given in a particular form, or by a particular time, to a particular individual or address, or that it must contain particular pieces of information. It is important that the charterer or owner intending to rely on the clause complies strictly with the notice requirements. If it fails to do so, it is likely to be unable to rely on the clause at all: *Adyard Abu Dhabi v. SD Marine Services* [2011] EWHC 848.

09

HARDSHIP CLAUSES AND ECONOMIC STRESS

9. HARDSHIP CLAUSES AND ECONOMIC STRESS

(1) Introduction

In the previous section, we discussed clauses that come into play when the performance of one party to a COA is prevented or impeded by some external event – a "force majeure" situation. Often however, outside events will not stop a party from performing – but they will make one or other party's performance more onerous or more expensive. In the context of the long-term relationship that is the COA, the bargain may become a bad one for one or other party.

English law's approach to such difficulties, traditionally, has been to say: "*tough*". If a party has made a bargain which turns out to be a bad one, the law will not interfere to rescue that party or to rewrite the deal.

That is all well and good but in the long run can cause difficulties. Where an owner or charterer is dissatisfied with what the deal has become, or where it is under genuine economic stress and is finding performance difficult, it may seek to terminate the COA prematurely, or perform in a way that is sub-par. Whilst the other party may be able to insist on its legal rights, it can be difficult and expensive to enforce the bargain, and legal rights are scant comfort if the counterparty descends into insolvency.

For these reasons, the market has developed different types of clause which enable the parties to modify their relationship in the light of external events that impact on their bargain. Some of these work more effectively than others: they are not easy to draft, because it is not always easy to foresee all the circumstances that might arise.

(2) Escalation and adjustment clauses

Changes in costs or the financial environment are amongst the matters that can "*tip the bargain*" in favour of either the owner or charterer under a COA. These can be addressed, if the parties so wish, by tailored clauses addressing a particular issue.

Bunker adjustment clauses have been discussed earlier in this Pack.

Currency adjustment clauses protect one or both parties from fluctuations in exchange rates.

Freight adjustment clauses: charterers are at a financial disadvantage if they are tied to a charter rate that is suddenly far above market; conversely, where owners' expenses increase because of changes in market conditions they may find that the freight rates charged under the COA are inadequate. Tying freight rates in whole or in part to an index can alleviate these difficulties. In addition, there are clauses in some long-term time charters which call for an annual review of hire rates based on owners' average monthly expenses; these can be adapted to become freight review clauses for use in COAs.

(3) Hardship clauses

More radical – to English lawyers' eyes at least – is the hardship clause which is now found in some long-term COAs. Such clauses entitle a party which claims to be suffering from hardship or economic stress owing to an event unforeseen at the time of contracting to give notice to the other party requiring it to seek to renegotiate the contract in good faith. If negotiations fail, the injured party is entitled to cancel the contract or, under some clauses, to invite an arbitrator to "*write in*" a new provision. There are standard hardship clauses and the ICC has a standard form hardship clause.[7]

Hardship clauses are often used, and are recognised as valid, in civil law jurisdictions. The common law has historically adopted a more cautious approach, because of concerns that "*agreements to agree*" are unenforceable as a matter of English law (see the next section for a more detailed discussion). However, Rose J in *Associated British Ports v. Tata Steel UK Ltd.* [2017] EWHC 694 considered a hardship clause which provided that:

> *"It is hereby agreed between the parties that in the event of any major physical or financial change in circumstances affecting the operation of [Tata's] Works at Llanwern or Port Talbot or ABP's operation of the Tidal Harbour on or at any time after the 15th day of September 2007 either party may serve notice on the other requiring the terms of this Licence to be re-negotiated with effect from the date on which such notice shall be served. The parties shall immediately seek to agree amended terms reflecting such change in circumstances and if agreement is not reached within a period of six months from the date of the notice the matter shall be referred to an Arbitrator (whose decision shall be binding on both parties and who shall so far as possible be an expert in the area of dispute between the parties)…"*

Rose J held that the clause was not void for uncertainty, and constituted a binding arbitration agreement, it being for the arbitrator to determine whether the clause had been triggered and, if it had, how the licence should be amended.

That decision was welcome, and commercially realistic. Clauses very similar to this have operated for many years in a number of areas – notably in long-term gas supply contracts, which often contain "price review clauses" that afford a large measure of discretion to arbitral tribunals to reset prices in the light of changed economic circumstances.

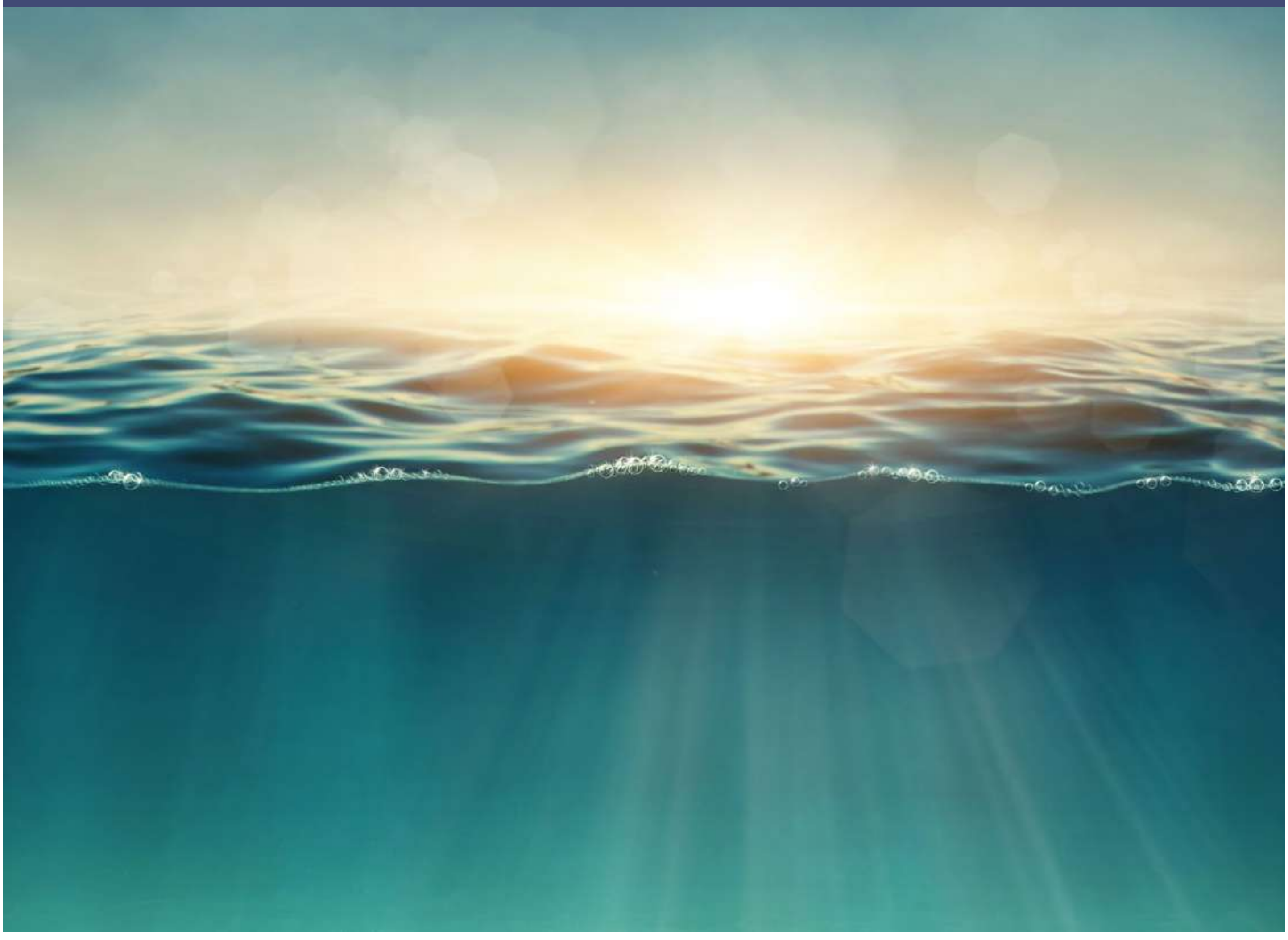
Thus, it is likely that a "hardship clause" in a COA will be enforced, if sufficient care is taken in its drafting so as to ensure that it is sufficiently certain to be workable. The less open-ended, the better. In particular, it will assist if the parties specify what is to happen if they cannot reach agreement: for example, by specifying that the matter is to be resolved in arbitration (preferably also identifying how any arbitral tribunal is to be appointed).

Any party wishing to trigger the hardship clause must also, as with force majeure clauses, take care to ensure that any requirements as to notice are strictly complied with.

[7] https://iccwbo.org/content/uploads/sites/3/2020/03/icc-forcemajeure-hardship-clauses-march2020.pdf

10

GOOD FAITH AND COAs



10. GOOD FAITH AND COAS

(1) What is good faith?

Defining "good faith" is not straightforward. A practical though perhaps unsatisfying starting point might be to say that good faith is the opposite (or absence) of bad faith, and that bad faith is something that “*you know when you see*”.

Traditionally, English law does not impose on parties to contracts a positive obligation to act in good faith. However, in the past 5-10 years, English courts have developed a more sophisticated (and less hostile) approach to contractual obligations of good faith. The existence and scope of any such obligation(s) will depend on the particular express terms and context of the relevant contract; but "*the usual content of the obligation of good faith*" may be said to be:

- to act honestly and with fidelity to the bargain;
- not to act dishonestly;
- not to undermine the bargain entered or the substance of the contractual benefit bargained for; and
- to act reasonably and with fair dealing having regard to the interests of the parties (which will, inevitably, at times conflict) and to the provisions, aims and purposes of the contract, objectively ascertained.

This summary comes from a judgment of *Leggatt J in Sheikh Al Nehayan v Kent* [2018] EWHC 333 at [175], quoting Australian authority. He added an important caveat: “*the obligation of fair dealing is not a demanding one and does no more than require a party to refrain from conduct which in the relevant context would be regarded as commercially unacceptable by reasonable and honest people*”. It is fair to say that Leggatt J – now Lord Leggatt – has been a driving force behind the introduction of concepts of good faith into the English law of contract.

(2) No general obligation of good faith

However, the general position in English law is – still – that "*there is no general doctrine of good faith in English contract law and such a term is unlikely to arise by way of necessary implication in a contract between two sophisticated commercial parties negotiating at arms’ length*": *Greenclose Ltd v National Westminster Bank plc* [2014] EWHC 1156, [2014] 2 Lloyd’s Rep. 169, Andrews J at [150]. That general position is based on (i) concern not to undermine the certainty and predictability of commercial contracts and (ii) a view that parties should be entitled to act as they see fit in their own interests provided that they do so within the terms of their contract.

That starting point does not prevent the implication of more specific terms which might well be analysed as components of "good faith". It will often be an implied term of a contract that a party will act honestly: *Yam Seng PTE v International Trade Corp Ltd* [2013] EWHC 111, [2013] 1 Lloyd’s Rep 526, Leggatt J at [135]-[137]. Further, it will frequently be appropriate to imply a term that one party will not actively prevent the other performing its contractual obligations, or that the parties are to cooperate to achieve some specific objective. If one party has a discretion affecting both parties, it will usually be implied that the discretion cannot be exercised arbitrarily, capriciously or irrationally: *The Product Star* [1993] 1 Lloyd’s Rep. 397 (owners’ discretion to refuse to proceed to any port they considered dangerous); *Braganza v. BP Shipping Limited* [2015] UKSC 17. More context-specific terms will be implied where necessary in order to make the contract work as the court considers the parties must objectively have intended it to work.

Implied terms of this sort in COAs are likely to be familiar from voyage and time charterparties, though routine charterparty implied terms cannot simply be transposed into the COA itself. For example, a notice of readiness is ineffective if given in the knowledge that it is untrue – and this is on the basis that "*There must by implication be a requirement of good faith*": *Colbelfret NV v Cylclades Shipping Co Ltd (The Linardos)* [1994] 1 Lloyd's Rep. 28, Colman J at [32:2] (obiter). Does it follow from this that notice of a laycan by the charterer or nomination of a vessel by the owner under a COA is ineffective if given in the knowledge that in fact the cargo / vessel is not available? Almost certainly not: the contractual context is different, and the innocent party is better off being able to treat the notice as effective and sue for the resulting breach, rather than having to treat the notice as a nullity.

It must also be borne in mind that there can be no implied obligation of good faith, whether general or specific, if such an obligation is inconsistent with the express provisions of the contract: *TAQA Bratani Ltd v RockRose UKCS8 LLC* [2020] EWHC 58, [2020] 2 Lloyd's Rep. 64.

(3) Express obligations of good faith

It is also open to parties to contract expressly that one or both parties should act in good faith, whether generally or in the performance of specific duties only. Express obligations of good faith per se do not appear in any of the standard form COAs, and are unlikely to be found in bespoke COAs.

Having said that, many long-term COAs do in fact include clauses requiring each party to consider the interests of the other. The prime example of this is a hardship clause (considered earlier in this Pack), which necessarily imports an element of good faith. But various other express clauses, such as force majeure clauses, freight / bunker adjustment clauses and the charterer's obligation to nominate "*fairly evenly spread*" shipments, may all be seen as express mechanisms articulating in more or less concrete form how the parties are to maintain the overall contractual objective and deal reasonably / fairly with one another.

(4) Obligation to negotiate in good faith

One form of express obligation of good faith that deserves particular mention is an express obligation to negotiate in good faith: such an obligation can, in particular, often find a place in a hardship clause. The House of Lords in *Walford v Miles* [1992] 2 AC 128 held that a duty "to carry on negotiation in good faith" was unenforceable as "*inherently repugnant to the adversarial position of the parties when involved in negotiations", and "unworkable in practice*". But in *Petromec Inc v Petroleo Brasiliero* [2006] 1 Lloyd's Rep. 121, the Court of Appeal would have been prepared to enforce an express term requiring parties to negotiate the cost of upgrading a vessel. And in *Knatchbull-Hugessen v SISU Capital Ltd* [2014] EWHC 1194, Leggatt J said that notwithstanding *Walford v Miles*, it was "*now generally accepted that … a contract may impose an obligation on one or both parties to conduct negotiations in good faith*". *Chitty on Contracts* (33rd ed) at [1-052] still regards the validity of an express term to negotiate in good faith as "*doubtful*"; but Leggatt J is now Lord Leggatt, a Justice of the Supreme Court, and it cannot be long before the point is resolved authoritatively by that court.

(5) COAs as Relational Contracts?

While there is no general duty of good faith in English contract law, it seems now to be cautiously accepted that there are certain categories of long-term contract, which have been called "*relational contracts*", where the parties do have a general obligation to act in good faith towards one another. The question arises: might a COA qualify as a "*relational contract*" for these purposes?

Leggatt J described a "*relational contract*" in S*heikh Al Nehayan v Kent* [2018] EWHC 333 at [167] as "*a category of contract in which the parties are committed to collaborating with each other, typically on a long term basis, in ways which respect the spirit and objectives of their venture but which they have not tried to specify, and which it may be impossible to specify, exhaustively in a written contract*". Distribution and franchise agreements are paradigm examples, though even these may not qualify.[8] And Fraser J in *Bates v Post Office* (No 3) [2019] EWHC 606 at [725] suggested a list of nine "*characteristics … relevant … to whether a contract is a relational one or not*".

However, a note of caution must be sounded. A number of more recent decisions suggest that the idea of a "*relational*" contract has been overplayed: see, for example, the *TAQA Bratani* decision (above), and *UTB LLC v Sheffield United Ltd* [2019] EWHC 2322, in which Fancourt J cautioned against the notion that simply labelling a contract "*relational*" imports a whole swathe of additional obligations.

COAs are, of course, typically long-term contracts, requiring co-operation between the parties in various respects, and having to survive both risk and changed circumstances over the period of their operation. Much of the content of the parties' obligations is left to be "*filled in*" after initial agreement of the COA: dates / locations of shipment, precise volumes of cargo, even freight rates. To that extent, it might theoretically be possible to describe them as "*relational*", and one commentator on COAs, Professor Lars Gorton, has suggested that COAs do or at least may so qualify.[9]

However, the key point about a COA (or at least a well-drafted one) is that it sets out expressly and (more or less) precisely which party is to make which determinations within what limits. The shipment dates and quantities are to be determined by the charterer. The freight rate will generally be fixed or otherwise calculable (e.g. pegged to a benchmark). Furthermore, the parties' obligations under a COA are in fact relatively few in number, and clearly defined: they are to provide conforming vessels / cargoes, pay freight, and comply with the associated procedural requirements. A third key point is that COAs often contain express *quasi* good faith mechanisms (such as hardship, force majeure or price escalation clauses) – and where they do not do so, the inference is likely to be that this is deliberate.

It is unlikely, therefore, that an English court or tribunal would consider it appropriate to supplement the parties' express obligations under the COA with a general duty to act in good faith, particularly given that – as noted above – the concept of a "*relational contract*" is increasingly being treated with some caution.

[8] See e.g. Carewatch Care Services Ltd v Focus Caring Services Ltd and Grace [2014] EWHC 2313 (Ch) and Acer Investment Management Ltd and another v The Mansion Group Ltd [2014] EWHC 3011, in both of which the contracts were held not to give rise to general duties of good faith.

[9] Lars Gorton 'Volume Contracts of Affreightment – Some Features and Principles' (2013) 46 Scandinavian studies in Law, pp.61-91.

11

BREACH AND TERMINATION

11. BREACH AND TERMINATION

(1) Which contract?

Most of the claims for breach that are likely to arise in connection with a COA will be where one or other party is alleged to have breached an obligation under the voyage charterparties that have been entered into pursuant to the COA. These will be resolved in the same way as any other claim under a voyage charterparty, so nothing more need be said here – save to note that many COAs (e.g. INTERCOA and GENCOA) will provide that in the event of any conflict between the terms of the voyage charterparty and the terms of the COA, the terms of the COA take precedence.

(2) Can breach of a voyage charterparty result in repudiation of the whole COA?

Having said that, the parties' obligations under the COA and the individual voyage charterparties are not completely separate. It is possible that a party's breach of its obligations under one or more of the voyage charterparties could amount to a repudiation of the whole COA and not just the voyage charterparty/ies in question. But this would be the exception rather than the norm. For example, in *P v A* [2008] EWHC 1361, [2008] 2 Lloyd's Rep. 415, a charterer repudiated a voyage charterparty and breached the COA, but did not thereby repudiate the whole COA.

P v A involved a COA on the Americanized Welsh Coal Charter form for 6 cargoes each of "*70,000 metric tons 10% more or less in Charterers option of Iron Ore or Coal*". The charterers sent a message to the owners giving the laycan for shipment No. 5 under the COA as 5/14 October. Soon afterwards the charterers said that they would like to move the laycan to 21/30 October because the shippers would not have a cargo for the period between 5/14 October. The owners declined to change the dates. They offered to cancel the fifth voyage and perform the sixth voyage on the new laycan. In place of the fifth voyage, charterers then proposed a replacement voyage at the COA freight rate. The owners maintained their position that a substitute voyage was not acceptable. The arbitral tribunal found (by a majority) for owners, and an appeal to the High Court was dismissed by David Steel J: once the laycan notice was given it was written into the COA and could not be changed save by agreement and charterers' insistence that they had the right to move the laycan dates demonstrated a clear intention not to be bound by the original nomination. The tribunal held that 'the Charterers' conduct amounted to a repudiatory breach of the fifth voyage thereby releasing Owners from any further performance of that particular voyage.' There is no indication that Owners were released from their obligation to perform the sixth voyage.

(3) Cancellation rights

A contractual cancellation right should be distinguished from the general common law right to terminate for repudiatory breach. Cancellation rights arise by virtue of express provision in the contract, and depend simply on the terms of the relevant clause, which will regulate whether, when and how any right to terminate can be exercised. General law concepts relevant to repudiatory breach cannot (necessarily) be imported: for example, while a party may terminate for anticipatory repudiatory breach where the other party has indicated before the time for performance that it has no intention of performing, there is no such thing as an "*anticipatory*" exercise of a contractual cancellation right. A party who exercises a contractual cancellation right has no automatic right to compensation, while a party who terminates for repudiatory breach is in principle entitled to damages to compensate it for the other party's failure to perform over what would have been the remainder of the contract.

Both VOLCOA and INTERCOA contain (amendable) provisions that if one or other party fails to perform one of its key obligations under the COA three times then the other shall be entitled to cancel the entire COA. For example, Clause 15 of VOLCOA deals with Owners' Failure to Nominate Tonnage. It provides:

"*Should the Owners fail to nominate tonnage according to the applicable provisions of this Contract, the corresponding quantity shall be deducted from the total contracted quantity, except if such failure results from any event which cannot be avoided or guarded against. However, the Charterers shall have the option to postpone the shipment within the period of the Contract, exercisable by giving notice of their decision not later than one month after the failure, and advising the Owners about adjustment of the programme of shipment. If the Owners have failed to nominate tonnage more than three times, unless another number of times is provided by Box 22, then the Charterers shall have the right of cancelling the remaining part of this Contract. Such right shall be exercised by written declaration and shall not be applicable to any vessels which have been validly nominated. Whether or not the Charterers exercise any option under this Clause, no claim whatsoever that they may have on the Owners shall be prejudiced thereby.*"

There is no such provision in GENCOA, which instead specifies in clause 11 that "*If a shipment is cancelled by virtue of the appropriate cancelling provisions of the attached charter party, other than by default, the cancellation applies to that shipment only and the corresponding quantity of cargo shall be deducted from the outstanding balance of the total contracted quantity*." There may be uncertainty over the scope and effect of the "other than by default" wording, but to date, none appears to have been litigated.

(4) Exercising Rights to Cancel or Terminate

Care must be taken over the wording of any notice of cancellation or of termination for repudiatory breach. There is a useful summary of relevant law in the judgment of Leggatt J in *Newland Shipping v Toba* [2014] EWHC 661, at [49]-[54]. Where a party may be entitled both to terminate for repudiatory breach and to exercise a contractual cancellation right, it is necessary for any notice it sends to make clear which of these is being exercised (at least where the consequences of exercising a contractual cancellation right may be different from terminating for repudiatory breach).

In other contractual contexts it may sometimes be possible for a notice of cancellation subsequently to be argued to have been an effective notice accepting a repudiatory breach of contract. But, typically, in the COA context, the remedial consequences of repudiation and cancellation are different and therefore, a party who exercises a cancellation right risks not being allowed afterwards to argue that its cancellation notice was or should be treated as having been the same as a notice of termination for repudiatory breach.

Be careful, clear and consistent when terminating a contract.

HFW

12

ASSESSMENT OF DAMAGES

12. ASSESSMENT OF DAMAGES

(1) The Compensatory Principle

The basic principle is that where one party has breached a contract, the other party is entitled to damages to put it in the same position as it would have been in if the contract had been performed. That requires the court or tribunal to compare (a) the position that the innocent party would have been in had the contract been performed with (b) the position it in fact ended up in as a result of the breach.

Position (a) is, of course, hypothetical. That has led to a small number of important cases exploring the question of how hypothetical the comparison should be. The answer appears to be "*as unhypothetical as possible*". It has to be assumed that the contract-breaker would have performed rather than breached its contract. Otherwise, any real-world events that have taken place between the date of breach and the date of trial which might have a bearing on what would have happened to the innocent party on that hypothesis, should be taken into account: *The Golden Victory* [2007] 2 AC 353.

If an owner claims damages from the charterer under a COA for failing to declare laycans for shipments, is it a potential defence for the charterer to show that the owner would not have been able to provide a vessel even if the laycans had been declared? This was the argument run (successfully) in *Flame SA v Glory Wealth Shipping PTE Ltd* [2014] QB 1080 on the basis that the financial crash of 2008 would have left the owner insolvent and unable to perform. [10] The arbitral tribunal rejected the charterer's argument but on appeal, the Commercial Court found in the charterer's favour, essentially on the basis of the compensatory principle. Its concern was that otherwise, the innocent owner might find itself in a better position than it would have been if the contract had been performed. The burden of proof is on the innocent party (here the owner) to show that it would have been able to perform.

(2) Minimum Performance Principle

The general principle where a claim is made against a defendant who had a choice as to how it would perform its obligations under the contract, is that damages will usually be assessed on the assumption that the defendant would have performed in the way most favourable to itself.

This principle should not be taken too far. In the COA context, for example, if an owner had a claim against the charterer for failure to declare shipments, it would be right to assume that the charterer would have shipped only the minimum permissible quantities, but wrong to assume that the charterer would have done so only on the dates that conferred the maximum advantage to it (and maximum disadvantage to owners) in terms of the differential between COA and market freight rates.

The principle was considered by the Court of Appeal in *Durham Tees Valley Airport Ltd v Bmibaby Ltd* [2011] 1 Lloyd's Rep 68 (not a COA case, as the party names indicate). Where a contract permits alternative methods of performance (e.g. choice of a range of permissible cargo volumes), damages will be calculated on the basis that the defendant had made the choice least favourable to the claimant. But where the defendant has a single obligation to perform (e.g. nominating shipments at intervals to be "*fairly evenly spread*"), the question for the court is "*what is most likely to have happened if that obligation had been performed" – rather than "how could the defendant have performed in the way least favourable to the claimant*".

[10] The converse position will also be true: that is to say, if an owner fails to provide tonnage under a COA and the charterer claims against it, it will be a defence to the owner to say that the charterer would not, in turn, have been able to perform its part of the bargain. However, a case where a defence along these lines succeeds on the facts is likely to be a rare one.

As Patten LJ said at [79], "*The judge conducting the assessment must assume that the defendant would not have acted outside the terms of the contract and would have performed it in his own interests having regard to the relevant factors prevailing at the time. But the court is not required to make assumptions that the defaulting party would have acted uncommercially merely in order to spite the claimant. To that extent, the parties are to be assumed to have acted in good faith although with their own commercial interests very much in mind*."

A recent though inconclusive example of these principles in application in a COA context appears in *Palmali Shipping SA v Litasco SA* [2020] EWHC 2581 at [63]-[64] . One of the questions in that case was between which ports the shipments would have taken place. The defendant argued that damages should be assessed on the basis that it would have chosen to ship the cargo using the route which would have involved the lowest payment to the claimant. The claimant argued that the minimum performance doctrine did not apply, or should be limited to reasonable choices on the part of the defendant; and that instead, damages should be calculated on the assumption that there would be the same distribution of voyages as those which did take place under the COA. The judge was not required to resolve the parties' competing positions, since he was dealing with pre-trial applications. [*IS THIS WORTH INCLUDING?*]

(3) Mitigation of Loss

An innocent party is expected to take reasonable actions to reduce or even eliminate the loss that it would otherwise have suffered as a result of a breach by the other party. Typically, courts and tribunals do not impose an exacting standard, and have sympathy for the fact that the innocent party is only having to take mitigating action because of the fault of the contract-breaker. The burden is on the party in breach to show unreasonable conduct by the innocent party. (An example in a COA context is *The 'Kriti Rex'* [1996] 2 Lloyd's Rep 171 at [198])

In the COA context, a charterer faced with a failure to nominate a vessel by an owner would typically be expected to go out into the market (if there is one) to charter an alternative vessel, while an owner faced with a failure to declare laycans would be expected to try to find alternative employment for the vessel. As to the latter, a shipowner may be able to say on the facts that there was no "market" for voyages of the type in question, and "T*he missing fixtures could only have been 'replaced' with fixtures for voyages elsewhere in the world but those were voyages which could and would have been done in any event, if necessary with more chartered-in vessels*". This submission was accepted by HHJ Mackie QC in *SwissMarine Services SA v Gupta Coal India Private Ltd* [2015] 1 Lloyd's Rep 456 (an HFW case), leading to the conclusion that the owner was entitled to the full profit that it would have earned from the fixtures in question.

A question arose in a New York arbitration [11] of whether, faced with owners' nomination of a vessel that was too small (albeit not by much) to carry the minimum quantity specified in the COA, charterers ought (by way of mitigation) nevertheless to have taken that smaller vessel in order to carry what it could. On the facts, the charterers had rejected the nomination; there had been a protracted period of negotiation; and only when that had failed, the charterers had gone out into the market and chartered an alternative vessel at a considerably higher rate. Owners' mitigation defence failed: on the facts, it was essential to the subcharterer (who had the same rejection rights) that the vessel could carry the full quantity of cargo

[11] The arbitration is reported in Nordisk Skibsrederforenings Medlemsblad, No. 557, p.5825ff, and described in an article by Professor Lars Gorton 'Volume Contracts of Affreightment – Some Features and Principles', Scandinavian studies in Law (2004) 46, pp.61-91.

because the number of liftings out of the port was limited. The tribunal's decision to award charterers their loss in full is therefore unsurprising.

(4) Timing

Where a court or tribunal has to determine the market freight rate in order to compare it with the COA freight rate, what is the relevant date for assessing the market rate? The basic position is that it is the market rate at the time when performance should have taken place that matters. If one party has granted the other an extension of time, it will be the market rate *as at the extended date for performance* which matters: see *SwissMarine Services SA v Gupta Coal India Private Ltd* [2015] 1 Lloyd's Rep 456 at [20]-[21].

13

COAs UNDER US LAW

13. COAS UNDER US LAW

(1) Contract Law Principles Applied to COAs

In the US (as in the UK), the term "contract of affreightment" simply means a contract for transportation of goods by ship, so strictly speaking it includes bills of lading as well as voyage and time charter parties. For practical usage, however, COA usually refers to a contract for consecutive voyage charters, volume contracts calling for carriage within a specified time, or generally a sort of master service agreement for carriage in multiple voyages.

A COA is a maritime contract within the US courts' admiralty jurisdiction, so it is governed by maritime law, subject to relevant choice of law rules. Normal contract law principles apply to COAs, so they are to be construed like any other contract, that is "*by their terms and consistent with the intent of the parties." Norfolk S. Ry. Co. v. Kirby, Pty Ltd.*, 534 U.S. 14, 31 (2004). Federal courts applying maritime law to COAs sometimes adopt contract interpretation principles from state law, from the Uniform Commercial Code, and from the Restatement (Second) of Contracts, unless that would somehow undermine concern for "*uniform meaning of maritime contracts.*" *Id.*, 534 U.S. at 28.

(2) Safe Port Obligations

The United States Supreme Court recently clarified interpretation of a safe berth clause in a voyage charter party, and its holding would apply to COAs that include a safe berth/safe port clause. The Court held that an unqualified safe berth clause constitutes a warranty that imposes on the charterer an absolute duty for safety of the berth it selects. *Citgo Asphalt Ref. Co. v. Frescati Shipping Co.,* 140 S. Ct. 1081 (2020). The safe berth clause in that case, from the ASBATANKVOY form, said "*the vessel shall load and discharge at any safe place or wharf . . . which shall be designated and procured by the Charterer, provided the Vessel can proceed thereto, lie at, and depart therefrom always safely afloat*." The Court applied plain language contract interpretation principles to conclude that this language imposes an absolute duty, binding the charterer to a warranty of safety. The Court also said the parties "*remain free to contract around" the warranty, "by expressly limiting the extent of their obligations or liability.*" *Id.,* 140 S. Ct. at 1093. Thus, a COA safe berth clause that expressly limits the shipper's duty to one of due diligence, like the INTERTANKVOY form clause, would not be a warranty of safety, instead imposing only a duty to exercise due diligence to nominate a berth or port that is safe.

(3) Force Majeure

Although the common law doctrine of force majeure has long been recognized in US law, the doctrine "*should not supersede the specific terms bargained for in the contract*." *Perlman v. Pioneer Ltd. P'ship,* 918 F.2d 1244, 1248 (5th Cir. 1990). In other words, the terms of the particular force majeure clause in a COA, or in any other contract, control its application. Thus, questions like what kind of event could excuse a party's performance, whether and when notice is required to invoke force majeure, and whether the COA could be terminated because of an unforeseen event, should all be decided based on the language written in the COA force majeure clause, if it has one.

(4) Good Faith and COAs

There is some authority in the US to support an implied duty of good faith in the performance of a COA. The United States Court of Appeals for the Ninth Circuit has said, as a matter of federal contract law, "*each contract carries with it a duty of each party to act in good faith and to deal fairly in performing and enforcing the contract.*" *Flores v. Am. Seafoods Co.*, 335 F.3d 904, 913 (9th Cir. 2003). The Flores court said that in the context of admiralty law governing a seaman's rights under a fishing contract, but the same principles arguably could be used to imply an obligation of good faith in a COA as a maritime contract. For example, in *Misano di Navigazione, SpA v. United States*, 968 F.2d 273, 275 (2d Cir.1992), the court found a charter party clause imposed a good faith standard of satisfaction for the charterer's inspector to approve or reject tank cleanliness for carriage of a designated special cargo. Relying on Restatement (Second) of Contracts § 228, the court said good faith meant the inspector's "*satisfaction must be honest and within the circumstances of the contract.*" *Id*., 968 F.2d at 276.

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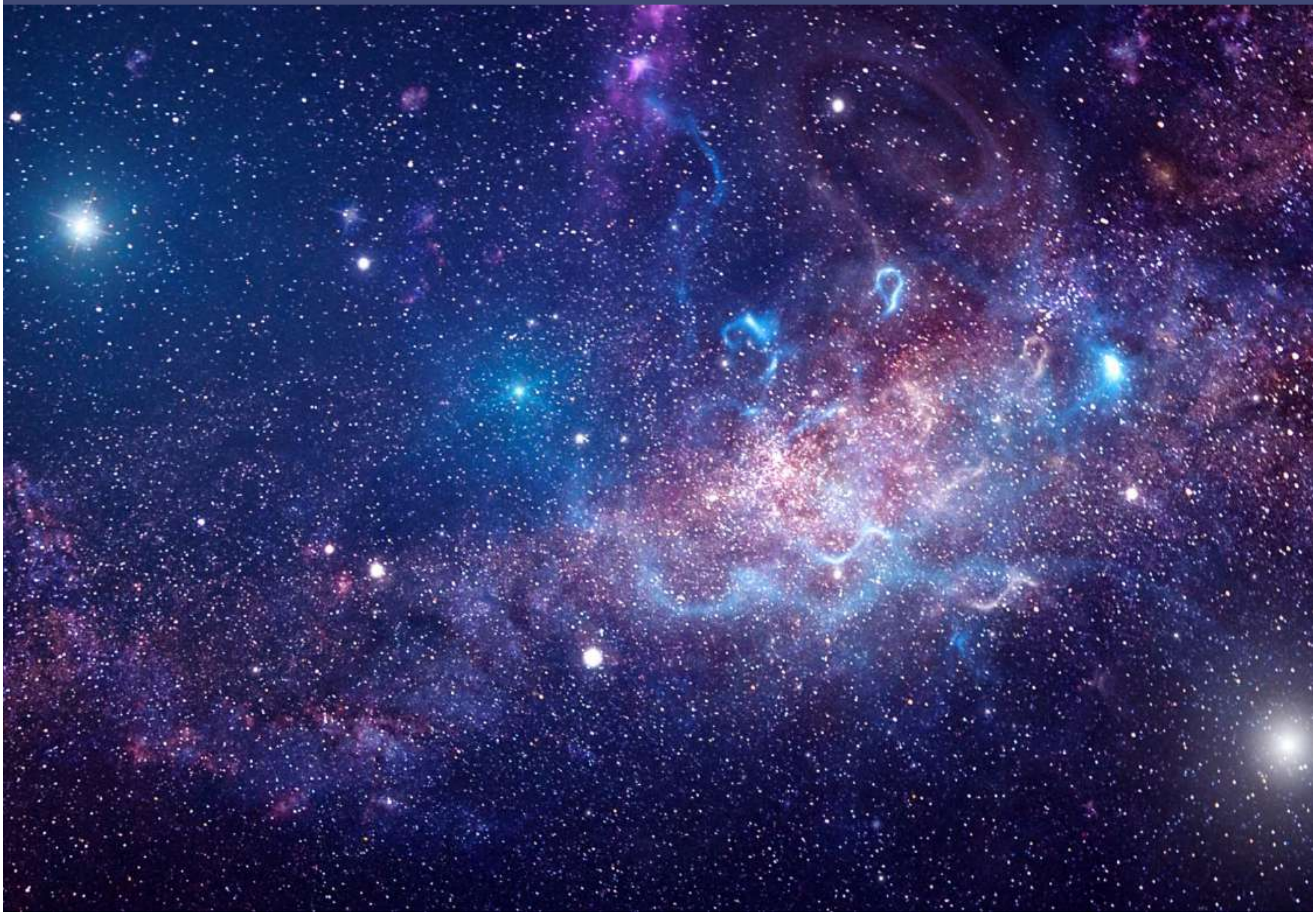
ON THE HORIZON – FUTURE PROOFING THE COAs OF TOMORROW



14. ON THE HORIZON – FUTURE PROOFING THE COAS OF TOMORROW

(1) Electronic bills of lading (E-bills)

The shipping industry has been slow to adopt the use of E-bills but there is an increasing interest in their benefits, particularly in light of Covid-19, which has caused parties to explore alternatives to contractual mechanisms which require face-to-face contact or the physical transfer of documents. It is likely in future, more COAs will require or allow the use of E-bills.

There are various benefits to E-bills, particularly in overcoming some of the problems caused by paper bills of lading ("BOL"). One of the key issues arises due to the carrier's obligation to discharge the goods on production of an original BOL. This is problematic given the fact that the cargo may be sold multiple times during carriage and the BOL may not be at the discharge port and in the hands of the consignee at the time the vessel is ready to discharge. The paper BOL is frequently not delivered to the consignee in time and the carrier often accepts a letter of indemnity ("LOI") from the charterer instead of production of the BOL. The charterer is also likely to seek LOIs from any sub-charterer, with further LOIs being provided along the contractual chain. This can create problems, particularly if the provider of an LOI becomes insolvent as the relevant LOI then has little practical value.

E-bills can be sent instantaneously, which avoids the time consuming burden of physically endorsing the BOL along a sale or banking chain and which also reduces the need for LOIs as there should be limited delay relating to transfers. Amendments to the BOL are also easier.

There are some legal obstacles; for example an E-bill is not automatically a document of title (unlike a paper BOL) and there is as yet little case law relating to the use of E-bills. Electronic trading systems (such as BOLERO) generally attempt to replicate the legal characteristics of paper BOLs but parties must carefully consider the legal implications of using E-bills.

If parties wish to have the flexibility of using E-bills, we recommend that a specific clause is included in the COA. An example is the BIMCO clause:

BIMCO Electronic Bills of Lading Clause 2014

(a) At the Charterers' option, bills of lading, waybills and delivery orders referred to in this Charter Party shall be issued, signed and transmitted in electronic form with the same effect as their paper equivalent.

(b) For the purpose of Sub-clause (a) the Owners shall subscribe to and use Electronic (Paperless) Trading Systems as directed by the Charterers, provided such systems are approved by the International Group of P&I Clubs. Any fees incurred in subscribing to or for using such systems shall be for the Charterers' account.

(c) The Charterers agree to hold the Owners harmless in respect of any additional liability arising from the use of the systems referred to in Sub-clause (b), to the extent that such liability does not arise from Owners' negligence.

(2) Resident Arbitrator Clauses

During the course of a lengthy COA, disputes between the parties can naturally arise. Too often within the shipping industry these disputes become protracted, increasingly acrimonious and then litigious. In the future, parties may consider an alternative means of settling these disputes at an earlier juncture through "resident arbitrator clauses".

Under such a clause a retired judge, a QC or a commercial arbitrator would be designated as a "resident arbitrator". Their role would be to resolve virtually any disputes that arise during the life of that COA. If a dispute arises, both parties make submissions to the resident arbitrator whose decision is then binding. This process is intended to stop disputes festering and instead to allow them to be resolved quickly and with as little damage to the parties' long-term relationship as possible. Such clauses should include sufficient safeguards to ensure fairness and consistency.

(3) Future crewing / ethical clauses

With its uniquely international character, shipping is a one of the most diverse industries in the world. However, this diversity has not always resulted in equal employment opportunities both on and off shore. In line with the wider societal push towards more equality in the workplace, parties may consider trying novel ways to encourage diversity. This encouragement could be in the form of so called "diversity clauses" included within shipping contracts such as COAs. Whilst not all parties may be willing to bind themselves to specific quotas, they could instead make a general commitment to diversity during the course of the COA.

An interesting trend in recent years has been the increased consumer awareness of how ethically their goods have been sourced and transported. In order to meet this growing awareness, there is perhaps room to raise standards in shipping and to ensure crewing health and safety, as well as to be more transparent and therefore more accountable. Parties to a COA could consider including an obligation for both sides to publish their crew safety records. This could encourage increased safety standards. Parties could also discourage the exploitation of seafarers by including a minimum wage clause for crew.

One of the greatest challenges approaching the shipping industry is how to deal with greater automation aboard vessels. Whilst the widespread adoption of autonomous vessels has not yet occurred, there are indications that the vessels of tomorrow will increasingly have more automation and fewer seafarers than those of today. Parties may therefore wish to consider whether their COAs allow for a smooth transition towards more autonomous vessels.

(4) "Green" clauses

With the visible evidence of extreme weather, the extinction of species and the melting of polar ice, humans have become increasingly aware of our impact upon the environment. Halting and correcting this impact has become a challenge for all industries, including shipping. It is likely that in future, COAs will contain clauses seeking to minimise the effect the parties have upon the environment.

On 1 January 2020 the IMO introduced a Global Sulphur Cap with the limit for sulphur in fuel used on board ships set at 0.5%. The introduction of this cap prompted a wave of sulphur emissions clauses being included within shipping contracts, including COAs. Popular clauses such as the BIMCO 2020 Marine Sulphur Fuel Clause generally defined "non-compliant fuel" in line with this 0.5% cap. However, those entering longer-term arrangements may want to consider whether their contracts allow for the possibility of the IMO amending the Global Sulphur Cap in the future. Parties may want to ensure that their contracts contain enough flexibility to avoid being adversely affected by any such change.

Parties should not restrict their consideration of fossil fuel emissions to sulphur. The IMO's ambitious goal of achieving decarbonisation is currently set for the second half of the 21st century. However, given the growing public and political consciousness about decarbonisation, it is not inconceivable that these decarbonisation targets will be brought forward. Parties wishing to pre-empt such actions may wish to include carbon limits or so-called "carbon offsetting" clauses.

Aside from emissions specific clauses, parties may also consider other "green" clauses. So called "climate change clauses" (whereby the parties endeavour not to amplify the impact of climate change), single use plastics clauses (limiting their use) and defining "Environmental Requirements" within COAs are all steps that can be taken to make contracts more environmentally friendly. With the ever-increasing investor, public and political emphasis upon green issues we expect to see an increasing number of such provisions within COAs.

Within ship finance we have already seen lenders establishing a framework to ensure that their counterparties have policies in place that are environmentally friendly and that they have certain aspirations in regard to their emissions footprint. The so-called "Poseidon Principles", announced in June 2019, have already had numerous prestigious signatories committed to implementing them, and helping their counter-parties to do so. Those principles include assessment, accountability, enforcement and transparency. Whilst the clauses relating to the Poseidon Principles are currently intended for financing agreements, it is foreseeable that similar clauses make their way into other shipping contracts, including COAs:

(5) Pandemic clauses

It would have been uncommon twenty years ago to have a specific "pandemic clause" included within a COA. However, the outbreak of Ebola in West Africa in 2014 caused greater awareness of the disruption that epidemics and pandemics can cause to shipping contracts. Therefore, in response to the Ebola outbreak, clauses such as the BIMCO "Infectious or Contagious Diseases" Clauses (2015) began to be widely incorporated. However, Ebola and Covid-19 are markedly different in character and impact and, in order to meet the Covid-19 threat, parties have increasingly sought to update these pandemic clauses. As the pandemic continues, we will likely see such clauses continuing to evolve and parties may find benefit in staying abreast of such evolution.

(6) Demurrage circuit break clause

Lengthy delays at ports are sometimes an unfortunate reality within shipping. However, while not exclusive to the Covid-19 pandemic, the virus has exacerbated these sorts of lengthy delays and exposed the unfairness that they can create with regards to the payment of demurrage. During periods of falling freight rates, owners have generally been content to collect demurrage earnt during these periods of lengthy delay. However, in a different situation in the future (one whereby there are port delays during a period of soaring freight rates), Owners may not want to be held during a lengthy delay being paid low demurrage. Therefore, parties in the future may see some benefit in having so-called: "circuit breaker" clauses. A circuit breaker clause could come into effect during a long period of demurrage and, after a certain period of time, would move the demurrage rate either higher or lower in line with the prevalent market level. The benefit of this would be that, in the short term, the parties would benefit from the certainty of a fixed demurrage rate. However, if the delay persists, the parties would also benefit from an adjusted demurrage rate that was more reflective of the market reality.

(7) Sanctions

A significant feature of international relations within recent years has been the increasing use of international trade sanctions by states and international organisations such as the EU and the UN. The U.S Office of Foreign Assets Control (OFAC) remains both the most prolific and the most aggressive proponent of international trade sanctions (their $8.9 billion fine of BNP Paribas in 2015 being the largest such fine in history). However, an increasingly long list of players are using sanctions as an extension of their foreign policy objectives.

International trade sanctions can be broad in scope, can be introduced without warning and there can be significant repercussions imposed for sanctions breaches. It is little wonder that their increased use has caused consternation amongst the shipping community.

It would be challenging to predict who will be imposing sanctions and who will be the target of them during the course of a long-term COA. Therefore, in order to overcome such uncertainty, we strongly recommend that such agreements contain robust sanctions clauses.

The terms of such clauses should not be overly specific (for example, they should not be restricted to nations currently under sanctions) but should instead be flexible and allocate risk between the parties should future sanctions affect performance. Termination and/or suspension rights can provide helpful "breathing space" when dealing with a sudden change in sanctions, whether that is new sanctions being imposed, previously permitted entities suddenly becoming prohibited, or suspended sanctions snapping back into place. Whilst such terms cannot prevent sanctions applying to the parties or the contract (or excuse a breach of sanctions), they can manage their impact on the performance of the COA.

(8) Insolvency and "fiscal fitness" clauses

It may be surprising to some that there is no English common law right to terminate a contract upon a counterparty becoming insolvent. Therefore, it is common practice in the contracts of many industries to include contractual terms specifically dealing with counterparty insolvency. Whilst this has not always been the case within shipping, we are increasingly seeing parties seeking to address specifically the "fiscal fitness" of their counterparties. Such clauses are particularly common within long-term COAs.

The most common approach to contractually protecting against counterparty insolvencies has been in the form of default clauses that cover insolvency or pure insolvency clauses. Default clauses contain a warranty that the counterparty is solvent and place them into default of contract if that does not remain the case. Alternatively, an "Automatic Early Termination" (AET) clause can be included which automatically terminates the contract upon the occurrence of some event, typically when a counterparty becomes insolvent.

An AET clause may add an extra layer of protection for the solvent party. This extra layer can prove particularly useful during periods of wider economic turmoil, where an earlier struck bargain suddenly looks expensive in comparison to the prevailing market. As the duration of COAs continues to rise, it is likely that more COAs will contain clauses seeking to mitigate the effects of counterparty insolvency. However, parties considering including an AET clause in a long-term COA should bear in mind that insolvency doesn't always lead to liquidation. Companies often become insolvent, but are later saved from being liquidated (and are thereafter able to continue as a going concern). Therefore, one of the potential disadvantages of an AET is that it can automatically terminate a long term contract on the basis of a short term (and temporary) insolvency. Due to the automatic nature of the clause, the terminating party has no control over whether or not the contract is actually terminated. This is particularly problematic when the underlying contract was struck on otherwise favourable terms.

The slew of shipping insolvencies cases following the 2007-08 global financial crash demonstrated some of the difficulties that can be encountered by long term contracts when a counterparty breaches a contract by becoming insolvent. A particular issue that emerged was how damages are calculated when a counterparty's insolvency causes a repudiatory breach of contract. In *The Kildare* [12] the defendant had entered into a Consecutive Voyage Charterparty (CVC) with the claimant's vessel prior to the crash. After the crash, and in repudiatory breach of the contract, the defendant charterers (who had encountered financial difficulties) redelivered the vessel early. One of the issues that arose was that (due to market forces after the crash) there was no equivalent market which the court could use to assess damages for breach. This is an issue that parties entering such long-term contracts should consider, that the market in which the contract was formulated could be wildly different (or non-existent) by the time a breach of contract occurs. In the Kildare, the court eventually found that the claimants should recover the difference between the stable earnings anticipated under the long term contract and the patchier earnings that the vessel was able to command on the spot market.

On a broader economic level, parties should recognise that under many contracts, events such as currency crashes would not constitute a force majeure event. Drafters may therefore consider trying to insulate against the risk from large-scale economic events. Whilst rare within shipping contracts, some have attempted to achieve this insulation through so-called "economic force majeure" clauses (such as a currency crash clause).

It is prudent for parties to long term contracts to cater for the financial fitness and solvency of their counterparties in their agreements. Doing so will allow parties to avoid some of the damage that can be caused when a counterparty becomes insolvent.

[12] Zodiac Maritime Agencies Ltd v Fortescue Metals Group "The Kildare" [2010] EWHC 903

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Whilst every care has been taken to ensure the accuracy of the information contained in this pack at the time of publication, the information is intended as guidance only. It should not be considered as legal advice.

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