



LACK OF ENFORCEABILITY A FREIGHT-ENING PROSPECT

The relationship between Shippers and Carriers when it comes to sea freight agreements has often been adversarial. The lack of a standardised, reliably enforceable sea freight agreement, which does not rely on the honesty of both parties, has left a gap that has often been filled by inadequately drafted agreements.

What we need and what we have

Sea freight agreements must be not only enforceable, but flexible. If an agreement turns out to be unenforceable, Shippers can suffer from delays, service failures, unexpected costs, lost sales and smaller margins. Carriers may have to deal with under-utilised vessels and less predictable revenue. If an agreement lacks flexibility, then it risks

becoming obsolete as time goes on and circumstances change. This discourages parties from entering into long-term contracts, which in turn leads to a tendency towards chains of short-term contracts which do little to cater to the individual needs of the parties.

If key provisions are not adequately drafted, they may be open to interpretation which can incur time and resources for both parties to administer and seek to enforce, and at worst could leave parties exposed to significant losses when provisions can't be relied upon. The effect of constant renegotiation on the bottom line of parties to such agreements should not be underestimated either. Developing new agreements on an ad-hoc basis puts an unnecessary burden on internal resources allowing time to be spent on more substantive business issues by providing a reliable standard template which parties can use as a starting point.

What's been done before

Producing reliably enforceable and flexible contracts has a significant positive impact on the profitability of all those involved in the carriage of freight by sea and several providers have tried to fill this gap. Unfortunately, many have been unsuccessful, at least at becoming widely adopted. An early example was from BIMCO, one of the largest shipping associations representing ship owners. BIMCO develop multiple standard contracts for use in shipping, including the Standard Service Contract (SERVICECON). SERVICECON covers situations whereby a Shipper undertakes to transport a minimum number of containers over an agreed given period, and supporting annexes allow parties to adapt the particulars to their individual circumstances. Despite its promise, it never gained much traction in the sector.

It has always been commercially unviable for Shippers and Carriers to enter into sea freight agreements that last more than one year with fixed freight rates due to market volatility

and the lack of flexible and enforceable provisions in standard agreements. Index-Linked Contracts allowed agreements to be extended to two or even three years, by replacing fixed prices with freight rates linked to an index that tracks the freight rates on a given route. Multiple indices have been developed including the World Container Index, Freightos Baltic Index and Shanghai Containerized Freight Index. As freight rates are often a main focus of negotiation in sea freight agreements, linking that aspect of the agreement to a standardised index measured and published by a trusted third party allows parties the opportunity to focus on the services provided in the contract rather than the freight rates. These are now gaining in popularity again as many Carriers seek to contract with Shippers for longer periods.

A new dawn

A promising emerging solution to the enforceability of sea freight agreements was launched by the New York Shipping Exchange (NYSHEX). NYSHEX offer a standard contract which can be adapted to individual needs or can work with the parties' own agreements mutually enforceable and reciprocal obligations which are binding on both parties. This creates the aligned expectations needed for the contract to be relied upon by both parties in the event of a dispute creating certainty and peace of mind. NYSHEX are showing significant promise, with claimed contract fulfilment rates of 99% versus a poor 67% industry average.

The administration of the contract takes place on the NYSHEX automated systems and allows parties to track relevant booking and shipment milestones to assess performance, identify issues and administer settlement of agreed liquidated damages. Fees for using the service are zero for Shippers, and Carriers pay a flat fee per TEU. The key differentiating factor for NYSHEX-based agreements is the completeness of the service. The option

to use NYSHEX contract templates or existing ones, the monitoring of price and capacity/volume and the process for resolving disputes are all dealt with by the same third party.

As more Shippers and Carriers place their trust in the system, it will become more attractive and accepted as a mechanism for monitoring and enforcing sea freight agreements, whether using the NYSHEX standard templates or bespoke ones sourced elsewhere. Widespread use of NYSHEX among Shippers and Carriers will mitigate risk and ultimately improve business relationships. Uptake in the United States has been very strong, leading to a shift in focus towards the Far East/Europe market in 2021. Leading carriers like Maersk, Hapag-Lloyd and CMA CGM already use NYSHEX themselves to develop mutually enforceable contracts. If successful, the system could prove to be a trusted monitoring and enforcement mechanism for sea freight agreements being concluded and performed in the market.

The recent COVID-19 pandemic has had a significant impact on the carriage of sea freight – during the initial lockdowns, the market slowed, but following that initial period there has been an unprecedented surge in demand which, along with other supply chain challenges, has caused widespread disruption which is still far from being resolved. Now, more than ever, Shippers and Carriers need to have absolute faith in the enforceability of their sea freight agreements to continue business as usual.

If you would like to discuss how HFW can support you with your sea freight agreements and wider logistics and supply chain needs, please speak to:



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HFW has over 600 lawyers working in offices across the Americas, Europe, the Middle East and Asia Pacific. For further information about our logistics capabilities, please visit www.hfw.com/Logistics

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