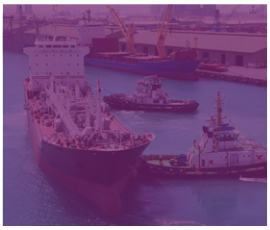
Shipping

February 2016

SHIPPING BULLETIN



Welcome to the February edition of our Shipping Bulletin.

We start this edition by examining a judgment of the Singapore High Court dealing with the topical issue of whether a shipowner is obliged to pay for the bunkers provided to the vessel, and which emphasises the importance of knowing who you are contracting with.

The next article considers the risks of liquefaction, the provisions of the IMSBC Code, and specifically the steps that the IMO is taking in relation to the treatment of bauxite, and provides some practical advice to shipowners and cargo interests on these issues.

In our latter two articles we look at the steps a party can take when its counter-party is in financial difficulty. The first article focuses on the *CLIPPER MONARCH*, in which time charterers who had not been paid freight and demurrage sought to exercise their rights to lien and sell the cargo, and then to have the proceeds of sale released to them. Our final article provides an overview of the various practical measures that an owner can take if his time charterer stops paying hire.

Should you require any further information or assistance with any of the issues dealt with here, please do not hesitate to contact any of the contributors to this bulletin, or your usual contact at HFW.

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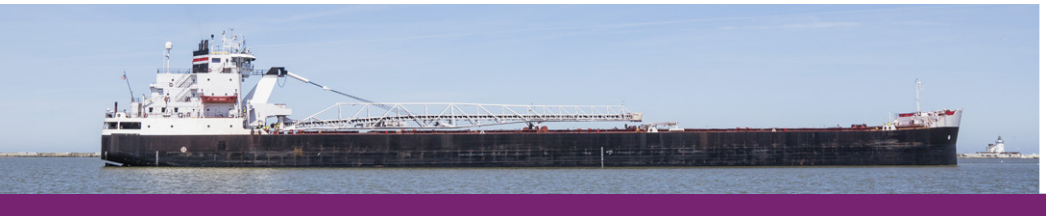


The *BUNGA MELATI 5*: Singapore bunker supplier loses US$21 million as Singapore High Court dismisses its claim

This case is important for shipowners and marine fuel suppliers entering into bunker supply contracts as it highlights the need for contracting parties to clearly identify their counterparties. Taking such steps will eliminate costly assumptions that could give rise to unintended contractual relationships and the risk of litigation.

This decision is important as it illuminates the dangers that emerge when contracting parties are not certain of the identity of their counterparties. It highlights that it is dangerous to make assumptions that one party is acting as another's agent.

HUGH GYLES, ASSOCIATE

Introduction

The recent Singapore High Court decision of *Equatorial Marine Fuel Management Services v MISC Berhad*[1] concerned whether the defendant, a substantial shipowner and operator, had to pay the plaintiff, a marine fuel supplier, for bunkers supplied to the defendant's ship. The US$21 million dollar question hinged on what role a company called Market Asia Link Sdn Bhd (MAL) played and whether it was acting as the defendant's agent.

Background

The dispute emerged in 2008 after Equatorial Marine Fuel Management Services (EMF) had supplied MISC Berhad (MISC) with US$21 million worth of bunkers to its vessels through brokers. EMF proceeded to initiate legal action against MISC after it chose not to pay for the bunkers.

The role MAL played in the facilitation of the bunker supply contracts was crucial in determining liability. EMF claimed it was clear from the evidence that MAL was acting as MISC's agent when it entered into the contracts and therefore MISC was liable as principal for payment. Conversely, MISC claimed it was not liable for payment because MAL was not its agent and MISC was not a party to the bunker contracts. EML must therefore look to MAL, its contractual counterparty, for payment.

The key issue for consideration was whether MISC had granted actual authority to MAL to act as its agent in respect of the contracts.

Did MAL have actual authority to enter into the contracts on MISC's behalf?

EMF invited the court to infer that actual authority had been granted by MISC to MAL to go into the market and purchase bunkers on its behalf. EMF attempted to persuade the court that MISC had approved MAL as its registered bunker supplier on the basis that:

1. If a proper assessment of MAL's suitability had been made by MISC, it is unlikely the MAL's application would have been granted.
2. MAL lacked both capital and experience in the supply of bunkers.
3. It was "incredible" that MAL had risen to become the major bunker supplier to MISC having had no prior experience or track record as a bunker supplier.
4. The bunker contracts were unprofitable for MAL.

MISC countered that:

1. The approval of MAL's application to supply bunkers, even if insufficiently considered and improperly granted by MISC, was no basis for the inference that MISC granted authority to MAL to act as an agent.
2. There was nothing untoward about the number of contracts that MISC had awarded to MAL given that MAL was the lowest bidder on most occasions. Where a lower bidder was received, the contract was awarded to the other bidding party.

1 [2015] SGHC 190

3. The fact that the contracts were unprofitable to MAL reinforced the possibility that they were a bargain for MISC and explained why MAL became a major bunker supplier to MISC.

The decision

The court preferred MISC's arguments and decided that the evidence did not support an inference that MISC authorised MAL to act as its agent. The court noted that since MISC had put itself in the position of getting cheap oil from MAL, it would have been inconsistent with that objective for MISC to have granted MAL authority to act as its broker with authority to make more expensive contracts on its behalf. Consequently, EMF's claim was dismissed.

HFW's perspective

This decision is important as it illuminates the dangers that emerge when contracting parties are not certain of the identity of their counterparties. It highlights that it is dangerous to make assumptions that one party is acting as another's agent.

Where contractual negotiations involving counterparties are concerned, due diligence should be exercised so as to make clear beyond doubt who are the parties to that contract. Intermediate sellers, buyers, brokers and agents should always be identified to avoid unintended contractual relationships and the associated risk of litigation.

For more information, please contact Hugh Gyles, Associate, on +61 (0) 3 8601 4528 or hugh.gyles@hfw.com, or your usual contact at HFW.

Liquefaction – a shift in IMSBC Code classification in sight following the *BULK JUPITER* bauxite incident?

The IMO Sub-Committee on Carriage of Cargoes and Containers issued a circular in October 2015 on the potential liquefaction of bauxite, which is currently categorised as a cargo not at risk of liquefaction. It stated that the risks of carrying bauxite are being investigated, which may lead to an amendment of its classification. In the meantime, caution both from the carrier and shipper's perspective is required.

Following incidents in Brazil, Indonesia and Malaysia, in particular the *BULK JUPITER* tragedy in January 2015, in which 18 lives were lost – which some believe to be caused by bauxite liquefaction – the Sub-Committee has issued a circular on bauxite liquefaction that should be read attentively by all parties involved with bauxite.

Liquefaction occurs when a solid acts as a liquid – which can cause a cargo shift on board. It is most likely to occur in loose solids with a high moisture content. The finer the particles, the higher the risk. As pressure is applied – for example from the movement of a vessel due to swell – the water present in the cargo is forced into a lower pressure area. Where the cargo is made up of large particles, water will normally be able to escape to the gaps between the particles. This will not always be possible with fine particles with little or no space between them, however, and the pressure will build until it is released by the solid "flowing". This potentially causes a cargo shift and can result in instability, listing or even the capsizing of a vessel.

The risk of liquefaction is normally reduced by the requirement that relevant cargoes be notified as belonging to within Group A (*cargoes at risk of liquefaction*) of the International Maritime Solid Bulk Cargoes (IMSBC) Code. Group A cargoes are subject to a rigorous testing and certifying regime to ensure they are safe to ship. Bauxite, however, is a Group C cargo (cargoes not at risk of liquefaction).

Bauxite under the Code

As listed in Group C of the Code, bauxite has the following properties:

1. Moisture content of 0%–10%.
2. 70%-90% lumps between 2.5 and 500mm.
3. 10%-30% powder.

Liquefaction occurs when a solid acts as a liquid – which can cause a cargo shift on board. It is most likely to occur in loose solids with a high moisture content.

STEPHEN LOVE, ASSOCIATE

The risk of liquefaction is normally reduced by the requirement that relevant cargoes be notified as belonging to within Group A (cargoes at risk of liquefaction) of the International Maritime Solid Bulk Cargoes (IMSBC) Code.

Heavy rain during open mining will inevitably lead to a higher moisture content, but as bauxite is in Group C it does not need to be tested for its moisture content or flow characteristics.

Recent Code updates

Amendments to the IMSBC Code made in 2013, resolution MSC.354(92) came into force on 1 January 2015. These amendments include among other things numerous new cargoes being classed in Group A. A further resolution (MSC.393(95)), which comes into force on 1 January 2017, will add iron ore fines as a Group A cargo.

There is arguably increasing evidence of bauxite liquefaction, but bauxite remains a Group C cargo under the Code. However, the Sub-Committee has now issued a circular which warns that bauxite may be prone to liquefaction and that its classification may be changed to that of Group A.

The Sub-Committee's circular therefore advises that a master should not accept bauxite if:

1. The moisture content is above 10% and/or particles of size 2.5mm to 500mm do not make up at least 70% of the cargo.
2. The cargo is declared as Group A and the shipper has declared the transportable moisture limit[1] and the actual moisture content is higher than this.

If the competent authority of the loading port determines that the cargo does not present a Group A risk, the master can load.

While the flag state for *BULK JUPITER* has investigated the loss and concluded liquefaction was the likely cause of the tragedy, the IMO has been more cautious while further investigations are being undertaken. Until a definitive answer is reached concerning the risk of bauxite liquefaction, it would seem appropriate for shipowners and cargo interests alike to treat the carriage of bauxite with caution and to be acutely aware of the dangers inherent in a high moisture content in order to prevent what are avoidable risks.

For more information, please contact Stephen Love, Associate, on +33 (0)1 44 94 40 50 or stephen.love@hfw.com, or your usual contact at HFW.

1 Transportable Moisture Limit – this is the maximum moisture content of a cargo that is considered safe for transportation in ships.

hfw *CLIPPER MONARCH*[1] liening on Silver Rock Investments

Where a disponent owner exercises its power of lien over its voyage charterer's cargo and subsequently obtains an order for sale of the cargo, what rights will that disponent owner have over the proceeds of sale?

Facts

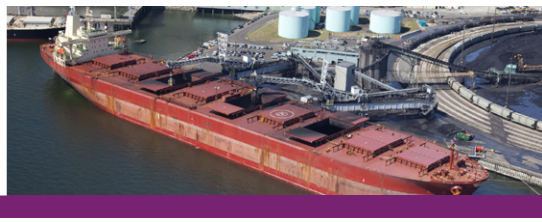
Silver Rock Investments, the voyage charterer of the vessel *CLIPPER MONARCH*, failed to make a payment of freight and demurrage due to Castleton Commodities Shipping (CCS) as the disponent owner. Acting in reliance on a clause in the voyage charter which provided that *"owners shall have a lien on the cargo for freight, deadfreight, demurrage and damages for detention"*, CCS ordered the vessel to anchor in international waters until the payment was received from Silver Rock.

When payment was not forthcoming, CCS obtained an order from the English High Court that Silver Rock's cargo should be sold and the proceeds *"treated as if subject to the same rights (if any) as the claimant had in respect of the goods prior to their sale."*

There was some uncertainty as to whether the cargo was owned by the shipper or Silver Rock at the time the sale order was made. Accordingly CSS secured an assignment of the carrier's rights under the bills of lading which incorporated the voyage charter's lien clause.

1 [2015] EWHC 2584 (Comm) *Castleton Commodities Shipping Company Pte Limited* (Claimant/Respondent) *v Silver Rock Investments* (Defendant/Appellant)





CCS obtained arbitration awards against both Silver Rock and Grupo Minero, the seller of the cargo to Silver Rock, in respect of the freight and demurrage and these awards were converted into High Court judgments for the purposes of enforcement. CCS then applied to the High Court for an order that the sale proceeds be released to it.

The judgment

The court accepted that CCS was entitled to the sale proceeds on the basis that it was a judgment creditor of both Grupo Minero and Silver Rock, the two possible owners of the cargo. However, the court also found that CCS's rights derived from the exercise of its lien over the cargo, conferred an alternative right to the proceeds of sale. Although the judge did not explore this issue in detail, he decided that:

1. The cargo was either bound by a non-possessory lien in favour of CCS as disponent owner under the voyage charter, or a possessory lien in favour of the carrier, of which CCS was the assignee, arising under the bills of lading.
2. CCS had exercised its non-possessory lien over the cargo by ordering the vessel not to proceed to its discharge port and the carrier had exercised its possessory lien by following this instruction.
3. In the circumstances of this case, *"the rights of lien, which pre-existed the sale, can be said to have been transformed into a right to the proceeds of sale of the cargo concerned"*. The judge did not seem to think it mattered whether the lien which bound the cargo prior to the sale was a possessory or non-possessory lien.
4. Accordingly, CCS was entitled to be paid out of the proceeds of the sale up to the amount of the debt by reference to which the lien was exercised.

...the case indicates that the rights of a lienee may extend beyond the mere right to possession of the cargo, opening up a new avenue through which owners can obtain payment of sums owed by charterers.

BAPTISTE WEIJBURG, ASSOCIATE

Significance

For owners who are chasing recalcitrant voyage charterers for payment, the judgment is significant in two ways:

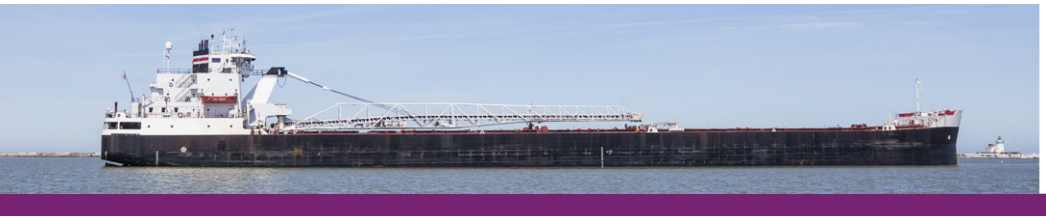
1. Owners can be confident that if the cargo is perishable, or some other applicable ground applies the court will be prepared to order the sale of the cargo under CPR Part 25.
2. The judgment suggests that it may not be necessary for owners to obtain an arbitration/court judgment in order to obtain an order for sale, and that in certain circumstances owners may become entitled to such an order simply by exercising their rights of lien.

HFW's perspective

As the judge found for CCS on the "judgment creditor" grounds, the "lien grounds" are arguably obiter and are not therefore binding authority in respect of the above points. Nonetheless the case indicates that the rights of a lienholder may extend beyond the mere right to possession of the cargo, opening up a new avenue through which owners can obtain payment of sums owed by charterers.

HFW Partner Brian Perrott and Senior Associate Patrick Knox acted for the successful applicant.

For more information, please contact Baptiste Weijburg, Associate, on +44 (0)20 7264 8248 or baptiste.weijburg@hfw.com, or your usual contact at HFW. Research conducted by Marcus Price, Trainee Solicitor.



Sign of the times? Dealing with an impecunious charterer

The poor state of the market over the last few years, and in particular the dry bulk market, has meant that many shipping companies find themselves in financial difficulty. A number of these have become insolvent, or have gone into administration or other protective proceedings, with the latest being Daiichi Chuo, which filed for rehabilitation proceedings in Japan on 29 September 2015. This article provides a general overview of the steps an owner may consider if his time charterer gets into financial difficulty, and cannot pay the hire.

Such agreements can take a number of forms, such as the defaulting charterer "dropping out" of the charterparty chain, or his granting to owners an assignment of his right to receive hire from the sub-charterers.

EDWARD WAITE, ASSOCIATE

Agreement

An agreement as to how the parties affected will deal with the charterers' non-payments can be the most efficient and cost-effective means of resolving the issues. Such agreements can take a number of forms, such as the defaulting charterer "dropping out" of the charterparty chain, or his granting to owners an assignment of his right to receive hire from the sub-charterers. A negotiated solution would require the parties being able to reach agreement on any new arrangement, and this can often be problematic because of the number of entities that could potentially be affected by any change in the contractual arrangements - for example sub-charterers, receivers and, in the case of protective proceedings, the court or its appointed receiver. In most cases no agreement will be possible, and the following courses of action should be considered.

Withholding performance – slow steaming and delaying discharge

Owners could seek to withhold temporarily the services of the ship to try to force payment. Temporary withholding usually involves not proceeding on the voyage, or ceasing cargo operations. This right is only available if there is an express term to this effect in the charter, without which temporarily suspension of the services would be a breach of charter. Owners should also note that, even if they have the right to take this step under the charter, if they deliberately slow steam or delay loading or discharge, this may be a breach of owners' obligations under the bill of lading to undertake the voyage with due despatch.

Lien on cargo

Liening cargo is a further option for the owner, but he will need to make sure that doing so is permissible under local law. It also remains an open question whether an owner may validly exercise a lien where the charter allows it, but the bill of lading does not, and the cargo is not owned by the charterer. In practice, maintaining a lien sometimes means that the owner will have to discharge and store the cargo ashore.

Seeking to intercept subhire or subfreights

Using this remedy, the owner requires his sub-charterer, or other charterers down the chain, to pay the sub-charter hires directly to him. The owner must ensure that the charter enables him to exercise this right for non-payment of hire, rather than subfreight, and that there is an unbroken chain of assignments in the charter chain supporting that right. The lien will only catch sums unpaid at the time the lien notice is received. Practically speaking, the owner should expect that in the immediate term the sub-charterer may well refuse to pay anyone. An owner may also seek to intercept

freight payable under the bill of lading, which requires a separate lien notice to be sent to the shippers and/or consignees.

Withdrawal of the vessel

Most charters contain a contractual option to withdraw if any installment of hire is unpaid. If an owner wishes to take this drastic step, he will need to act promptly, as he may otherwise lose his right to withdraw, and that he fully complies with any grace period notice provisions. Normally, he will also wish to ensure that the vessel is cargo free when exercising his right, since if the vessel is withdrawn with cargo on board, then owners will still be obliged to deliver the cargo to destination under the bill of lading contract. The owner will be entitled to be paid all hire owed up to the time of withdrawal. However, he should also bear in mind that, whilst this area of the law is not yet finally settled, the better view is currently that he will probably not be entitled to damages for loss of charterparty earnings that would have become due after withdrawal.

Termination of the charter

It may also be possible for the owners to terminate the charter. To do so lawfully, an owner will need to be able to show that the charterer will not, or cannot, perform the charter so as to be in repudiatory breach. If so, an owner may accept that breach and end the charter. In that case an owner will be able to maintain a claim for any losses he has suffered in the way of future earnings, for example if the available market rate is lower than the charter rate.

Conclusion

Prior to entering into a charter with a counterparty it is essential to undertake due diligence to ascertain the financial worth of the other party. However, even rigorous due diligence can never rule out the possibility of a charterer counterparty getting into financial difficulty. If this occurs, taking legal advice early will enable an owner to assess the full range of his available options according to his own particular circumstances.

For more information, please contact Edward Waite, Associate, on +44 (0)20 7264 8266 or edward.waite@hfw.com, or your usual contact at HFW.

Related publications

We also recommend to readers the recent briefings detailed below:

Damaging the brand: the impact of bribery by associated persons

One of the main talking points when the UK Bribery Act 2010 (the Act) was first introduced was the new section 7 offence. This introduced corporate liability for failure to prevent bribery by an "associated person" and marked a novel approach under English law to the problem of bribery and corruption on behalf of corporates.

To read more, please visit: http://www.hfw.com/The-impact-of-bribery-by-associated-persons-December-2015

Why are we weighting? Time to act

The implications of the verification of the gross mass of containers — a relatively modest change to the International Maritime Organization (IMO) Safety of Life at Sea Convention (SOLAS) that in essence reiterates the existing responsibility of shippers to declare gross mass accurately — are reverberating through the container supply chain.

To read more, please visit: http://www.hfw.com/Why-are-we-weighting-Time-to-act-January-2016


Conferences and events

Decommissioning & Abandonment Summit
Houston, USA
23-25 February 2016
Presenting: Paul Dean

Superyacht Investor Conference
London, UK
14-15 March 2016
Presenting: Elinor Dautlich, Alistair Feeney and Jay Tooker
Attending: Will MacLachlan, Adam Shire, Tom Willan, Alex Sayegh, Jess Taylor and Lucy Greenish
HFW is sponsoring this event.

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