Comparing notes

At the *ARACON* conference in October, organised by Petrospot and held this year in Rotterdam, one of the sessions provided close scrutiny of many of the legal conundrums relating to bunker supply contracts which have been brought sharply into focus following the collapse of OW Bunker in November 2014.

Unsurprisingly, the session explored the decision in July by the UK High Court to uphold an earlier London Maritime Arbitration Association (LMAA) arbitration in the case of *PST Energy 7 Shipping v OW Bunker Malta Ltd & ING Bank N.V. (*the *Res Cogitans)*. In his ruling, Mr Justice Males dismissed the claim of the owners that OW Bunker and their assignees, ING Bank, could not claim the price of the marine fuel supplied to the *Res Cogitans* because OW Bunker had not paid the physical supplier, and the physical supplier, in holding a retention of title (ROT) clause in its contract, therefore retained property in the bunkers. The owners also argued that OW Bunker's failure to pay the physical supplier had breached s12 of the *Sale of Goods Act*.

In a detailed judgment which set the proverbial cat among the pigeons, Mr Justice Males agreed with the arbitrators that the contract in question was not one to which the *Sale of Goods Act* applied.

At the time of the *ARACON* event, this decision was still under appeal. A few days later, the UK Appeal Court also concurred with the LMAA and High Court judgments, and Paul Taylor of Hill Dickinson provides a further analysis of the ramifications of this decision in this issue of *Bunkerspot* (p.62). At the time of writing, it remains to be seen if the Appeal Court judgment will be referred to the Supreme Court, but for many owners the prospect of paying twice for fuel remains a very real concern.

The *ARACON* session, however, providing a forum for a useful and illuminating exchange of views between the delegates and three lawyers who have expert knowledge of the OW case and also of the 'protection', or otherwise, afforded to suppliers by the incorporation of a choice of national law in their general terms and conditions.

In a lively Q&A session, Paul Taylor of Hill Dickinson, Steve Simms of Simms Showers, and Carel van Lynden of AKD gave their perspectives on what should be included in supply contracts in an attempt to make them as 'OW proof' as possible. Given their respective knowledge of bunker contracts in relation to national jurisdictions – namely the United Kingdom, the United States and the Netherlands – they were able to shed light on other recent and ongoing tussles over OW in other courts of law. They looked at maritime liens, the tensions at play between the retention of title clause in a contract and the recent interpretations of the *Sale of Goods Act*, and they also provided a thorough overview of what interpleader arrangements may – or may not – be able to achieve.

What follows is an edited version

of the exchanges at the session.

Paul Taylor (PT) set the scene from the perspective of English law as it applies to bunker contracts, and he also flagged up some of the key issues in relation to terms and conditions which were then explored further in the subsequent panel discussion.

PT: A principle in English law is privity of contract and in essence this means that there are only contractual rights between the parties to the contract. Ordinarily, in a bunker supply chain you have a number of individuals and OW was no different – there were several OW counterparts in many of the transactions. So normally you would have the physical supplier contracting with OW who in turn enters into a contract with the owners. The supplier provided the bunkers to the owner and there was a bunker delivery note (BDN).

So what does a physical supplier do when it doesn't have a direct contractual relationship with a shipowner? Most bunker supply contracts contain a ROT clause – this is a means of following your goods through to the end party which possesses them. Until such time as you have been paid you still need to trace the goods. That's good as far as it goes, but ROT needs to be brought to the attention of owners or time charterers for it to be effective.

Is a BDN of use to a physical supplier? It could be, but in my view it is not likely to create contractual relationships between owner and supplier. I have seen BDNs which refer to specific terms and conditions but unless those terms and conditions have been brought to the attention of the owner they are unlikely to bind.

A second remedy which has caused some consternation is the maritime lien – in English law the supply of bunkers does not give rise to a maritime lien. In the United States it does, and I understand in Singapore it doesn't.

There are varying effects depending on the law that governs the supply contract as to whether the supplier can assert a right against the bunkers. Irrespective of the contract, he has a direct right *in rem* against the vessel to which the bunkers were supplied.

The problem with OW is the effect of multiple claims. You have a claim from the contracting party, by way of a simple debt claim, but also there is a claim by the physical supplier which is a non-contract claim, either by way of a lateral contract or normally a maritime lien. Even if, as a shipowner, you pay your contractual counterparty that won't necessarily provide you with a defence to a claim from a physical supplier where there is a maritime lien.

Charterers may seek to limit their liability by inserting terms in the charter party or by stamping the BDN with non-lien clause wording. This is good in theory but in practice all the bunker suppliers have done is to insert clauses in their supply contracts which state that the BDN will not be valid. So this, as a means of limiting exposure therefore for a time charterer or owner, may be of limited effect.

> 'Is a bunker delivery note (BDN) of use to a physical supplier? It could be, but in my view it is not likely to create contractual relationships between owner and supplier'

Interpleader proceedings have gained ground in the United States. This is a method which enables a party which says, 'I am ready to pay, but who do I pay? Do I pay my contracting party, do I pay my physical supplier?' simply to say to the claimants: 'You decide among yourselves – I'll commence an action, I will pay money into court and you can argue over it.'

In England, we do not have this method. There is a means by which you could pay monies due into an escrow account but this is voluntary and not binding. So the risk of multiple claims in the English system is still very high.

What a lot of counterparties in the OW scenario have attempted is to raise technical defences – to say that an action for the price being brought by OW will fail because they don't meet certain criteria under the *Sale of Goods Act*.

The *Res Cogitans* is the first test case in England on the nature of the bunker supply contract as a matter of law and we have seen that both the arbitrators and the judges have worked legal gymnastics.

The arbitrators decided that the *Sale of Goods Act* simply didn't apply to a bunker supply contract. It wasn't a contract where property would pass in return for payment. Thus the charge holder did not need to satisfy either of the two clauses in section 49 [of the Act] and their claim was just a simple debt claim. The arbitrators sidestepped the Act altogether.

This went on to appeal to the High Court. The judge, although he recognised that there were inherent difficulties with the Act and there are lots of competing claims from physical suppliers, wasn't going to be swayed by those difficulties. He agreed with the arbitrators and said it was not a contract within the meaning of the Act because bunker suppliers did not agree to transfer title of goods in return for payment.

ROT needn't be a problem if you have goods which aren't going to be consumed. But here, in a bunker context, bunkers are consumed and extinguished very quickly – and that's the problem.

The judge found that because of ROT clauses and consumption of bunkers prior to payment, it meant the property of title in the bunkers couldn't, and didn't, pass to the owners. It was a straightforward claim of debt that was not subject to any requirement as to the passing of property in bunkers to owners at the time of payment.

The English system doesn't have the same mechanisms that exist elsewhere in the world whereby interpleader arrangements and maritime liens [can be used] to deal with these issues of multiple claims.

In respect of the owners' arguments, it was my view at the outset [of the case] before we had these decisions that the arguments themselves might have been technically and legally sustainable but I didn't really think that they were meritorious. I don't mean to be unduly contentious but let's see what happens.

Question: 'How important are stamps on a BDN? Is it not too late in relation to a bunker supplier?'

PT: *It's a good question because it hasn't been legally tested. BIMCO came up with the idea and we can see between owners and charterers that certainly there will be a clause in the charter party. So if, for instance, the attempt to prevent a supplier from asserting a lien by way of stamping this non lien clause proved to be ineffective on the BDN, there would be a claim from the owners against the charterers under the charter party to indemnify them when the vessel gets arrested. So people higher up the chain will clearly be affected.*

The intention on the owners' side is that charterers are going to have to stamp these BDNs because the owners need to protect their vessels. In essence, we see that this is of limited success because already the bunker suppliers are providing against it in their terms and conditions. So will it be successful? Is it too late? You might well be right. It is, however, the best idea that BIMCO has come up with so far.

Question: We have also faced several instances where bunkers suppliers don't allow masters to put any stamps on [the BDN].

Steve Simms (SS)▪*That's when your litigation – your claims – starts to get expensive: when you have not made it absolutely clear to your physical supplier that no stamps are to be accepted on the BDN. We see this all too often – the barge captain will just let the mate put anything on [the BDN].*

It is also important – and this is what has come out in the previous year because of OW – to understand that your terms and conditions are critical to your ability to recover. The Res Cogitans *decision turned on terms and conditions. And another very recent decision –* Canpotex *out of the Federal Court of Canada (a terrific decision which got the supplier the money) – turned on the terms and conditions of the supplier that turned on the terms and conditions of OW* (Canpotex Shipping Services Limited, et al. v Marine Petrobulk Ltd (Federal Court of Canada, 2015 FC 1108, 23 September, 2015)).

A silver lining of OW's terms and conditions was that they incorporated the physical supplier's terms and conditions all the way through.

We have been urging our clients – many of whom are physical suppliers who got tagged by OW and who are what I call downstream of the broker – to look back at their terms and conditions and have a separate set for upstream sales, and to make sure that they become the assignee of the rights of arrest of the upstream suppliers.

If you are a physical supplier, in many countries normally you may not have the rights of arrest, but rights of arrest, at least under US law, are freely assignable. As a condition of you extending credit you can require the broker that you are selling to – or whichever counterparty is up the line – to assign their rights.

You can tie this together with a ROT clause. As a matter of fact you can have a choice of law for specific parts of your contract. You can have an English choice of law for your ROT only – it's not as good in the United States – but a US choice to cover everything else. If that had been the case in Res Cogitans *we probably would not have had the problems that are there.*

And so this is our approach to what I call 'OW proofing' for physical suppliers – and it uses the BDN. And I think Paul is right – there is absolutely a question on the BDN over whether it will bind the shipowner, but from my standpoint it doesn't hurt.

PT▪*Steve, your hybrid option is something that Carel brought to my attention with the NOVE terms.*

Carel van Lynden (CvL)▪*So we have had a view from US law and English law, and it is extremely important which law applies. A ship can be arrested anywhere in the world and then the question is which law will be applied – which rules will actually govern the relationship.*

Most continental European laws do not know the concept of the maritime lien. What we did in the NOVE [The Dutch Association of Independent Bunker Suppliers] conditions (used by many Dutch suppliers) was to insert a clause, as Steve says, where we said that generally Dutch law applies but for the question of whether there is a maritime lien then US federal laws apply.

It has been tested, but not in final judgments yet. There has been a recent Dutch first instance court judgment which deals with a lot of these things. In a judgment of July a ship was arrested for a bunker claim against OW but the bunker supplier said it had a direct claim against a ship and the primary position was that it had a contractual claim because the BDN had a clause that the bunkers were bought on the credit of the ship and the chief signed it. Many other things were also dealt with in that case, but none of them were accepted.

The BDNI is not a contract – the Dutch court just considered it to be a signed receipt for bunkers and in fact the contract was entered into much earlier.

So invoicing to master and owners – I always say to my clients, do it, because you never know where you end up. But under Dutch law this will not create a contractual obligation by the owners because they were not party to the contract.

Also in the terms and conditions, you will see the definitions of the buyer and then everyone is mentioned – the vessel and the owners and the managers. But again, those conditions only apply between the two contracting parties – this is the privity of contract that Paul talked about.

So in the Netherlands this approach doesn't work and you might have to try other means, which we did in the NOVE conditions using this differing of general provisions, with Dutch law applying to the contract, but for the question of a lien you must look at US law.

'If you are a physical supplier, in many countries normally you may not have the rights of arrest, but rights of arrest, at least under US law, are freely assignable'

And so, Stephen, I am very interested to hear whether that would work because there is also case law in the United States where it says if you are not a US supplier and you supply to a non-US company outside of the United States and to a non-US flagged vessel there is no lien, but I know there are also other cases. But I also know that if you don't try then you don't succeed.

In our system also the law of the flag of the ship must allow such a lien to be exercised and if those two conditions are met you can arrest them in evidence and you can take recovery against the ship for your contractual claim against someone else.

SS▪*What you need is as many bullets as you can – and this starts with the basics, such as issuing your invoice to master, owner and supplier. The buyers on the other end – or your downstream suppliers – are smart people and, especially if they are in a distress situation, they are going to have a bunch of bills to pay and they can't pay all of them. So if your contract gives you more leverage than the other guys, you are going to get paid.*

Or let's say the ship pulls into Rotterdam,

and, as Carel says, you don't have many rights here. Then guess what, the ship is probably going to go somewhere else. It might come to Canada, Australia, the Panama Canal – or the United States, where the majority of case law says if you have a US controlling law clause and the ship calls in the United States you have a good chance of arresting it in rem*. And that's an unusual thing in the United States; it doesn't matter whether the owner or the charterer are the same, the ship comes in – that's all that makes a difference – and you might even be able to attach before judgment property of the owner (which is the ship) or the bunkers.*

Question: Can you explain how an interpleader arrangement works?

SS *An interpleader is where somebody – in this case the shipowner – says: 'I know I have to pay for the bunkers, so I am going to throw the money into the court and you guys can fight over it.'*

In theory, it is not a bad idea, particularly if you are a shipowner, because you don't want to pay two or three times.

However, one of the things we are seeing today in the market is that if you are at the broker end your customer is going to say to you: 'I am not paying you until you can prove that you have paid the physical supplier.'

If you are a physical supplier, you will like that. If you are a broker, then it really messes up your cash management. So what the interpleader does is then have everybody fight each other for the money – the physical supplier or the broker.

I don't like that a whole lot because judges, even in the United States, don't understand what an in rem *right is.*

In US law, you have the right, if you are a broker or a trader and you have provided bunkers to a ship, to either arrest the ship or go after your direct customer – it is considered to be a separate thing.

If I can pursue my in rem *right then I have priority over everyone else, particularly in a bankruptcy situation, because I have a claim against the ship, and so OW doesn't matter – they can be as bankrupt as they want to be. But the trouble with interpleaders that we have seen is that the personal claims against OW have got mixed with* in rem *claims against the ship, and the judges are not allowing us to recover on those* in rem *claims.*

We will never ever give up before a physical supplier has to give its money to ING – so there will be appeals of these interpleader proceedings for some time to come!

So what we advise the physical supplier to do now is to 'interpleader proof' your transaction with your terms and conditions. In the Canpotex *decision that is basically what the Canadian court stated. In effect, it said: 'You are interpleader proof – as a physical supplier you have the right to the money, ING doesn't, and so we are going to stop everything right here and the physical supplier is going to get paid.'*

Therefore, in general, if you have an enforced in rem *right you can throw off interpleader proceedings.*

CvL *In the Netherlands and most continental European countries, if you have two people coming in and saying I want the money and I am entitled to the money, then you can put it into the court and they can fight it out. But in this case, this is not what happens, because one has a direct contractual claim and the other has a claim based on another concept of law. So it is not one or the other, but both have a right. There is no uncertainty – the only uncertainty is whether you can fight it in court or not.*

So this concept would actually not work with us.

Question: Does the escrow account option work in a similar way to the interpleader arrangement? If you know you have to pay a bunker bill do you ask your lawyers to create an escrow account and pay your money there, until it is finally known which party you have to pay? OW is costing quite a lot of interest to our company because of the late payment issue.

PT *The escrow option is voluntary, but it is something that I have put forward to clients and I have discussed with ING. ING wanted bank security, and I suggested escrow because the interest provisions in the OW general terms and conditions are draconian – 3% per month compounded monthly.*

There are a lot of owners out there waiting to see if the tide might turn in the case of the Res Cogitans *but ultimately, if they are not successful they will find that their interest is as much as the principal. And they are often not very large sums of money – the supplies we are talking about might be 30-40 tonnes each time. You might be talking about $300,000-$400,000 but these sums are being doubled with interest.*

Escrow is a method which works – well, not with ING – but in principle, where you have bunker supply contracts subject to English law and therefore there isn't the same risk of maritime lien, it can work.

The interesting thing that I hear from these interpleader discussions with Stephen and Carel is that it should be a mechanism to assist but the courts in the United States are interpreting it as a holistic answer when in fact it is merely supposedly dealing with contractual claims – the in rem *claim could be bought entirely outside of the interpleader.*

But coming back to the NOVE terms, I think that is very clever and it could work because we have seen that the Australian courts are prepared to implement that type of hybrid. You have got an arrest which has been upheld in Australia subject to the rights of maritime lien that arise from US law and that were built into the general terms and conditions – even where there is absolutely no connection with the United States in the case in point. The Australian court faced jurisdiction arguments raised by the other side but the court said, no, the jurisdiction here in Australia is made out and the maritime lien is clearly made out as a matter of US law.

SS *I think we will see this more and more. Australia and Canada have picked this up and I think that Panama will follow, and so a US choice of law clause is essential. At the same time, a UK choice of law clause is something that the* Res Cogitans *case is showing will cause you some problems. So if you don't do anything else, look at your terms and conditions and find out which choice of law is included in them.*

> 'What we did in the NOVE conditions used by many Dutch supplier was to insert a clause where we said that generally Dutch law applies but for the question of whether there is a maritime lien then US federal laws apply'

Question: Do you have any advice for owners in the OW case? Who should we pay?

PT *I recognise that the bunker suppliers are always trying to be one step ahead of the owners, so whereas the owners want to implement non lien clauses it is the bunker suppliers who are already excluding them. So it comes back to the bargaining power that you have.*

Owners are probably in a better position with UK law than they are with US law because they are not as exposed in terms of maritime liens, and their vessels are not likely to be arrested if the bunker supply contract is not subject to US law.

But in terms of actually getting interpleaders off the ground or agreeing who they should pay, that remains a real difficulty for owners and I think we all recognise that.

CvL *There may also be another legal reason why you as an owner would have to pay, because the bunker supplier will say I supplied bunkers which at the end of the day were used by you and only you could make money because I supplied these bunkers and I haven't been paid – you as the owner have been unjustly enriched because you used the bunkers without paying the supplier. This argument is presently pending in the Dutch courts – whether the 'bunkers enrichment concept' is sufficient ground to create a direct claim again the owner. I don't know if that would work with you in England?*

PT *It could but I suppose my solution for any owner is only trade with a physical supplier!*

SS *That is a good solution! Another solution is one that Hapag Lloyd has employed.*

Hapag Lloyd has its own bunker sales terms and conditions and so it tells brokers or suppliers that it will pay them when they present the receipt of their payment to their physical suppliers. Some people will sell on that basis, but you, as a broker or a trader or a supplier, always have the chance to say no.

Question: Another form of protection, when you use a broker or trader, is a payment confirmation letter. This means the supplier and the trader are the only parties, not as in the OW situation where there are many parties. This means that the supplier gives a letter stating that the trader has paid in full and so in this way the owner has peace of mind.

We have been doing this for the past two years – but know your traders, know the company they represent, be sure it is the only party involved and that you don't have two or three traders back to back, and know which suppliers they use even before fixing the bunkers.

PT *This is excellent management. Due diligence and counterparty risk assessment would be essential to such a scheme, and I think that we as lawyers find ourselves in situations where the links in the chain have not been subject to that level of scrutiny and, sadly, there has not been that level of dialogue and communication between the parties.*

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