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THE TIDE CONTINUES TO RISE: SELECTED DEVELOPMENTS IN THE EVOLUTION OF U.S MARITIME LAW

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Man Ferrostaal Inc. v. M/V AKILI, 704 F.3d 77 (2d Cir. 2012)

This case presents an important appellate exploration into the origins *of in rem* liability and the factors limiting exposure under the bailment theory for entities who are not the statutory "carrier" under the U.S. Carriage of Goods by Sea Act, which is the U.S. domestic enactment of the 1924 Hague Rules.

The case arose out of damage to a cargo of steel pipe shipped from China to the United States due to bad stowage when the shipper and sub-sub-charterer's pipe was over stowed with heavier pipe as a consequence of the sub-charterer's own stow plan. Owners had previously time chartered the ship to A, whom, in turn, sublet it to B. B then relet the vessel to C. C then sub-chartered space to Ferrostaal, the buyer of the pipe cargo from the Chinese manufacturer. This space charter provided that the handling of the cargo was to be "free of risk to the vessel" and that claims

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for cargo damage were to be governed by the Hague-Visby Rules. As an aside, the court quickly equated the terms of Hague Visby to those in COGSA, an important statement for the international community in and of itself. Agents for C issued a bill of lading, which was not signed "for the master" and so the bill was not an "owner's' bill. Indeed, the bill of lading acted only as a receipt for the cargo and was never negotiated.

Ferrostaal sued both the ship *in rem*, and her owners, together with the operators *in personam*.

Owners argued that their ship was not liable *in rem* because (1) the vessel was not a "carrier" under COGSA, and (2) the "free of risk to the vessel" provision in the sub-sub-charter party absolved the vessel of liability.

In respect to the *in personam* claim against the Owner and Operator, the court agreed with the trial court that there was no *in personam* liability because the bill of lading contract was on the letterhead of the sub-sub charterer, and was not signed by the Master. Under U.S. law, the signature by or on behalf of the Master on the face of the bill of lading would have ratified the contract and created *in personam* liability for the Owner. But as the bill of lading was worded, it was only a contract with the sub-sub-charterer.

As to the *in rem* claims, the court agreed that charter parties are not subject to COGSA or the Hague Visby rules by law, and that while the latter argument the language "free of risk to the vessel" in the sub-sub-charter party would normally be effective, in this case the sub-sub-charter party had a paramount Clause that made Hague Visby applicable as a matter of contract. Consequently, the vessel could not be held free of risk as that would effectively violate COGSA/Hague Visby rules by reducing the carrier's liability below those established by the Conventions as incorporated into the space agreement. As the operative contract, the statutory terms which had been incorporated prohibited a carrier or the ship from contracting for a waiver of their statutory obligations regarding cargo damage.

As to the *in rem* argument, the court held that COGSA does not create the *in rem* liability, and so whether the vessel was a "carrier" was deemed irrelevant. However, the court noted that COGSA addresses the liability of both the "carrier" and the "ship." The court began its reasoning by stating that the use of "ship" in the statute "assumed that maritime law supplied *in rem* liability coextensive with carrier liability." The court went on stating that the *in rem* liability arose out of U.S. case law, long predating the enactment of COGSA, holding that a special relationship arises when cargo

is loaded onboard a vessel. The vessel has impliedly ratified the underlying contract and established a maritime lien securing performance of the agreement. Here, taking the cargo onboard impliedly ratifies the underlying contract of carriage – here the sub-sub-charter – and a lien was created securing performance of that agreement.

On the bailment issue, the court held that since the bill of lading was not issued by Owners, they did not have the exclusive control over the cargo necessary to establish a bailment under which Owners could be found liable.

The opinion does not explain why Ferrostaal, having procured the vessel's *in rem* liability (and was the holder of a club letter of guarantee) required *in personam* judgments against the owner and operator.

At least two points emerge from this decision. First, there is no relief from *in rem* liability under COGSA or Hague Visby as interpreted by this decision. However, if the contract of carriage is a charter party, and the charter party has a clause that provides that the transport shall be "free of risk" to the vessel, that clause can be enforced as along as the operative agreement does not make COGSA or the Hague Rules applicable with a chain of charterers as was present here, the case presents some difficult

contract drafting issues for the vessel's owner when he charters the vessel out and the charter allows relets.

The *Akili* decision projects three lessons for ship owners: (1) once cargo is on board, *in rem* liability will be difficult, if not impossible, to avoid; (2) therefore, careful use of indemnification clauses in the head charter may provide relief from such liabilities which arise through no fault of the owner; and (3) incorporation of COGSA/Hague Visby into contracts to which these statutory schemes are not otherwise applicable should be carefully considered. This is particularly true with respect to the possibility they will appear in sub-contracts which may become binding on the vessel owner.

In the Matter of the Complaint of Frescati Shipping Company Ltd., 718 F.3d 184 (3d Cir. 2013).

Although this matter is not concluded, the United States Court of Appeals' decision is significant (1) because in the context of safe berth and safe port warranties, it recognized the right of the true vessel owner to proceed directly against a sub-charterer for breach of the safety warranties it had given, treating the owner as the "third-party beneficiary" of the sub-charter's warranties, and (2) for the first time defined the limits of the "approach" to a terminal for which a terminal operator is responsible. The

court held that the “approach” will most often begin at the point where the vessel leaves the main channel and assumes the normal pathway into the terminal.

The third-party beneficiary doctrine holds that where contracting parties specifically intend to confer a benefit on a third party, the third party may bring suit on that promise. For example, if two parties agree that a payment is due a third party, that third party may sue the contracting parties for nonpayment.

This right to proceed directly, skipping intermediate charterers in the chain, should actually reduce the end charterer’s quantum of liability because the accrued interest and fees that otherwise accumulate as parties go down the chain of agreements will be avoided and counterparty solvency issues may, likewise, be short-circuited. The rights, however, are reciprocal, and charterers may also take advantage of the ruling and proceed up a chain of agreements going directly against an owner for breach of warranties which actually concern the charterer whose cargo is being carried. Again, such rights may assume considerable practical significance where counterparty financial issues arise.

The basic facts are simple and may be quickly stated. The vessel was trading as a member of the Star Tankers Pool, and was on time

charter to the Pool. The Pool, in turn, had voyage chartered the vessel on the Asbatankvoy form to Citgo Asphalt Refining Company. Owners prosecuted the breach of warranty claim against Citgo as the remote charterer. The Asbatankvoy form, of course, contains absolute safe port and safe berth warranties; the warranties provide:

> **"2. DISCHARGE PORT(S)**: One (1) or two (2) safe port(s) . . . .
>
> The Vessel . . . shall . . . proceed as ordered to Loading Port(s)… and being so loaded shall forthwith proceed, as ordered on signing Bills of Lading, direct to the Discharging Port(s), or so near thereunto as she may safely get (always afloat), and deliver said cargo."

As to safe berths, the Asbatankvoy form states:

> **"Section 9, Safe Berthing – Shifting.** The Vessel shall load and discharge at any safe place or wharf, or alongside ships or lighters reachable on her arrival, which shall be designated and procured by the Charterer, provided the Vessel can proceed thereto, lie at, and depart there from always safely afloat, any lighterage being at the expense, risk and peril of the Charterer."

The Charterer directed the vessel to load in Lake Maracaibo, Venezuela for discharge at its Paulsboro, New Jersey terminal. The terminal lay to the east of a federal anchorage. Vessels could access the terminal only by crossing the anchorage. The vessel, when about 900 feet off the dock and still proceeding in the anchorage area, struck an

abandoned anchor, whose presence previously had not been ascertained. The impact holed a cargo tank disgorging about 6,500 barrels of crude oil into the Delaware River. The cost of a cleanup amounted to about $180 million; damage to the vessel and related expenses were another $8 million, while third-party claims against Owners were negligible.

The Court of Appeals, in finding for Owners, relied on a fifty-plus-year-old Supreme court law granting third party beneficiary status to vessel owners in a different context, and the 1962 decision of the Second Circuit in Paragon Oil Co. v. Republic Tankers S. A., 310 F. 2d 169 (2d. Cir. 1962). That never before cited decision deemed a remote charterer a third-party beneficiary of the sub-charterer's safety warranty. Building on those authorities, the Athos court found that the third-party beneficiary concept had been established because it was the "vessel" that bore the risk of a failure of the warranty; consequently, the benefit should inure to the vessel owner, who bore the ultimate risk of the loss.

On the terminal operator's side of the case, the court was forced to define "approach" because the offending anchor was in the federal anchorage which the ship had to cross in order to reach the dock. The terminal argued that it had no responsibility to warn of the submerged anchor because it did not "control" the anchorage, that is, it could not

unilaterally dredge the area as those functions fell within the purview of the U. S, Army Corps of Engineers. CARCO made this argument notwithstanding that the U. S. Supreme Court 115 years earlier in an oft cited and expansive opinion had stated that “control” is irrelevant to the terminal operator’s duty to exercise reasonable care in locating hidden hazards in its berths and the approaches and warning mariners of their presence. Smith v. Burnett, 173. U. S. 430.

The Court of Appeals has now defined the “approach” to a berth as:

> “When a ship transitions from its general voyage to a final, direct path to its destination, it is on an approach. … In most instances, the approach will begin where the ship makes its last significant turn from the channel toward its appointed destination following the usual path of ships docking at that terminal.” … Again, we believe it may be useful to analogize a final approach of the vessel to a port to that of a driveway leading to a home from the public road. It is the last segment of the voyage leading directly to the host’s door.”

The appeals court has sent the case back for a new trial on the question whether the warranties in fact had been breached and whether the terminal operator breached its duty to conduct reasonable inspections.

Regardless of the outcome on the retrial, the Court of Appeals has laid down legal principles having recurring application in our practices.

On the terminal operator's side, though Smith v. Burnett is cited in every case where a terminal operator is charged with negligence, the Athos is the first one to require a definition of "approach." A review of the published cases suggests that because the facts made clear the ship either was in the "approach" and the question was, therefore, not contested or that the ship had gotten out of the normal pathway to the dock - had left the driveway and gone up on the lawn - discussion of the issue was not required. Will another 115 years pass before a court must again wrestle with the question?

What will be the reach of the decision on the benefit of the warranties? The warranties in the ASBATANKVOY form at issue in the case specifically state that it is the "Vessel" which charterer is to send to safe places, and while the court did not refer explicitly to this language, it did depend in its reasoning on the risk to the "vessel" posed by unsafe places.

Many forms of charters in common usage such as the NYPE, the Baltime, the Gercon and several tanker forms all refer to the "vessel" in this context of a safe berth, thus furnishing a "hook" to broadly extend the doctrine of the Athos I. Whether the bar chooses to make those arguments and the courts opt to accept them remains to be seen.

Also, extension of the concept to other provisions in sub-charters as well as sub-charters looking directly to owners should not be ignored. On the other had, Paragon Oil quietly drifted unnoticed on the judicial seas for 50 years before the Athos court rescued the opinion from oblivion. At a minimum, though, the decision should make both owners and charterers consider how the decision might change their exposure and whether they should take steps to minimize risks they do not wish to assume.

MSC Flaminia (Case No. 12-civ-08892) Southern District of New York.

Litigation growing out of the July 2012 fire in the mid-Atlantic on board the M/V MSC Flaminia, is just beginning in the federal court in New York. The owners and operators have filed a petition for exoneration from or limitation of liability under U.S. law in the Federal Court in New York and it appears venue is not being contested.

While on a voyage from Charleston, South Carolina to the UK, when about 1,000 miles from the entrance to the English Channel, the vessel experienced an explosion and fire killing three crew members, and eventually requiring the ship be abandoned. She was carrying about 2,900 loaded containers.

Smit Salvage BV conducted salvage operation under a Lloyd's Open Form 2011 contract. The salvors extinguished the fire and towed the vessel toward Europe, only to be held at the entrance to the English Channel for nearly a month while a place of refuge was sought. Eventually, the ship found refuge in Wilhelmshaven, Germany.

Once the vessel was ready to discharge the containers, a major dispute arose regarding security to be posted in favor of both the salvors and for the very substantial general average expenses. Estimates of the salvage costs and other GA expenditures well exceeded the value of the cargo.

Ultimately, salvors demanded as security 65% of the cargo's value, while the general average adjusters demanded 100% of the value. Apart from the salvage, very substantial GA costs, including wharfage, the handling and storage of containers under distressed conditions, and the disposal of contaminated firefighting water had been incurred.

Eventually, the cargo interests did not contest the salvor's claim for 65% of the value but did protest the 100% claim made by the GA adjusters arguing that the demand was "unreasonable." When agreement could not be reached, the cargo interests brought the matter before the New York court. The ship owner defended the adjuster's demand, but in so doing, did

not address the reasonableness of the adjusters' demand. Rather, Owners argued that the court should accede to London as the agreed forum for the adjustment and that it was up to the adjuster to determine the level of GA security. The court, however, chose to override the owner's position and, in an order dated March 5, 2013, ordered owners to release its possessory lien on the cargo once cargo posted security in the amount of 100% of the value of the cargo, that security should be apportioned 65% to the salvors in accordance with the order of the London salvage arbitrator and 35% to the GA adjuster with the understanding that if the salvage award ultimately was for less than the 65% the remainder is to be credited to the general average security.

While this allocation is not a happy situation for the vessel owner and its insurers, there appears to be a certain practicality to the result. The ultimate option for all concerned was to let the cargo go to a sale at which point the cargo interests and the salvors would, or more accurately, the salvors and the GA adjuster, would fight over the allocation. Given that the salvage arbitrator had already awarded 65% of the value as security to the salvors and to the extent that the salvors' lien takes priority, the judge's allocation may be viewed as reflecting the ultimate outcome after a sale. At

this point, then, there is only the full value of the cargo available in any event.

If, at the end of the day, GA security is inadequate to cover the approved GA expenditures, it appears that the vessel interests may still have an *in personam* claim against the cargo owner for further GA payments, but that will depend on the solvency of the cargo interests and the ability to find them in order to either make a claim or enforce a judgment which might be obtained in the context of the New York litigation. It is also doubtful that cargo underwriters will pay more than 100% of the value of the cargo for GA and salvage. Whether the security that has been posted will include a clause requiring the cargo interests to appear in any *in personam* action is not known. On the other hand, since cargo routinely contests its obligation to make GA payments on the grounds of the unseaworthiness of the carrying vessel, such claims for the overage may well wind up being an integral part of the New York litigation, as the cargo interests have appeared there and exposed themselves to claims from the vessel interests.

As an aside, it appears that the trial court's order is not appealable at this stage.

In the meantime, the joint hull committee here in London recently announced that it is launching an insurance product to deal with issues arising out of GA declarations involving large box ships. One article appeared in the May 10, 2013 edition of Trade Winds and, in fact, cited the MSC Flaminia casualty as an example of the need for reform of the general average process in the context of large container ships. The proposed program would provide insurance of $30,000 per box and it is expected that the ship owner will recover the cost of such insurance through its freight rates. It is expected that the premium charge will be minimal at best. In short, the purpose of the cover will be to take general average out of the settlement of container ship casualties because cargo's contribution will be replaced by the insurance cover. It remains to be seen whether this concept will take hold.

The ever-present issue of port of refuge has played a large role in this case. It is a very troublesome issue, and in the case of the MSC Flaminia situation resulted in the vessel being delayed access to a port of refuge for nearly a month. We understand that apparently the Flaminia situation has motivated the EU to examine the problem.

Costa Concordia.

This casualty has produced some litigation in the United States against Carnival, the parent company of Costa Lines. At least three complaints with passengers as the plaintiffs have been filed and all are pending in the Florida state court, 11th Judicial District in Miami. These cases are Abeid –Saba v. Carnival, Civil Action 12-26072 CA02, Perez v. Carnival, Civil Action 12-09163 CA22, and Scimon v. Carnival, Civil Action 12-26076 CA30.

They allege, not surprisingly, that Carnival is the alter ego of Costa Line and, therefore, responsible for Costa's faults. There are also allegations of direct involvement by Carnival with Costa's operations, which, if proven, will lead to Carnival's liability quite apart from that of Costa.

Also, the Scimon and Abeid-Saba complaints have joined the naval architect involved in the design of the Costa Concordia alleging design defects.

Because different judges in the same court have the cases, the results on motions to send the cases to Italy as the situs of the disaster, and presumably the venue chosen in the passenger tickets, have met with contradictory results. All the Abeid - Saba plaintiffs have all been sent to Italy. The American Scimon plaintiffs, however, remain in Florida, while the

foreign plaintiffs who joined the Scimon lawsuit have also been transferred to Italy.

The federal 11th Circuit court of Appeals which covers Florida also recently transferred to Italy class action seeking losses claimed by businesses in Giglio, Italy, the site of the wreck. Giglio Sub v. Carnival, Court of Appeals No. 12-15533.

The Deep Water Horizon-(New Orleans –Multi District docket No. 2179)

The April 20, 2010 Deep Water Horizon disaster has produced a series of decisions which should be of interest to those involved in both the on-shore and off-shore aspects of U. S. energy business.

The litigation is sprawling to say the least, but a very brief overview of the basic facts and identity of the main parties will be useful in following the discussion below.

BP and Anadarko were the co-owners of the Macondo Well, located on the seabed in the Gulf of Mexico. A blowout of the well occurred on April 20, 2010 resulting in explosions and a fire on the DEEPWATER HORIZON, a mobile offshore drilling unit ("MODU"). The drilling unit sank two days later, breaking the riser pipe that connected it to the Macondo Well. Oil flowed from the seabed through the blowout preventer ("BOP")

and remaining section of riser pipe, and the oil was then released into the Gulf of Mexico. This release into the ocean water took place well below the water's surface. The subsequent discharge of millions of gallons of oil into the Gulf resulted in multiple lawsuits being filed, which were consolidated. Transocean, the owner of the MODU, filed a ship owner's Limitation Action under 46 U.S.C. § 30501, et seq. In the Limitation Action, numerous claims were asserted primarily for personal injury, wrongful death, economic loss, and property damage.

The United States government has filed a suit against BP, Anadarko and Transocean, claiming natural resource damages and civil penalties under the Clean Water Act. In this context, the U.S. government is seeking a determination that BP was guilty of gross negligence and thus exposed to a trebling of the spill penalties from a maximum of $1100 per barrel to $3300 per barrel. The parties are awaiting the court's decision on this point in a non-jury proceeding.

On the insurance coverage side, BP has sought additional insured status on Transocean's liability program. Reported limits are $750 million. That suit is on appeal to the Fifth Circuit Court of Appeals in New Orleans. The question is whether BP is on the policy at all, and if so, was it intended

to be on the policy generally or only for the liabilities arising under the indemnity provisions of the drilling contract.

The trial court held that BP was not an additional insured because the contract required insurance only for the tort liabilities which Transocean had assumed in the drilling contract. The court also held that Transocean had not assumed insured liabilities with respect to pollution from subsurface sources.

To the extent BP is an additional insured for the Deepwater Horizon losses, the policy only responds for one limit. Generally, insurers must pay the claims as presented. Consequently, if there is a reversal of the trial court's decision, we may witness a scramble between BP and Transocean to get claims paid, and concerns on Underwriters' part as to which claims should be paid without incurring exposure to a disgruntled insured whose claims have not been paid.

The Government is awaiting a decision on its argument that BP's gross negligence caused the disaster. If the court finds in favor of the United States on this issue, the financial consequences will be severe since, although the amount spilled is not agreed, it is agreed that several million barrels escaped before BP succeeded in capping the well. (Trial on the amount spilled is to begin September 30th)

Other decisions of note in the case are as follows:

(a) On February 22,2012, the court ruled that because a MODU is not being navigated, it has no liability for subsurface discharges; rather the liability rests with the permittee or lessee from the U.S. government of the subsea block being drilled. The court also held that all lessees of a given block were jointly and severally liable under the Oil Pollution Act. This latter holding may come to life in cases where the operating partner doing the drilling is not one of the energy industry giants and does not have the financial means to meet its liabilities. 2012 WL 569388

(b) On January 26, 2012, the trial court decided the scope of the indemnification clauses in the BP-Transocean contract. The drilling contract between BP and Transocean allocated to BP the risk of pollution originating beneath the water's surface, and to Transocean, the operator of the MODU, the risk of pollution originating on the water's surface. Thus, BP agreed to indemnify Transocean for the risk of subsurface oil pollution, "without regard for whether the pollution. . .is caused in whole or in part by the negligence of Transocean . . .and without regard to the cause or causes thereof . . .the unseaworthiness of any vessel . . .breach of contract, strict liability, . . .gross negligence."

The Court was asked to decide whether BP was required to indemnify Transocean for gross negligence, strict liability and statutory fines and penalties. The Court answered "yes" to strict liability under OPA and to gross negligence, but "no" to reckless or intentional conduct, punitive damages, and fines and penalties. The court predicated the "no" on public policy grounds stating that to allow such a transfer of risk would defeat the purpose behind such rules which is to "punish" and "deter" the malefactor. 2012 WL 246455.

(c) The trial court has ruled that OPA does not preclude punitive damages. This decision is at odds with a decision about 12 years ago from a federal court of appeals in Boston. See Southport Marine v. Gulf Oil Limited Partners, 234 F.3d 58.

(d) BP has also moved for an order directing the claims administrator under a court approved class action settlement to suspend payments. When the court approved settlement late last year, BP estimated payments would run up to $7.8 billion. Now, about nine months later, press reports put the estimate at $9.6 billion.

BP's allegations of fraud prompted the judge overseeing the case to appoint a former director of the FBI to investigate the charges which included misconduct of the Fund's administrator. The investigation has

reportedly, earlier this month, advised the judge that he found no misconduct on the part of the administrator, but did find issues with certain lawyers working for the Fund. The next chapter remains to be written.

BP also alleges conflicts of interest involving lawyers on the panel processing the claims and misinterpretation of the settlement agreement's provisions regarding economic losses. The latter point is on appeal, having been argued August 29, 2013.

Skullduggery in these mass settlements regrettably is not unknown and has come up previously in the phen-phen diet drug settlement and the silicosis settlements.