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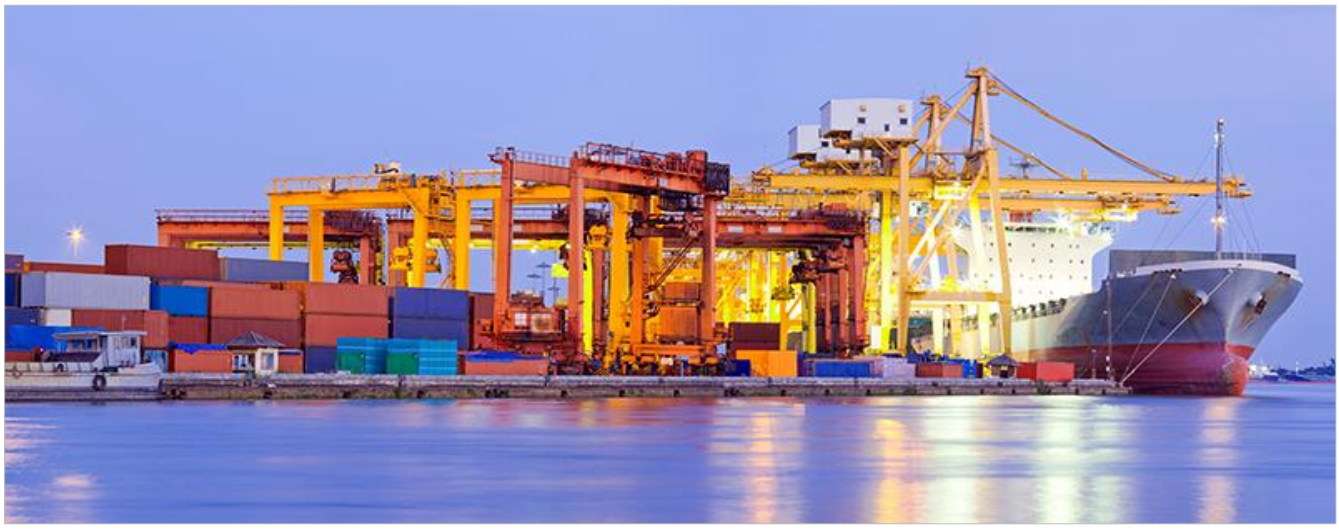

Cover Story

Must a Carrier First Disprove Negligence in order to Rely on the Defences under the Hague Rules?

Introduction

In the recent case of *Volcafe & Others v CSAV* [2016] EWCA Civ 1103, the English Court of Appeal has considered the much-debated question of whether a carrier can rely on the defences under Article IV Rule 2 of the Hague Rules when confronted with an allegation of breach of Article III Rule 2 by way of negligence. In that case, the Court has clarified that a carrier does not first need to disprove negligence before it can rely on the defences under Article IV Rule 2 of the Hague Rules.

The Facts

In 2012, the defendant carrier carried 9 consignments of Columbian coffee beans from Buenaventura, Columbia to various ports in Northern Europe. The Hague Rules were incorporated into the bill of lading for each consignment. Pursuant to the said bills of lading, the carrier was responsible for preparing and stuffing the bags into the containers. After preparing and stuffing the containers, the containers were then moved to the export area and loaded onto vessels during the period from January to April 2012.

According to the bills of lading, the shipments were in apparent good order and condition when loaded. However, upon discharge, the bags in all but two of the containers were found to have suffered some degree of condensation damage.

As a result, the cargo owners filed a cargo claim against the carrier to claim for damages on the basis that loss and damage were suffered by them as a result of the condensation damage which was caused by the negligence of the carrier. Further or alternatively, the cargo owners claimed that the carrier was in breach of its obligation to under Article III Rule 2 of the Hague Rules.

The Relevant Provisions in the Hague Rules

The relevant provisions in dispute were Article III Rule 2 and Article IV Rule 2 of the Hague Rules.

Article III Rule 2 provides that:

> *"Subject to the provisions of Article IV, the carrier shall properly and carefully load, handle, stow, carry, keep, care for, and discharge the goods carried."*

Article IV Rule 2 provides that:

> *"Neither the carrier nor the ship shall be responsible for loss or damage arising or resulting from: …(m) wastage in bulk of weight or any other loss or damage arising from inherent defect, quality or vice of the goods…"*

The cargo owners argued that the carrier was in breach of Article III Rule 2 in causing the condensation damage, whilst the carrier sought to rely on the exception set out in Article IV Rule 2 as its defence.

The First Instance's Decision

At first instance, David Donaldson QC ruled in favour of the cargo owners and held that the defendant carrier must establish inherent vice or inevitability of damage and to disprove negligence before it can rely on Article IV Rule 2. He considered that there was "complete circularity" between Article III Rule 2 and Article IV Rule 2 such that Article IV Rule 2 was not in any real sense a true exception.

In the circumstances, he held that the carrier failed to disprove negligence. He also held that the carrier was unable to demonstrate a "sound system" for shipping the cargo because, among others, it had failed to adduce evidence of a suitable empirical study that a particular weight and/or type of paper was sufficient in practice to prevent damage throughout the carriage. In addition, he rejected the carrier's argument that it can rely on the alternative defence of inevitability of damage. As a result, the defendant carrier appealed.

The Court of Appeal's Decision

The Court of Appeal had unanimously overruled the first instance's decision and allowed the carrier's appeal. Below are some key issues that the Court of Appeal had addressed in its judgment:-

Burden of Proof

Regarding burden of proof, the Court of Appeal rejected the approach of the first instance and held that once the carrier has shown a prima facie case for the application of the exception of inherent vice in Article IV Rule 2, the burden shifted to the claimants to establish that the exception did not apply because of the carrier's negligence.

In reaching such conclusion, the Court of Appeal placed much emphasis on the common law principle that "he who alleges must prove". Mr. Justice Flaux, who gave the leading judgment, said that the question of whether there was some inherent defect, quality or vice in the cargo (on which the burden of proof is on the carrier) is anterior to the question whether there was negligence on the part of the carrier or breach of the duty to properly and carefully care for and carry the cargo (on which the burden is on the claimant to disprove the operation of the exception).

Inherent Vice

The Court of Appeal was also of the view that the judge at first instance was wrong to equate the concept of "inherent vice" with that of "inevitability of loss". In Mr. Justice Flaux's view, "inherent vice" encompasses damage caused by the inherent

qualities of an otherwise normal cargo, which not the same as “inevitability of loss”.

In light of the above, the Court of Appeal held that although the cargo owners had established their case in the present case, the carrier had also made out a defence on the basis of inherent vice under Article IV Rule 2 based on the expert evidence given. The onus therefore fell on the cargo owners to establish negligence on the part of the carrier. The Court of Appeal held that the cargo owners failed to show that the carrier was negligent during the carriage.

Sound System

Regarding the issue of “sound system”, the Court of Appeal held that the first instance’s decision was misdirected as to the correct interpretation of whether a system is “sound” for the purposes of determining whether a carrier was in breach of its obligation to properly care for and carry goods under Article III Rule 2. In Mr. Justice Flaux’s view, the first instance had adopted an “overly rigorous approach” which “overstated to a considerable extent what was required for a sound system”. In particular, he criticized the first instance’s requirement for a scientific calculation or empirical regarding the sufficiency of lining in that it imposed a standard that went beyond what the law requires.

On the facts of the present case, the Court of Appeal was satisfied that the carrier had adopted a “sound system” by using kraft paper to line container surfaces, which was a widely accepted practice in the container industry.

Temporal Applicability of the Hague Rules

Last but not least, whilst noting that the parties were free to determine what acts or services fell within the operation of “loading” for which the Hague Rules would apply, the Court of Appeal confirmed the first instance’s decision in relation to the temporal scope of the Hague Rules, and held that the Hague Rules also apply to the stuffing of the containers by the carrier’s stevedores at the container yard. The carrier’s appeal in this regard was therefore rejected.

Conclusion

The Court of Appeal’s decision in this case is welcome as it clarified the operation of the burden of proof in cargo claims where the Hague Rules apply. It is now clear that a carrier does not first need to disprove its own fault or negligence in order to rely on the defences under Article IV Rule 2 of the Hague Rules. Cargo claimants are required to positively establish negligence on the part of the defendant carriers.

This case also provides valuable guidance on the scope of the inherent vice defence and the test for assessing of whether a system is “sound” for the purposes of determining whether a carrier is in breach of its obligations to properly care for and carry the cargo under Article III Rule 2.

In light of the above, it is important to ensure that there is sufficient contemporaneous evidence of the conditions of the cargo both on shipment and on arrival. If the cargo was indeed shipped according to the standard industry practice, it would be difficult for cargo owners to prove negligence on part of the carrier to prevent the carrier from relying on the defences under the Hague Rules.

APL launches weekly service linking New Zealand to North Asia

The Singapore-based container shipping company APL has recently launched a new weekly service called "New Zealand Express II" ("**NZ2**"), linking New Zealand and North Asian ports. The new NZ2 service includes calls at five ports in New Zealand to provide a broad coverage in the Oceania Trade Lane. With the launch of the new service, APL said it would offer a network of six Oceania Services to connect Asia with Australia and New Zealand.

The inaugural trip of NZ2 was commenced from Shanghai on 29 December, 2016. The NZ2 service calls the ports of Shanghai, Ningbo, Chiwan, Kaohsiung, Brisbane, Auckland, Chalmers, Lyttelton, Napier, Tauranga, Hong Kong and Keelung. "APL introduced the new NZ2 service to serve the China-New Zealand market in a direct and more efficient way", said Tonnie Lim, APL's head of Intra-Asia trade.

Koch gets another Diana vessel on time charter

The Singapore-based Koch Shipping has entered into a time charter contract with Diana Shipping Inc., a global shipping company specialising in the ownership of dry bulk vessels for one of its capsize dry bulk vessel Seattle. Seattle is a 179,362 dwt vessel built in 2011. The gross charter rate is US$11,700 per day, minus a 5% commission paid to third parties, for a period of 14 to 17 months. The charter is expected to commence on 6 February 2017.

According to VesselsValue data, this deal increases the total number of Koch Shipping's vessels under time charter to seven capesizes and one ultramax vessel. It is expected to generate approximately a minimum of US$4.91m of gross revenue for Diana Shipping Inc.

Cosco Shipping new semi-submersible to serve Shell deep-water drilling project

The Shanghai-listed Cosco Shipping Specialised Carriers ("**Cosco**") has just taken delivery of its new semi-submersible ship, the 98,000 dwt "*Xin Guang Hua*", which will participate in Shell's Appomattox deep-water oil drilling project in the Gulf of Mexico. Built at Guangzhou Shipyard International, the ship is currently the world's second largest semi-submersible ship. It can drive to a depth of 30.5m and load units up to 10,000 tonnes. It features an unobstructed deck space of up to 211m by 68m.

Han Guomin, the chief executive of Cosco states that "despite an overall weak market due primarily to low oil prices, Cosco is encouraged by the reception this vessel has received from the market". He believes that the vessel can meet the demands for the uprising trend of manufacturing modules as well as for deepwater oil and gas developments.

Jinhui offloads property assets for US$12.6m

In order to improve liquidity, the Hong Kong-listed Jinhui Holdings ("**Jinhui**") has recently entered into two transactions to dispose of two of its property assets to Vantage Asia Ltd ("**Vantage**") for a total sum of HK$97.5m (US$12.6m).

The first transaction was between Vantage and Fair Group International, a wholly owned subsidiary of Jinhui, for the sale and purchase of Jinhui's offices in Hong Kong for a sum of HK$94m. The second transaction was between Vantage and Star Board Investments, which Jinhui holds 55% of its shares, for the sale and purchase of a car park for a sum of HK$3.5m. Based on the value of the assets, Jinhui is expected to book HK$13.4m and HK$1.8m gain from the sale of the two properties respectively. The net proceeds will be used as general working capital for the group.

Transgrain Shipping (Singapore) Pte Ltd v Yangtze Navigation (Hong Kong) Co Ltd

[2016] EWHC 3132 (Comm), Queen's Bench Division, Commercial Court

* *

This is an appeal from an LMAA arbitration award regarding the proper construction of clause 8(d) of the Inter-Club Agreement 1996 (the "**Clause 8(d) of the ICA**") which had been incorporated into the New York Produce Exchange Form charterparty.

The claimants (the "**Owners**") were the owners of a vessel called *Yangtze Xing Hua* which they chartered to the respondents (the "**Charterers**"), for a time charter trip carrying soya bean meal from South America to Iran. The charterparty was on the New York Produce Exchange Form. The Charterers had delayed in discharging the cargo at the discharge port in Iran for over 4 months because they were not being paid by the receivers. When the cargo was finally discharged in May 2013, it was found to be damaged due to overheating. The receivers made a claim against the vessel for Euros 5 million and finally settled with the Owners in the sum of Euro 2,654,238. The Owners claimed that sum together with hire in the sum of US$1,012,740 from the Charterers.

It was the common ground between the parties that the liability was to be settled in accordance with Clause 8(d) of the ICA, which provides for a 50/50 liability split between the Owners and the Charterers unless there is clear and irrefutable evidence that the claim arose out of the act or neglect of either one of the parties. The arbitral tribunal held that the Charterers' decision to withhold the cargo in the vessel was an "act" falling within Clause 8(d) and therefore should bear 100% liability. The Charterers appealed against the tribunal's decision, and the issue before the Court was whether the term "act" under Clause 8(d) meant a culpable act or simply any act, whether culpable or not.

Teare J rejected the Charterers' argument that the words "act" or "neglect" had equivalent or complementary meaning, so that "act" requires a sense of fault. Teare J was of the view that the meaning of the word had to be construed with regard to the language of the ICA as a whole, which was designed to solve insurance problems but not problems concerning moral culpability. As such, the word "act" was to bear its ordinary and natural meaning without regard to any element of fault, and the Court upheld the tribunal's decision and dismissed the Charterers' appeal.

Oldendorff GmbH & Co Kg v Sea Powerful II Special Maritime Enterprises; Oldendorff Carriers GmbH & Co Kg v Scit Services Ltd; Scit Trading Ltd v Xiamen C&D Minerals Co Ltd (The "MV Zagora")

[2016] EWHC 3212 (Comm), Queen's Bench Division, Commercial Court

This claim concerned a series of letters of indemnity issued for the discharge of cargo in China without presentation of the original bill of lading. A cargo of iron ore was shipped by the vessel "*Zagora*" from Australia to China. A series of indemnities down the charterparty chain were given in respect of delivery of the cargo of iron ore. The cargo of iron ore had been delivered without presentation of the bill of lading. When the Bank of China brought a claim of mis-delivery as holders of the original bill of lading, the shipowners called on their indemnity pursuant to the letter of indemnity (the "**LOI**") from the charterers who made a similar claim on the indemnity from the receivers.

Pursuant to the LOI, the nominated receiver was Xiamen C&D Minerals Co Ltd ("**Xiamen**"). In other words, the LOI required delivery of the cargo to Xiamen or an agent of Xiamen. However, delivery was made to Rizhao Sea-Road Shipping Agency Co. Ltd. ("**Sea-Road**"), an agent of Xiamen's sub-purchaser. It was therefore argued that the LOI and the other indemnities were not enforceable as delivery had not been made to the nominated receiver.

Teare J held that the indemnities were enforceable because Sea-Road, whilst being an agent of Xiamen's sub-purchaser, is also an agent of Xiamen. This is because it was more likely than not that Xiamen intended Sea-Road to take delivery of the cargo on Xiamen's behalf, in order to keep it until delivery to the ultimate buyers, and that Sea-Road was aware of that intention and accepted that it was acting on behalf of Xiamen when it took delivery of the cargo from the shipowners. Conversely, the shipowners had no interest in discharging the cargo into the possession of Sea-Road as their own agent, as this would not invoke the protection under the LOI because it would mean that the shipowners have retained possession of the cargo through Sea-Road. In light of the above, Teare J concluded that the cargo was delivered to Xiamen through the agency of Sea-Road as required by the LOI. The LOI as well as the other indemnities down the charterparty chain were enforceable in the circumstances.

Regulus Ship Services Pte Ltd v Lundin Services BV and another

[2016] EWHC 2674 (Comm)

* *

By an ocean towage contract on BIMCO Towcon terms dated 21 August 2012 (the "**Contract**"), Regulus agreed that its tug, the "AHTS Harmony 1", would tow the FPSO "IKDAM" from Tunisia to Malaysia, on behalf of Lundin. There is an express term in the Contract that the "IKDAM" would be in "light ballast condition". Regulus brought the present proceedings against Lundin claiming (i) that Lundin was in breach of the Contract by providing "IKDAM" in heavy ballast condition, as a result of which Regulus incurred excess fuel, port demurrage charges and miscellaneous expenses; and (ii) for delay payments pursuant to Clause 17(a)(ii) of the Contract. On the other hand, Lundin argued that Regulus was in breach of an implied obligation (or a collateral agreement) under the Contract that the convoy would maintain an average speed of 4.5 knots, and counterclaimed damages against Regulus in respect of the alleged breach. Further, Lundin counterclaimed against Regulus for the hire of the substitute tug and its associated costs as a result of Regulus' repudiation breach of the Contract.

Accordingly, there were four main issues before the court: (i) what is the meaning of a requirement for a tow to be in "light ballast condition" for the purposes of towage operations ("**Issue 1**"); (ii) what is the scope and effect of clause 17(a)(ii) of the Contract in relation to the tugowner's entitlement to contractual delay payments ("**Issue 2**"); (iii) whether Regulus was in breach of the implied term of the Contract by its failure to maintain an average speed of 4.5 knots ("**Issue 3**"); and (iv) whether Regulus was in repudiatory breach of the Contract ("**Issue 4**").

Regarding Issue 1, Lundin argued that in order to be in "light ballast condition", a tow must not only be physically safe, but must also be legally fit for the towage. This would include being insured for the voyage which would also entail compliance with the requirements of the marine warranty surveyor (and any ballast conditions the surveyor deemed necessary) and within the vessel's class. Phillips J rejected Lundin's argument in this regard and held that the proper test was that the light ballast condition was concerned with ensuring physical fitness, primarily stability, for the tow's voyage. Phillips J held that the "IKDAM" was not in "light ballast condition" as required under the Contract. However, Phillips J was of the view that Regulus has not proved that Lundin's breach of its obligation to provide the "IKDAM" in "light ballast condition" has caused any delay to the voyage, and

therefore Regulus was only entitled to nominal damages in respect of Lundin's breach of the Contract.

Regarding Issue 2, Phillips J rejected Regulus's claim and held that the Clause 17(a)(ii) can only be triggered by a deliberate decision of a tugowner to slow steam when it considers that the tow cannot be towed at the intended speed. In this case, there was no evidence that Regulus made a decision to slow stream. In fact, the tug had attempted to reach the originally contemplated speed and the IKDAM was not incapable of being towed at such speed. It was the tug that could not average that speed using just two of its four engines. It followed that Regulus could not rely on Clause 17(a)(ii) to claim for delay payments.

In relation to Issue 3, Phillips J rejected Lundin's counterclaim and held that based on the facts there was no collateral agreement between the parties, and there was no implied term of the Contract requiring Regulus to maintain an average speed of 4.5 knots as a term will only be implied into a contract if it is necessary to give it business efficacy or it is so obvious that it goes without saying.

Regarding Issue 4, Phillips J held that Regulus was in repudiatory breach of the Contract by sending an email to Lundin indicating that it was withdrawing the "AHTS Harmony 1" from service with immediate effect, and such repudiation was accepted by Lundin in its subsequent email to Regulus. Phillips J held that Lundin was entitled to damages in respect of the additional costs of making alternative towing arrangements as a result of Regulus' repudiatory breach of the Contract.

Conducting Maritime Arbitration in Hong Kong (Part II)

Introduction

As mentioned in our previous issue, there has been a phenomenal growth of arbitration as a mechanism for resolving shipping disputes in most jurisdictions, including Hong Kong. In this regard, the Hong Kong International Arbitration Centre ("**HKIAC**") was set up as an independent institution in Hong Kong which provides one-stop services in relation to arbitration, mediation and domain name cases etc. to parties in dispute. To give you a more complete picture of maritime arbitration in Hong Kong, the general maritime arbitration procedures in Hong Kong will be discussed as below.

Which set of Arbitration Procedures are applicable?

Parties may agree, either before or after the dispute has arisen, that the dispute will be heard under the rules of an arbitral institution, e.g. the rules of the London Maritime Arbitrators Association ("**LMAA**"), HKIAC Administered Arbitration Rules or the UNCITRAL arbitration rules. In addition, parties may also designate the HKIAC to hear and/or administer the arbitration. "Ad-hoc" arbitrations, which follow no particular rules leaving the parties or tribunals to agree on the procedures, are also permissible.

Arbitration under the HKIAC Administered Arbitration Rules

Appointment of Arbitrators

Under the HKIAC Administered Arbitration Rules, the parties are free to determine the number of arbitrators. Where the parties fail to agree on the number arbitrators, HKIAC will decide whether one or three will be appointed.

The parties are normally free to appoint an arbitrator of their choice. Nevertheless, the HKIAC Administered Arbitration Rules do specify some minimal restrictions on who may be appointed as arbitrator. For example, there is a restriction under Article 11.2 that where the parties are of different nationalities, a sole arbitrator shall not have the same nationality as any party unless agreed in writing by the parties. In addition to the said restrictions under the HKIAC Administered Arbitration Rules, the parties should also observe the special requirements in relation to the appointment of an arbitrator as set out in their arbitration agreement.

Under the HKIAC Administered Arbitration Rules, the parties are also free to agree on the procedure for appointing the arbitrator(s). Should the parties fail to reach an agreement:-

- in an arbitration with three arbitrators, each party will appoint one and the two arbitrators thus appointed will appoint the third
- in an arbitration with a sole arbitrator, the HKIAC will appoint one upon the request of either party

If a party fails to appoint an arbitrator within 30 days of a request to do so from the other party, the HKIAC will appoint one upon the request of the other party.

Rules of procedures, place and language of arbitration

The tribunal will adopt suitable procedures for the conduct of the arbitration, but the parties are free to agree on the place and language of arbitration. If the parties failed to reach such agreement, these issues will be determined by the tribunal.

Exchange of submissions or pleadings

The HKIAC Administered Arbitration Rules do not impose strict time limits for the exchange of submissions or pleadings between the parties. The parties may therefore agree on the sequence of pleadings and the relevant time limits. Otherwise, the tribunal may exercise its wide discretion to set the time periods.

Notwithstanding the aforesaid, the claimant must communicate a statement of claim stating his case and the relief sought to the respondent first, failing which the tribunal may be entitled to terminate the proceedings. After receiving a statement of claim from the claimant, the respondent would then be required to communicate a statement of defence and counterclaim (if any) to the claimant. Failure to do so may allow the tribunal to make an arbitral award in favour of the claimant on the evidence before it.

Interim Measures

Pursuant to Article 23 of HKIAC Administered Arbitration Rules, the tribunal may make orders for interim measures. It may also require the parties to provide security in connection with such measure.

Hearings and written proceedings

Subject to any contrary agreement between the parties, the tribunal will decide whether oral hearings are necessary or that the disputes between the parties can be determined on paper (i.e. on the basis of documents and other materials). However, unless the parties have agreed that no hearings shall be held, the tribunal must hold such hearings at an appropriate stage of the proceedings, if so requested by a party or if it considers fit.

The tribunal is free to determine whether further submissions are required from the parties and the manner in which a witness or expert is examined.

Arbitral award

The arbitral award will be in writing, stating the reasons upon which it is based, unless the parties have agreed that no reasons are to be given. An arbitral award will be final and binding on the parties and the parties will be deemed to have waived their rights to any form of recourse or defence in respect of enforcement and execution of the award.

Appeals

Arbitrations under HKIAC Administered Arbitration Rules reserve no right of appeal to the Court on a point of law. As such, unless the right to appeal on a point of law is expressly stated in the arbitration agreement, the Court can only set aside an award on very limited grounds, e.g. party not given proper notice of the appointment of the arbitrator or arbitrators having exceeded their jurisdiction, etc.

“Documents Only” procedures

Where the parties consider that there is no need for an oral hearing to be held, they may choose the “Documents Only” procedure. The “Document Only” Procedure has proven to be a popular option for shipping disputes.

Contrary to the standard arbitration procedures, strict time limits are imposed on the exchange of submissions and pleadings when the “Documents Only” procedure is invoked:-

The claimant has to deliver written claim submissions

and supporting documents within 28 days of agreeing to adopt this procedure or of the order of the tribunal.

- The respondent has to deliver defence and counterclaim submissions within 28 days thereafter.
- The claimant has to deliver reply to defence and counterclaim submissions within 28 days (21 days if the respondent has no counterclaim) thereafter.
- The respondent has to deliver its final submissions on the counterclaim within 21 days thereafter.
- The tribunal will then proceed to issue an award within one month from receiving all relevant documents and submissions.

Legal advice should be sought where there is doubt as to the suitability of invoking a “Documents Only” procedure to resolve a particular dispute.

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