WATSON FARLEY
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BRIEFING

OIL FOR NOTHING?

MAY 2016

- AN IMPORTANT UPDATE FOR THE BUNKER INDUSTRY IN A DISPUTE ARISING FROM THE INSOLVENCY OF THE OW BUNKER GROUP.
- CONTRACTING FOR THE SALE OF GOODS USING RETENTION OF TITLE CLAUSES.
- DEVELOPMENTS IN THE ENGLISH COURTS' APPROACH TO THE ALLOCATION OF RISK IN CHARTERS.

This briefing analyses the Supreme Court's decisions in *PST Energy 7 Shipping LLC v OW Bunker Malta Limited*[1] and *NYK Bulkship (Atlantic) NV v Cargill International SA*[2].

Introduction

In August 2015 we released a briefing on the English High Court's decision in the *PST Energy v OW Bunker Malta* case. The final appeal from that decision was made to the Supreme Court, which recently issued a judgment of particular importance to ship-owners, to the bunker/marine fuel industry and to parties selling or buying goods under English law contracts featuring a retention of title.

On the same day, the Supreme Court handed down a decision in *NYK Bulkship v Cargill International*, dealing with the circumstances in which a vessel will be off-hire under a time charter following the arrest or detention of the vessel. This decision is likely to lead to vessel owners re-drafting off-hire clauses to allocate these particular risks more precisely.

In this briefing we consider those two decisions and their implications for the maritime sector.

1 [2016] UKSC 23
2 [2016] UKSC 20

PST Energy ("Owners") v OW Bunker Malta ("OWB Malta")

The Facts

In a typical bunker supply situation a chain of contracts is formed, such that the entity which physically supplies bunkers to the vessel will not have a contract with the vessel owner, but only with the party above it in the chain. Each contract in the chain will usually contain a clause in favour of the seller purporting to retain title to the bunkers until payment is made, although the bunkers may in fact have been consumed by the vessel before payment falls due under the various contracts and the money passes along the chain.

"EACH CONTRACT IN THE CHAIN WILL USUALLY CONTAIN A CLAUSE IN FAVOUR OF THE SELLER PURPORTING TO RETAIN TITLE TO THE BUNKERS UNTIL PAYMENT IS MADE, ALTHOUGH THE BUNKERS MAY IN FACT HAVE BEEN CONSUMED BY THE VESSEL BEFORE PAYMENT FALLS DUE..."

In *PST Energy v OW Bunker Malta*, OWB Malta had a direct contractual relationship with the Owners of the vessel. OWB Malta contracted with another OW Bunker entity, which in turn contracted with Rosneft Marine (UK) Limited.

However, when the OW Bunker Group went into insolvency in late 2014, the OW Bunker entities stopped making payment.

Rosneft was the party in the chain left out of pocket, and sought payment directly from Owners of the price for the bunkers on the grounds that it held title to them pursuant to the contractual retention of title clauses.

The Owners were unsure which entity to pay: OWB Malta, the now insolvent entity with which the Owners had a direct contract, or Rosneft, the supplier which purported to hold title to the bunkers?

The Legal Issues

The first instance decision, on appeal from an arbitration award, in which it was held that payment should be made to OWB Malta, was itself upheld by the Court of Appeal. Owners pursued this matter to the Supreme Court, which was asked to determine two legal questions:

1. Was the contract between Owners and OWB Malta a "contract of sale" within the meaning of section 2(1) of the Sale of Goods Act 1979 ("the Act")? Key to that question was whether, in substance, the contract between Owners and OWB Malta was for the transfer of legal title to the bunkers, or for the right to use those bunkers lawfully to propel the vessel. If the contract was not a "contract of sale" of goods, payment should be made to OWB Malta, subject to Question 2, which was that:

2. Was the contract between Owners and OWB Malta subject to an implied term that OWB Malta would perform or had performed its obligations to its supplier, in particular by making timely payment so as to ensure that legal title to the bunkers had passed to it?

"...THE CONTRACT WAS NOT A STRAIGHTFORWARD AGREEMENT TO TRANSFER PROPERTY FOR A PRICE..."

The Supreme Court's Decision

Lord Mance gave the judgment of a unanimous Supreme Court. His judgment recognised that the terms on which the bunkers had been purchased from OWB Malta expressly anticipated that the Owners would use the bunkers to propel the vessel and were at liberty to do so before payment was made. This right was described by Lord Mance as "*a vital and essential feature of the bunker supply business*".

Therefore, the contract was not a straightforward agreement to transfer property for a price. It was, in substance, an agreement, first, to permit consumption of the bunkers prior to payment and, second, if and so far as bunkers remained unconsumed, to the transfer of the property in those bunkers, in return for Owners paying the price to OWB Malta.

The liberty on the part of the Owners to consume all or any part of the bunkers without acquiring property in them or having paid for them was a feature quite different from a "contract of sale" of goods to which the Act might apply. The fact that *some* bunkers might not have been consumed by the date that OWB Malta received title to them through the chain of contracts, and OWB Malta would thereupon be obliged to pass title to those bunkers to Owners, did not make the contract *as a whole* a "contract of sale" of goods.

Lord Mance went further, stating that even if the contract were to be analysed as a "contract of sale" (contrary to his previous analysis), OWB Malta would not owe any obligation to transfer property in the bunkers before payment. Therefore, its obligation to transfer property would come to an end as and to the extent that bunkers had in fact been consumed before payment had been made.

On that basis, the Supreme Court agreed with the Arbitral Tribunal, the High Court and the Court of Appeal in deciding Question 1 in favour of payment by Owners to OWB Malta, its direct counterparty.

As to Question 2, the Supreme Court held that there was no implied term requiring OWB Malta to obtain title to the bunkers in a timely fashion (i.e. before they were consumed by the vessel). The only term held by the Supreme Court to be necessary to imply to the contract was that OWB Malta had the legal entitlement to give Owners permission to consume the bunkers.

"THIS ISSUE IS OF IMPORTANCE GENERALLY BECAUSE AN ACTION FOR THE PRICE IS A DEBT CLAIM TO WHICH THE PRINCIPLES OF REMOTENESS, CAUSATION AND MITIGATION DO NOT APPLY. AN ACTION FOR THE PRICE CAN THEREFORE BE A MORE EFFICIENT WAY TO OBTAIN AN AWARD OR JUDGMENT."

However, the Supreme Court did not end its judgment there.

The Court went on to consider in *obiter dicta* comments whether, if it had found that the contract was a "contract of sale", OWB Malta would have been prevented from suing Owners under the Act for the price of the bunkers?

A Court of Appeal decision in an earlier case[3] had found that, where title did not pass due to a retention of title clause, no claim could be made for recovery of the price unless it fell within the limited categories listed in section 49 of the Act.

This issue is of importance generally because an action for the price is a debt claim to which the principles of remoteness, causation and mitigation do not apply. An action for the price is therefore a more straightforward way to obtain an award or judgment.

Since OWB Malta did not hold title to the bunkers as a result of the retention of title clause, the suggestion was that the decision in the earlier case would have prevented OWB Malta from suing for the price (if its contract with Owners had been a "contract of sale" to which the Act applied).

3 *F G Wilson (Engineering) Ltd v John Holt & Co (Liverpool) Ltd* [2014] 1 WLR 2365

The Supreme Court suggested that the earlier case had been wrong to decide that section 49 was fully prescriptive of the circumstances in which a seller may sue for the price of goods. On an analysis of previous case law, Lord Mance stated that the seller may sue the buyer to recover the price under the Act in respect of goods which remain the seller's property but are at the buyer's risk and are destroyed. This was the situation faced by Owners and OWB Malta: (i) the bunkers remained the property of OWB Malta, (ii) they were at Owners' risk under the contract and (iii) Owners were permitted to consume the bunkers for their own commercial benefit.

The Supreme Court concluded that there may be other situations in which the price may be recoverable outside of this exception and the circumstances listed in section 49 of the Act.

"THE MOST SIGNIFICANT IMPACT FOR PARTIES INVOLVED IN THE SALE OF GOODS, PARTICULARLY THOSE WHICH USE RETENTION OF TITLE CLAUSES, MAY COME IN THE OBITER COMMENTS BY LORD MANCE OF THE CIRCUMSTANCES IN WHICH A PARTY MAY SUE FOR THE PRICE OF THE GOODS EVEN THOUGH IT DOES NOT HOLD GOOD TITLE TO THEM."

Conclusions

The Supreme Court's decision provides some certainty to owners as to which party they should pay for bunkers supplied to the vessel, thereby mitigating the risk of double payment which has so vexed vessel owners since the OW Bunker group went into insolvency.

However, the uncertainty identified by the High Court still remains in that the Owners may have a liability to Rosneft under a system of law other than English law.

As a matter of English law, Rosneft has paid for the bunkers in full but is left holding the risk of having to pursue the insolvent OW Bunker entity with which it contracted to obtain some recovery.

The most significant impact for parties involved in the sale of goods, particularly those which use retention of title clauses, may come in the *obiter* comments by Lord Mance of the circumstances in which a party may sue for the price of the goods even though it does not hold good title to them. It is to be expected that there will be upcoming cases which will address the scope of the circumstances in which a party may sue for the price.

NYK Bulkship ("NYK") v Cargill International ("Cargill")

On the same day as the judgment in the *OW Bunker* case, the Supreme Court handed down judgment in a case which came to the courts on an appeal from an arbitration tribunal under section 69 of the Arbitration Act 1996. The case turned on the question of the liability of time charterers to pay hire following the arrest of the vessel. As the Supreme Court noted, this is a "*long-standing problem, aggravated by the difficulty in obtaining compensation for an arrest or detention which proves to be unjustified*".

As a result, parties to time charters often seek to address this risk by an express clause setting out the circumstances in which the vessel will be off-hire.

NYK, the vessel owner, had entered into an amended Asbatime time charter (based on the 1946 NYPE form) with Cargill, the time charterers. Clause 49 provided that hire was to be suspended for the period of the vessel's detention or arrest unless the arrest was "*occasioned by any personal act or omission or default of the Charterers or their agents*".

A dispute arose between Transclear S.A. ("Transclear") and IBG Investments Limited ("IBG"), the respective seller and buyer of cargo on board the vessel, in relation to demurrage. Neither had a direct contractual relationship with Cargill because Cargill had voyage chartered the vessel to another entity, which had in turn contracted in relation to the cargo. Transclear sought to arrest the cargo but, due to an error by the authorities, the vessel was arrested instead of the cargo, with subsequent delay to the vessel sailing.

"THE ISSUE TO BE DECIDED WAS WHETHER HIRE WAS PAYABLE BY CARGILL TO NYK DURING THE PERIOD OF THE VESSEL'S DETENTION?"

The issue to be decided was whether hire was payable by Cargill to NYK during the period of the vessel's detention? Central to deciding that issue were the questions: (i) were Transclear or IBG the agents of Cargill within the meaning of clause 49? (ii) if they were the agents, what was the scope of that agency, and was there a nexus between the functions which Transclear or IBG were performing as agent and the arrest?

Both NYK and Cargill accepted that the phrase "*Charterers or their agents*" was not restricted to the limited legal definition of an "*agent*" as a party contracting with authority on behalf of a principal. The Supreme Court agreed with this conclusion, having analysed authorities which showed that references to "*agents*" in a time charter cannot necessarily be limited to those with a direct legal relationship to the charterer. An "*agent*" was instead found to mean a party availing itself of a facility contractually derived either directly or indirectly from the time charterers. In this case, the relevant contractual functions were that Cargill had a right to call for the discharge of the cargo and an obligation to carry out the discharge operation. To the extent that they were exercising those functions, Transclear and IBG would be agents of Cargill.

However, on the facts, a majority of the Supreme Court found that there was no nexus between the arrest of the vessel and the actions of Transclear and IBG in relation to the cargo.

"HIRE WAS HELD TO BE SUSPENDED UNDER CLAUSE 49 FOR THE PERIOD OF THE ARREST."

Lord Sumption (with whom Lords Neuberger, Mance and Toulson agreed) gave the judgment of the Supreme Court in which the judgments of the High Court and Court of Appeal were overturned in favour of Cargill's appeal, with the result that hire was held to be suspended under clause 49 for the period of the arrest. The Court's rationale was that, under the terms of the charter:

- Cargill was obliged to carry out cargo handling, but the charter did not require the discharge to be carried out at any particular time. Cargill was obliged to pay hire regardless of when discharge occurred.

- There was a difference between defective performance of cargo handling on the one hand and an absence of cargo handling on the other. A failure to discharge the cargo by IBG was not, in the Supreme Court's mind, an exercise of a function of Cargill's under the charter and therefore IBG could only be considered to be Cargill's agent when it was actually performing the discharge, not when it was failing to perform the discharge.

- Looking at the arrest which led to the vessel being off-hire, the Supreme Court found that incurring or enforcing a liability for demurrage under a sub-contract between Transclear and IBG could not be regarded as the vicarious exercise of any facility made available to Cargill under the time charter.

Lord Clarke dissented from this judgment, motivated by a variety of commercial considerations. Among those considerations were that: (i) although Cargill was not itself obliged to ensure a particular time when discharge took place, it was in its commercial interests to ensure that it occurred as quickly as possible in order to maximise the earning capacity of the vessel, (ii) during discharge the vessel was acting pursuant to the orders of Cargill, as time charterer and (iii) Cargill should have been able to foresee the possibility of a demurrage liability arising.

Conclusions

The significance of this decision is in the different approaches which Lord Sumption and Lord Clarke took to the purpose of the 'off-hire' provisions of the time charter in circumstances of arrest.

"THE SIGNIFICANCE OF THIS DECISION IS IN THE DIFFERENT APPROACHES WHICH LORD SUMPTION AND LORD CLARKE TOOK TO THE PURPOSE OF THE 'OFF-HIRE' PROVISIONS OF THE TIME CHARTER IN CIRCUMSTANCES OF ARREST."

Lord Sumption, with whom the majority of the Supreme Court agreed, considered that the main purpose of clause 49 in the time charter was to protect the time charterer, Cargill. He took the view that express provisos within that clause would be generally interpreted narrowly, such that the vessel may be more readily considered to be off-hire in the event of an arrest.

This may come as some surprise to vessel owners and it is possible that charters will be increasingly amended to distribute this risk in a manner more favoured by Lord Clarke in his dissenting judgment. Vessel owners trading to certain ports, where delays or congestion may give rise to disputes between cargo sellers and buyers, otherwise risk the vessel being off-hire during a resulting arrest or detention of the vessel.

Lord Clarke's view was that the commercial expectation would be that the vessel should not be off-hire where the reason was outside the control of the vessel or her owners, a position which some in the industry may share, but for which they will now have to adapt their charters.

FOR MORE INFORMATION

Should you like to discuss any of the matters raised in this Briefing, please speak with a member of our team below or your regular contact at Watson Farley & Williams.

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