Standard Bulletin

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Board meeting 27 January 2009

The board met in Paris on 27 January 2009 and reviewed the club's overall business and outlook, and considered a number of matters concerning the current renewals.

New directors

We are delighted to report that Giulio Bozzini of Saipem and Bruce Chan of Teekay were elected to the board.

Renewal progress

We are in the throes of renewal as this issue goes to press. No renewal in recent history has ever been easy, but this time the renewals are taking place against a backdrop of exceptionally difficult conditions in the freight markets, particularly for dry cargo operators. It is never welcome to ask members for higher premiums, but we are committed to keeping the club in a good financial state. We are receiving good support from the membership, for which we are grateful, and are also receiving a number of enquiries for membership from other owners. Our aim at this renewal is to maintain the underlying strength of the club and to keep the club's development moving in a positive way.

Financial position

The board reviewed the club's financial position. It goes without saying that the club's investment portfolio has suffered losses in the last few months of financial 'meltdown', but at the same time, the underwriting performance has been slightly better than expected. The free reserves are expected to be down at 20 February 2009 from their record high level at February 2008, but the forecast free reserves are expected to still be sufficient, and the board determined that no supplementary premiums are expected to be needed for any open policy year. The release call levels were reaffirmed unchanged.

Club assistance

In these difficult freight markets and economic conditions, the club's services, particularly in the Defence Class, are proving to be greatly in demand. The club is helping many owners to assess their legal position under contracts and to take appropriate action against counterparties to secure their legal position. Usually, the legal position is not complicated - the problem is financial and that of counterparty risk - and, in these circumstances, a pragmatic rather than a strictly legal approach is usually more effective. But there are no easy solutions in such unprecedentedly difficult economic conditions.

Reinsurance

There will be an increase in the reinsurance rates for all ship types this year. This results from a deterioration in the reinsurance record over the last three years, with underwriters on the first layer of the reinsurance contract suffering losses. The reinsurance rate increases are being allocated to reflect the record of different ship types, with dry cargo ships (unfortunately when their market is so difficult) shouldering a relatively larger proportion of the extra cost than tankers, whose record is better at the moment.

US voyage surcharges

The system will continue for a further year but with reduced levels of surcharge.

In This Issue

Rules

The additional changes to the rules were approved by the membership and will take effect from 20 February 2009.

Limits and deductibles

Cover limits for the 2009/10 policy year are unchanged. The board approved increases to standard deductibles, and renewals will include increases to deductibles where they are currently low.

War risks and biochem

Cover remains as before, on the same terms and with the same limits.

Outlook

The club has good underlying fundamentals and is focused on helping its members in critically difficult economic times. We believe that the club will go into the 2009/10 policy year in good shape to continue to provide its members with the quality of service and security that they are entitled to expect.

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US Environmental Protection Agency (EPA) Vessel General Permit (VGP) requirements

In the *Standard Bulletin* dated 1 December 2008, we advised that all foreign flagged commercial vessels of 79 feet or longer, operating within US waters, will become subject to the US Environmental Protection Agency (EPA) final Vessel General Permit (VGP) requirements regarding the discharge of pollutants incidental to their normal operation.

The EPA was granted an extension to 6 February 2009 as the effective compliance date of the new regulation. This means that the current exemption for ship discharges remains in place until 6 February 2009, following which, under Section 1 of the permit, the industry will have a further two weeks, until 19 February 2009, to implement discharge inspections, training and record keeping requirements.

On 19 December 2008, the EPA issued the final VGP requirements and, although the implementation date has been extended, members whose ships will be calling at US ports are strongly recommended to ensure compliance with the requirements found in the finalised EPA VGP as soon as practicable.

General information

To obtain permit authorisation, the owner or operator of a ship that is either 300 or more gt or has the capacity to hold or discharge more than 8 cubic metres (2,113 gallons) of ballast water, is required to submit a Notice of Intent (NOI) to receive permit coverage from 19 June 2009 but no later than 19 September 2009.

NOI can be submitted through the EPA website by registering for an account at http://edx.epa.gov/warning.asp, and following the 'vesselNOI' link.

Until 19 September 2009, these ships will automatically be authorised upon permit issuance to discharge according to the VGP requirements. For ships that were delivered to the owner or operator on or before 19 September 2009, the ship will receive permit coverage on the date that the EPA receives the complete NOI. New ships that are delivered after 19 September 2009 will receive permit coverage 30 days after the EPA receives the complete NOI.

Ships that are less than 300 gt or are able to carry or discharge no more than 8 cubic metres of ballast water are not required to submit a NOI and will automatically be authorised to discharge according to the VGP requirements.

The electronic NOI filing system is expected to be operational by late spring 2009. In addition, the EPA will require a one-time permit report containing additional ship information for each ship within 30 to 36 months after obtaining coverage under the VGP.

Failure to meet any requirement of the VGP will constitute an enforceable permit violation. The EPA has included reporting requirements in the VGP that ensure that it, and other parties as necessary, are made aware of potential permit violations. All ships equipped with ballast tanks that operate in waters of the US must continue to meet the reporting requirements of 33 Code of Federal Regulations (CFR) 151.2041 and the record keeping requirements of 33 CFR 151.2045 regarding ballast water discharges.

The VGP details other spills and unauthorised discharges which must be reported to the EPA within 24 hours of the ship becoming aware of the discharge, should it endanger health or the environment.

Otherwise, under the VGP, shipowners / operators must report all incidents of non-compliance with the permit at least once a year to the appropriate EPA regional office.

The EPA may not issue a permit authorising discharges in the waters of a State until that State has granted certification under the Clean Water Act (CWA) or has waived its right to certify. As of the issuance date of the permit, the States of Alaska and Hawaii have not yet granted, denied or waived certifications pursuant to the CWA, so the permit does not yet provide coverage in these jurisdictions. The EPA will announce the availability of coverage under the VGP discharges in these jurisdictions as soon as it receives the appropriate certifications or waivers. It should be understood that compliance with discharge standards in individual states will be mandated in this manner, in addition to Federal standards.

Summary of significant changes from proposed VGP to final VGP

The final VGP addresses 26 ship discharge streams by establishing effluent limits, including Best Management Practices (BMPs), to control the discharge of the waste streams and constituents found in those waste streams. A list of these are provided on our website. For each discharge type, among other things, the final permit establishes effluent limits relating to the constituents found in the effluent, including BMPs designed to decrease the amount of constituents entering the waste stream.

The final VGP differs from the proposed permit in several ways. These changes include:

- modifying the greywater discharge requirements for existing medium-sized cruise ships unable to voyage more than 1 nautical mile from shore
- adding requirements for the discharge of pool and spa water from cruise ships
- prohibiting the discharge of tetrachloroethylene degreasers
- expanding the prohibition against discharge of tributyltin to a prohibition against discharge of any organotin compounds
- the addition of whole effluent toxicity testing to the requirements for ships employing a ballast water treatment system that discharges certain biocides

Other changes include combining three discharge categories into a new category that includes all oil-to-sea interfaces, modifying discharges and limits for large ferries, and additional clarifications added to several cruise ship discharges.

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Legal update

Letters of Indemnity

Farenco Shipping Co Ltd v Daebo Shipping Co Ltd (The "Bremen Max") [2008] EWHC 2755 (Comm)

This judgment delivered by the English High Court on 11 November 2008 is a reminder to shipowners holding letters of indemnity (LOI) that they should obtain verification from charterers that the person requesting delivery of the cargo is the party named in the LOI.

Facts

The Bremen Max was chartered by her owners on an amended NYPE form to Cosco Bulk Carrier (Cosbulk). The ship was sub-chartered under a chain of back-to-back charters. Each charterparty provided an obligation upon the owners 'to allow discharge and release the cargo' without production of the bills of lading against a LOI issued by the charterer.

In March 2008 a cargo of blast furnace feed was loaded in Brazil for delivery to Bourgas, Bulgaria. On arrival of the ship, each charterer provided a LOI to its disponent owner, to permit the delivery of the cargo to Kremikovtzi A.D. (a Bulgarian steel producer) without production of the bills of lading. Each letter was in the same form, based on the standard wording recommended by the International Group of P&I clubs, and stated that charterers would "provide on demand such bail or other security as may be required to prevent such arrest... or to secure the release of such ship"

Stemcor UK informed the owners that they were the holders of the bills of lading and arrested the ship in order to obtain security for its claims for misdelivery, in the sum of $11m. On the same day, the owners put up security and the ship was released. The owners subsequently obtained a Rule B attachment order in New York against Cosbulk's assets. Cosbulk's sub-charterer, Farenco Shipping (Farenco) put up security to Stemcor in order to prevent the possibility of Cosbulk obtaining a similar order against them. This request was passed down the line of charterers.

High Court proceedings

Farenco applied to the High Court for an order requiring sub-charterers to honour their obligations under the LOI. The ultimate sub-charterers argued that they were only required to put up security to prevent the arrest of the ship or secure her release and that this was impossible in the present case since the ship had already been released.

Decision

The High Court rejected this argument as being contrary to the intention and commercial purpose of the LOI; which was that the shipowner should not have to suffer the arrest of the ship and that any security to prevent its arrest should not be put up by the shipowner but by the charterer. Although the action of the owners in putting up security had the effect of ending the detention of the ship, it did not discharge the obligation of the charterers to put up security.

Under the charterparty it was the charterer's responsibility to discharge the cargo, but it was the shipowner's responsibility to release, in the sense of deliver the cargo, to another ashore against the LOI. The charterparty did not identify the person to whom delivery should be made. The LOI provided for the charterer to identify that person in the LOI.

The charterers identified Kremikovtzi as the receiver to whom delivery should be made. The LOI therefore contained a request to deliver the cargo to Kremikovtzi and an agreement by the shipowner to comply with that request in return for undertakings given by the charterer. The Judge commented that the shipowner need not enquire into whether the named receiver in the LOI is entitled to possession of the goods. He only needs to know that the person to whom he delivers the goods is the person to whom the charterer has requested that delivery be made.

Comment

This decision places the burden of proof upon owners to ensure that they know to whom they are delivering the cargo. A shipowner holding a LOI requesting delivery to a particular party should if there is any doubt as to whom the delivery should be made, seek clarification from the charterers and confirm this in writing.

Members are reminded that under the club's rules, cover for cargo claims is discretionary when delivery is made without production of the original bills of lading.

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The VGP also requires routine self-inspection and monitoring of all areas of the ship that the permit addresses. The routine self-inspection must be documented in the ship's logbook. Analytical monitoring is required for certain types of ships. The VGP also requires comprehensive annual ship inspections, to ensure even the hard-to-reach areas of the ship are inspected for permit compliance.

The permit imposes additional requirements for eight specific types of ships that have unique characteristics resulting in discharges not shared by other types of ships. These ship types are medium and large cruise ships, large ferries, barges, oil or petroleum tankers, research ships, rescue boats, and ships employing experimental ballast water treatment systems.

Further information on the VGP requirements, including the final VGP, can be accessed at: http://cfpub.epa.gov/npdes/home.cfm?program_id=350

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Legal update

Exclusion of consequential damages in offshore contracts even if caused by negligence

Sea Servizi Ecologici Affossamenti v. Muliceiro Servicos Maritimos [2007] EWHC 2639 (Comm)

This case is an addition to the limited case law on the interpretation and scope of the exclusion clause in the Supplytime '89 form. One of the main issues in this case related to the interpretation of clause 12(c) of the Supplytime '89, which provides:

"Consequential damages – Neither party shall be liable to the other for, and each party agrees to protect, defend and indemnify the other against, any consequential damages whatsoever arising out of or in connection with the performance or non-performance of this charterparty, including, but not limited to loss of use, loss of profits, shut in or loss of production and cost of insurance."

This case came before the High Court by way of an appeal from an arbitration award where the arbitrators found, upon determination of a preliminary issue, that the claims of the Charterer under the Supplytime '89 contract was excluded by Clause 12(c). The owners and charterers entered into a Supplytime '89 charterparty for a vessel that was to be used in pipeline post-trenching operations performed by the charterers for Petrobras. Among the charterers' claims was a claim for the loss of future business with Petrobras as a result of alleged negligence and breaches of contract by the owners under the charter. In the arbitration, the charterers accepted that the damages claimed relating to the loss of business of the project were consequential damages. Clause 12(c) was accordingly potentially engaged. The charterers argued, however, that the exclusion in clause 12(c) did not apply where the consequential damage had been caused by negligence.

In the arbitration, the arbitrators held that clause 12(c) covered cases even where consequential damages had been caused by negligence. The charterers appealed.

At the hearing before Mr. Justice Andrew Smith, the charterers relied on *Canada Steamship v. The Crown* [1952] AC 192 and argued that where negligence is not expressly excluded (as in the case of clause 12(c)), the exclusion may nevertheless be wide enough to exclude the consequences of negligence, but that that would only be so in cases where liability could arise only through negligence. This argument was rejected by the judge, who held that such a distinction only makes sense if there is a distinct liability for negligent and non-negligent breaches that the parties could reasonably be supposed to have decided to distinguish. For this particular contract, i.e. the Supplytime '89 form, where the clause on its face is directed to any and every breach of contract arising out of, or in connection with performance or non-performance of the contract, he found that the exclusion clause covers the scenario even where liability results from negligence.

Implications of this decision

There have been several attempts to qualify or restrict the operation of the knock-for-knock and exclusion clauses in the various Supplytime / Towhire / Towcon forms, which have failed. An example is the unreported case of *Smit International (Deutschland) GmbH v. Mobis and another (the "Janus")* [2001] decided before the English High Court, where one party tried to argue that the knock-for-knock provision in clause 18(2) of the Towhire Form did not apply if the vessel was unseaworthy. This was rejected by the English High Court. This case is another example where the court has once again protected the scope and effectiveness of the exclusion clause in these standard forms.

It is clear from this decision that claims for consequential damages will be excluded even if the liability resulted from negligence and the main focus when it comes to clause 12(c) is to determine whether the losses claimed falls within the definition of consequential damages as defined in clause 12(c). The emphasis therefore will be on the type of damage that has been sustained and claimed, rather than on how the damage has been sustained or caused. It should be mentioned, however, that one of the other issues raised by the charterers before the court was whether clause 12(c) would operate even if the consequential losses were a result of the unseaworthiness of the vessel, but this issue was not pursued. It remains to be seen therefore whether unseaworthiness of a vessel will defeat the operation of the exclusion clause.

Club News

The 2008 Standard Asia offshore forum and member training

The third Standard Asia Offshore Forum was held on Thursday 11 December 2008 in Singapore. The morning sessions included discussions regarding the overlap between poolable and non-poolable P&I cover and construction all risks (CAR) insurance, an overview of the report into the *Bourbon Dolphin* incident, and a presentation by Patrick Foss of Barlow Lyde & Gilbert on risk and insurance issues in offshore contracts.

During the afternoon, the club and Barlow Lyde & Gilbert presented a workshop examining in more detail how weaknesses in contract drafting can adversely affect the parties' liability and insurance position, in the aftermath of a claim arising on an offshore construction project.

In conjunction with the offshore forum, the club hosted training for members. Topics covered included defence cover, personal injury, cargo, collision and pollution issues. There was also a presentation from Ed Ion of Helix Media and presentations and a workshop on a major casualty scenario from Holman Fenwick Willan.