

THE CHARTERER

THE CHARTERERS P&I CLUB NEWSLETTER

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AUSTRALIAN JUDGMENT PUTS STEEL CARRIERS UNDER PRESSURE TO MODIFY VESSELS

Snapshot

In a recent case heard before the Australian Federal Court on 6th December 2005 (Stemcor (Asia) Pty Ltd V'S C.V. Scheepvaartonderneming Ankergracht {2005} FCA 1808) the court handed down a judgment finding two carriers liable for corrosion damage to two cargoes of coiled sheet steel caused by condensation within the holds on voyages from Japan to Australia. Although the claims were made under the Owners' bills of lading, this decision is important to charterers who issue bills of lading in their own name.

Accepting expert evidence, the Court found there was a high probability that as the vessels travelled from the Japanese winter across the equator to Australia, conditions for condensation would be created in the holds during the course of the voyages if free water was not eliminated or if moist air was introduced into the holds. While there was evidence that the shipper had knowledge that the vessels did not contain dehumidifying systems, the Court determined that the vessels were nonetheless unseaworthy by

reason of the shipowner's failure to install these systems within the holds for the voyages in question.

Facts

The two vessels were part of a single fleet, supplied under an affreightment contract which required the shipper to use the fleet's vessels to ship cargoes of steel unless there were no vessels available within the fleet at the time. The shipping manager responsible for the selection of the shipping line employed to carry the cargo was familiar with the vessels used and the nature of the holds, and one would presume with the vessel's capabilities.



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The cargo of coiled sheet steel was produced at a steel mill in Fumabashi, Japan for importation by the consignee for resale within Australia. Some of the sheet steel was galvanised and some was aluzinc. If the surface of freshly galvanised or aluzinc coated steel is allowed to come into contact with water, corrosion in the form of white rust will occur. A temporary protection from corrosion may be applied to the coil by a

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chromate coating. At the request of the consignee, the steel coils were unchromated, but were lightly oiled which left the steel coil particularly susceptible to corrosion from contact with water.

Soon after production at the steel mill, the coils were wrapped with an inner single sheet of paper lined with a film of plastic and fitted with an outer metal wrapper composed of waste steel sheet. The packaging contained a note requiring that the cargo be kept dry. The coils were then transported by covered barge from the Taiyo mill to the loading wharf.

Importantly, The Court made the following findings:

- the shipping manager responsible for the selection of the shipping line employed to carry the cargoes in question was familiar with the vessels and the nature of the holds;
- it was not a standard practice within the industry to transport steel sheet coils in vessels equipped with dehumidifying systems;
- the carrier was not informed that the steel coils were shipped in an unchromated state;
- rain occurred during loading operations of both vessels;
- there was water within the holds of both vessels prior to the commencement of their respective voyages having entered the holds with other cargo and dunnage. The amount of water in the holds meant that condensation during the voyage was virtually inevitable without taking active measures to remove the water from within the holds;
- the damage to both consignments of cargo was caused by condensation within the holds, rather than direct contact with water, which could have occurred prior to loading;
- packaging of the coils was in accordance with standard practice for the packaging of steel of the nature of the coils in question;

- the cargo was not water damaged on loading, despite the presence of water on the outer wrappings.

The Law

It was common ground that the parties obligations were governed by the Australian Carriage of Goods by Sea Act (Cth) 1991, enacting a modified version of the Hague-Visby rules. The cargo interests relied upon breach of Article 3 Rules 1 and 2 claiming that the carriers did not exercise due diligence to make their vessels seaworthy and their holds fit for carriage of the coils, or alternatively did not carefully and properly care for the coils during the voyage. The duties under Article 3 attract at the commencement of each voyage and are imposed by reference to the particular cargo on the particular voyage to the particular destination. In defence, the carriers submitted that the shipper did not pack the coils sufficiently to prevent the ingress of water, whether in liquid or vapour form.

The Court framed the “essential question” as whether the carriers were entitled to assume that the packaging of the steel coils was such that water in any form could not penetrate the packaging, or whether the shipper and the consignee were entitled to assume that there would not be sufficient water, either as liquid or vapour, in the holds of the vessels for condensation to occur on the coils.

Although the Court found that the packaging of the coils was not such as would prevent the ingress of water in the form of vapour, it held that the carrier nonetheless failed to discharge its burden of proof to exercise due diligence to make their vessel’s seaworthy. In the circumstances where the cargo in question was known to be sensitive to moisture, and the carrier ought to have foreseen that water would be admitted into the holds on other cargo and on dunnage and possibly because of rain, the vessels were not seaworthy for the purpose of carrying the cargo in question on

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that particular voyage at that time of year. During the voyage from the Japanese winter across the equator to Australia, the condition of the air within the hold and the temperature of the steel coils would change, ordinarily creating the conditions for condensation to form on the cargo. The judge determined that it was reasonable for the carriers to take steps to ensure that water would not be admitted into the holds, or to install a dehumidification system to remove excess water from the holds to prevent condensation. The failure to take these measures was a failure to use due diligence to make the vessel seaworthy and to make the holds fit and safe for the carriage of the coils.

Conclusion

The effect of this decision may mean that shipowners and charterers will have no option but to invest in temporary modifications to their vessels to satisfy the due diligence requirement under Australian law depending firstly, on the type of cargo to be carried and secondly, depending on the likely weather patterns encountered. Such modifications will inevitably be passed on to cargo interests in the form of higher freight rates.

This decision overlooks the fact that in the circumstance of this case, the shipper, who should be regarded having superior knowledge of its cargo, deliberately chose to ship its cargo on a vessel without the use of dehumidifying or heating systems within the hold. In future cases, shippers will not have the option to utilise these lower freight rate vessels as carriers are forced to adopt modifications to their vessels to prevent future cargo claims.

This decision is under appeal.

This decision, if affirmed on appeal, further tips the balance in favour of cargo interests on cargo claims litigated in Australia. The initial burden of proof to be satisfied by cargo interests has always been a relatively easy

hurdle to jump. The cargo interests must provide evidence of the initial condition of the cargo, and the outturn of the cargo. The burden then shifts to the carrier who must establish either that they exercised due diligence to prevent the loss or that the loss was caused by one of the accepted perils/defences available under Article IV Rule 2 of the Hague-Visby Rules. Prior to this decision, the question of whether the carrier had met its obligations under the Hague-Visby Rules was assessed by reference to the vessel's current structure, with the tools, apparatus and systems then on board the vessel. This assessment was reasonable, particularly where the cargo interests had knowledge of the vessel's capabilities. This decision places a positive obligation on carriers to actively modify their vessels, even when these modifications or capabilities were not requested by the cargo interests. This obligation raises difficulties for many carriers since they may operate in areas where it is difficult to source the necessary equipment such as dehumidifying systems and the personnel who are trained to use them.

Further, it also appears that carriers may need to obtain more specifics of cargo to be carried, as well as the mode and type of packaging. This will certainly apply to steel cargoes and to cargoes where particular types of treated steel are susceptible to sweating causing rust.

It follows that the clausing of the bills of lading and mates receipts must be sufficiently strong to at least raise the bar for any would-be claimant.

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Companies that charter vessels face significant potential risks. Vessel values frequently run into tens of millions of dollars and even after recent corrections, the freight market is still at historically high levels. When events transpire against the charterer they can end up facing multi-million dollar losses. Some typical situations that can have a material impact on a charterer's balance sheet include being held responsible for sending the vessel to an unsafe berth or port, the vessel sinking, supplying poor quality bunkers, an adverse movement in the freight market, or the failure of a counterparty.

Claims executives and operational staff are normally well aware of these potential exposures; but over recent years the average value of serious losses has risen sharply. Senior management needs to be fully apprised of the true 'financial' risk and to be aware that their corporate exposure to chartering activity is not just limited to the wording of the respective charterparty, or the bill of lading form. For example, a charterer with deep pockets may find himself in the firing line due to the failure of a counterparty.

To help raise awareness and address some of these issues, The Charterers P&I Club has

joined forces with The Baltic Exchange to organise a risk management seminar at Trinity House, London on 9th November 2006. The objective of this seminar is to explore the risks associated with chartering vessels and how such risks can be effectively identified, controlled, managed and/or transferred. The main focus will be on charterers rights to limitation, the management of counter-party risk and the use of financial instruments such as FFA's to hedge freight market risk. This event, which will be held on the morning of 9th November 2006, is aimed at senior chartering executives. The mornings proceedings will conclude with a lunch at Trinity House and will be preceded the night before by a cocktail reception at 30 St Mary's Axe one of London's most impressive architectural landmarks, with fantastic views over the City of London on a clear evening.



Attendance is free but places are limited to 120. In the event of being oversubscribed; then priority will be given to clients of the Charterers P&I Club. If you are interested in attending, or would like to propose topics for discussion; then could you please register on line at www.else.co.uk

The choice is yours

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