Commodities

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COMMODITIES BULLETIN

Prohibition and Default Clauses - a FOSFA decision

In last month's Bulletin, Partner Katie Pritchard considered an English High Court ruling on the application of the GAFTA Prohibition and Default clauses, *Bunge S.A. v Nidera B.V.* (29 January 2013). In February 2013, the Court handed down a decision on the equivalent clauses in the FOSFA terms. Associate John Rollason has reviewed the judgment.

In *Novasen v Alimenta* (27 February 2013), the English High Court considered the application of common law principles to the assessment of damages for breach of contract under FOSFA standard terms. It decided that a buyer's damages against a non-performing seller may be assessed very differently depending on whether or not it buys substitute goods.

The contract was for the sale of 2,000mt crude groundnut oil of Senegal origin CIF Genoa, with shipment December 2007/10 January 2008 on FOSFA 201 terms. These incorporate standard FOSFA clauses on Prohibition and Default. The shipment period was extended by agreement between the parties with no fixed expiry date. On 2 April 2008, Sellers gave Buyers notice of a prohibition of export imposed by the Senegalese government. The FOSFA Prohibition clause extended Sellers' time for performance by 30 days, until 2 May 2008. (The prohibition itself remained in force until 6 June 2008.)

However, in their message of 2 April 2008, Sellers also purported to terminate the contract on the basis of the prohibition. Buyers took this as a repudiatory breach and accepted it on 2 April 2008 as bringing the contract to an end. Buyers then brought a claim against Sellers for damages. The FOSFA arbitrators held that Buyers were correct and awarded them damages under the Default clause, based on the difference between the contract price of the goods and the market price on 2 April 2008.

Sellers appealed to the High Court, arguing that when assessing Buyers' damages, the arbitrators should have applied the principles from the

House of Lords decision in *Golden Strait Corp v NYKK (the "Golden Victory")* (28 March 2007) and taken into account what actually happened after 2 April 2008, when Buyers accepted Sellers' breach. Sellers could not have shipped within the period of the extension because the prohibition was still in force. On this basis, Sellers argued, Buyers had suffered no loss and should recover no damages.

The FOSFA Default clause provides (amongst other things):

> *"In default of this contract by either party, the other party at his discretion shall …have the right either to cancel the contract or the right to sell or purchase, as the case may be, against the defaulter who shall on demand make good the loss, if any, on such sale or purchase.*
>
> *"If the party liable to pay shall be dissatisfied with the price of such sale or purchase, or if neither of the above rights is exercised, the damages, if any, shall … be determined by arbitration.*
>
> *"The damages awarded … shall be limited to the difference between the contract price and the actual or estimated market price on the day of default…. If the arbitrators consider the circumstances of the default justify it they may, at their absolute discretion, … award additional damages. …"*

The Court found in favour of Sellers and remitted the award to the arbitrators. The Court said that damages should be assessed on two different bases under the FOSFA Default clause, depending on whether or not the "innocent" party chose either (1) to buy substitute goods (or sell to a substitute buyer if the "innocent" party is the seller); or (2) simply to claim damages without entering into a substitute contract.

If the "innocent" party did buy/sell against the defaulter, then the common law position would be modified by the clause and the "innocent" party would be entitled to compensation irrespective of subsequent events and the effect which they might have had on the contract if it had remained in force.

However, if the "innocent" party did not buy/sell against the defaulter, then the common law position would not be modified by the clause. The "innocent" party's entitlement to compensation would be the common law measure. Subsequent events would (where relevant) be taken into account when that compensation was assessed.

We understand that this decision has caused some surprise in FOSFA arbitration circles and that it is being appealed to the Court of Appeal.

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Can a contract for the sale of goods be enforceable despite some significant terms being uncertain?

In *MRI Trading (MRI) v Erdenet Mining Corporation LLC (Erdenet)* (12 February 2013) the Court of Appeal was asked to determine whether a contract for the sale of copper concentrates which left terms, including certain charges and the shipping schedule, to be agreed, was enforceable.

A dispute had previously arisen between the parties which had been referred to arbitration at the London Metal Exchange. As part of an agreement to settle that dispute, three contracts for the sale of copper and molybdenum concentrate were concluded. Two of the contracts were performed but no goods were shipped under the third and no agreement was reached on certain charges, or on the shipping schedule.

The sale contracts contained an implied term that any disputes concerning the charges and the shipping schedule were to be referred to arbitration. A Tribunal was therefore asked to determine whether Erdenet was under an enforceable obligation to deliver copper concentrates under the third contract. The Tribunal held that the contract was merely an *"agreement to agree"* as the charges and shipping schedule were material terms which prevented performance. Erdenet therefore had no obligation to deliver the copper and the contract was unenforceable due to uncertainty. MRI appealed to the High Court.

Mr Justice Eder held that the tribunal's decision was *"somewhat*

surprising if not bizarre" and *"that no reasonable tribunal correctly applying the relevant principles could have reached such a conclusion"*. The award was varied by applying the correct legal principles and otherwise set aside. Permission was granted for Erdenet to appeal.

The Court of Appeal rejected Erdenet's appeal. It held that the sale contract was to be construed in the context of the wider transaction and the parties' long-term relationship.

The sale contract was part of the series of contracts with similar terms entered into as part of the settlement agreement under which MRI had abandoned its arbitration claim. Erdenet had therefore already received some benefit from the wider transaction.

Both the sale contract and the settlement agreement used the mandatory term "shall" in several provisions. This was held to demonstrate that the parties had intended there to be obligations under the sale contract. The language implied the obligations were not intended to be destroyed if the parties could not agree the charges and the shipping schedule. If the parties could not agree the charges and the shipping schedule then reasonable charges and a reasonable shipping schedule were to be adopted. The contract provided an arbitration clause which could be used to determine any disputes over the charges or the shipping schedule.

For parties regularly trading with each other, the Court of Appeal's approach will be of particular interest. Parties should be aware that their trading relationship will be taken into account when a dispute arises over the existence of a particular contract. The Court will consider whether one party has had any benefit from the alleged contract or wider relationship and will look at the nature of the language used by the parties. Where a contract is found to exist, the Court will apply "reasonable" terms to cover any aspects on which the parties cannot agree.

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A tangled web - do the roles of receiver and sub-charterer overlap?

Partner Brian Perrott and Associate Alice Marques represented Cargill International S.A. in a dispute that will be of interest to commodity traders who also act as charterers in the course of their business.

The Commercial Court's decision in *NYK Bulkship (Atlantic) N.V. v Cargill International S.A.* (1 February 2013) arose out of an appeal by Owners (NYK) against a decision of an arbitral tribunal in favour of Charterers (Cargill). The dispute concerned the construction of an off-hire clause in a time charter.

Cargill had time-chartered M/V "Global Santosh" (the Vessel) from NYK and had sub-chartered it to Sigma Shipping Ltd. Transclear SA (Transclear), who were assumed to be a sub-voyage charterer, sold a cargo of cement to IBG Investment Ltd (IBG) and IBG were named as the notifying party on the bill of lading.

Under the sale contract, IBG were responsible for unloading the cargo and were liable to Transclear for any demurrage incurred as a result of delays in discharge.

The cargo was to be discharged at Port Harcourt, Nigeria. After delays as a result of congestion, the Vessel was finally called to berth. However, she was sent back to anchorage because Transclear had obtained an Arrest Order against the cargo for a demurrage claim against IBG. By mistake, the Vessel had also been named in the Arrest Order. As a result of the Arrest Order, the cargo could not be discharged.

As time-charterers, Cargill withheld hire from NYK whilst the Arrest Order was in place in accordance with the following clause in the charterparty:

"Should the vessel be ... arrested by any authority or by any legal process during the currency of this Charter Party, the payment of hire shall be suspended until the time of her release, unless such ...arrest is occasioned by any personal act or omission or default of the Charterers or their agents..."

NYK took the view that the proviso *"unless such…arrest is occasioned by any personal act or omission or default of the Charterers or their agents"* applied and that hire continued to be payable. They argued before the Tribunal that *"agents"* included sub-charterers and receivers who were performing the tasks of charterers and that IBG was Cargill's agent in relation to unloading the cargo; that the arrest had been *"occasioned by"* both IBG's failure to unload within the stipulated time (which gave rise

to Transclear's demurrage claim) and its failure to pay and/or secure Transclear's demurrage claim. NYK also submitted that Transclear was Cargill's agent and that the arrest of the Vessel had been *"occasioned by"* Transclear obtaining the Arrest Order.

The Tribunal held that there was no evidential basis for finding that Cargill had consented to Transclear arresting the Vessel, nor was there evidence that IBG was performing Cargill's obligations in respect of discharge. Transclear's action in arresting the Vessel was found not to be in the capacity of *"agent"*, but on its own behalf.

NYK appealed to the English High Court, maintaining the submission that those beneath Cargill in the charterparty chain had been delegated the performance of Cargill's responsibilities under the charterparty and were therefore Cargill's *"agents"* for the purposes of the proviso. NYK submitted that the question *"Why was there a demurrage claim?"*, could only be answered by reference to Cargill's employment of the Vessel for trading purposes and that as a consequence, the arrest was *"occasioned by"* Cargill's agents.

Cargill submitted that the proviso in clause 49 only applies to acts, omissions or defaults that occur in the course of performing some delegated task. The Court agreed, holding that Transclear's arrest of cargo and Vessel was not done in the performance of a delegated task.

However, the Court also found that the Tribunal had failed to consider (i) whether the acts, omissions or default of IBG occurred while IBG was under an obligation, as a delegate of Cargill, to unload the Vessel and (ii) if yes, whether the arrest was "occasioned by" those acts, omissions or default of IBG.

The Court held that IBG had become a delegate of Cargill in respect of the obligation to unload pursuant to clause 8 of the Charterparty, which provides that *"Charterers are to perform all cargo handling at their expense"*. IBG's failure to unload within the laydays specified in the sale contract between IBG and Transclear was an act, omission or default in the course of performing the obligation to discharge, as delegated from Cargill.

The question of causation - whether IBG's acts, omissions or defaults *"occasioned"* the arrest - has been remitted to the Tribunal.

Both parties have been given leave to appeal to the Court of Appeal. This is due to be heard between July and November this year.

It seems a radical step to import an obligation owed by a receiver to discharge within set laydays in a sale context, into a time charterparty. Cargill owed no obligation to NYK under the charter as to when the cargo would be discharged, or how long the discharge would take. It is hard to understand how clause 8 of the charterparty can imply an obligation to discharge within third party negotiated laydays.

We shall provide a further update once the decision of the Court of Appeal has been made publicly available.

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Conferences & Events

Commodities Breakfast Seminar
HFW Singapore
(25 April 2013)

Oil and Gas Seminar
HFW Singapore
(25 April 2013)

HFW Energy and Resources Seminar
HFW Perth
(15 May 2013)
Presenting: Hazel Brewer, James Donoghue, Julian Sher and Cheryl Edwardes

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