

Unpaid bunkers – the Dilemma for Shipowners and Bunker Traders

by Zeina Wakim - z.wakim@tamimi.com -

June 2014

Bunker fuel is the fuel oil used mainly in powering ships. It gets its name from the containers on board ships and in ports that it is stored in, which are called bunkers. Bunker fuel constitutes a fundamental element and one of the largest expenses in ships operation.

In difficult market conditions, this fact leaves bunker suppliers faced with delays in payment, non-payment or requests to provide credit terms.

One of the common features of bunker supply contracts is the allowance of all or part of the purchase price to be paid after delivery of the bunker fuel. For the past few years, when the market condition was difficult and the bunker prices were high, these credit terms affected bunker traders since they were left unpaid for the bunker they supplied. In addition, shipowners were faced with an unexpected risk of vessel arrest pursuant to the action *in rem* initiated by the unpaid bunker traders who supplied the vessel with bunkers at the request of charterers.

The supply of bunkers at the request of the vessel's charterer is the most common practice in the industry. When merchant vessels are not trading under the owners' control, owners will not have any control over the purchase of the bunker by charterers (and consequently the fulfillment of the charterer's obligations under the bunker supply contracts) where the vessel is chartered out on a time or bareboat charterparty.

Arrest threat – Is a bunker claim a maritime claim?

Ship arrest is an excellent way to obtain security for a claim and potentially prepare for a judicial sale of the vessel, should that become necessary. In addition, ship arrest constitutes a considerable pressure on the debtor to settle the claim due to the business disruption which usually leads parties to amicably settle the claim. Therefore, arrest may be a suitable remedy for a variety of creditors, such as unpaid bunker traders, since a bunker claim has been categorised as a maritime claim in many jurisdictions where the 1952 Arrest Convention has been ratified or where similar wording has been incorporated into domestic legislation.

Under the Arrest Convention of 1952, an arrest may be made on a vessel in respect of which the maritime claim arises if the owner is liable for the claim or if, under the applicable law, recovery against the vessel following such arrest is possible. Article 1(1) of the 1952 Arrest Convention lists these maritime claims.

These different claims are enumerated in Article 115 of the UAE Maritime Commercial Code being Federal Law No. 26 of 1981 (as amended) (the "Maritime Code") as follows:

1. Damage caused by the vessel by reason of a collision or otherwise.
2. Loss of life or personal injuries occasioned by the vessel and arising out of the use thereof.
3. Assistance and salvage.
4. Contracts relating to the use or exploitation of the vessel under a charterparty or otherwise.

5. Contracts relating to the carriage of goods under a charterparty, bill of lading, or other documents.
6. Loss of or damage to goods or chattels being carried on board the vessel.
7. General average.
8. Towage or pilotage of the vessel.
9. *Supplies of products or equipment necessary for the utilisation or maintenance of the vessel, in whichever place the supply is made.*
10. Construction, repair or fitting out of the vessel, and costs of it being in dock.
11. Sums expended by the master, shippers, charterers or agents on account of the vessel – or on account of the owner thereof.
12. Wages of the master, officers and crew, and other persons working on board the vessel under a contract of maritime employment.
13. A dispute as to the ownership of the vessel.
14. A dispute in connection with the co-ownership of the vessel, or with the possession or use thereof, or with the right to the profits arising out of the use thereof.
15. A maritime mortgage.

In addition article 117 of the Maritime Code stipulates that the vessel may be arrested for a maritime debt for which the charterer is responsible if the following conditions are met:

1. the vessel arrested is the concerned vessel (i.e. not a sister vessel); and
2. the charterer has the navigational management of the vessel, namely where he is a time charterer or a bareboat charterer and not a voyage charterer.

Therefore, the merits of a vessel arrest will depend on the jurisdiction in which the vessel is being arrested since in certain jurisdictions an arrest order will only be granted if the debtor is the owner of the vessel. In the UAE, a vessel may be arrested for a bunker claim where the bunkers were ordered by the charterer as long as the conditions stipulated in article 117 of the Maritime Code above are met. However, the issue that remains unsolved in the UAE is whether the courts will issue a judgment in the main action that needs to be filed after the arrest order against the owners obliging them to pay to the bunker traders their unpaid invoices.

Notwithstanding, if the arrest of the vessel for a bunker claim (where bunkers have been ordered by a charterer) is not possible, will the arrest be possible on the grounds of a maritime lien?

Arrest threat – Does a bunker claim give rise to a maritime lien?

A maritime lien is a secured right in the property (whether vessel, cargo, freight or bunkers) which arises with the claim without registration or other formalities and which travels with the vessel surviving its conventional sale (not its judicial sale). In general, the issue of whether an unpaid bunker trader will have the right to a maritime lien will differ from one jurisdiction to another.

Under English Law, maritime liens are strictly limited to a number of claims (such as salvage claims damages caused by the ship and crew wages) and bunker traders will not have a maritime lien.

Unlike English Law, the US Maritime Lien Act provides that an unpaid bunker trader will have a maritime lien against the vessel where the bunker was ordered by “a person authorised by the owner”. This Act states that an officer or agent appointed by the charterer is “presumed to have authority to procure necessaries (bunkers) for the vessel”. In this context it must be noted that it remains possible to rebut the presumption that the charterers had authority to order the bunkers for the vessel.

In addition, and as a general rule, the US Courts will not apply the Maritime Lien Act to every arrest in the USA. They will only apply it if there is a close contact between the bunker supply and the USA. In other words, the more contacts the bunker supply has had to the USA the more likely it is that the owners and their vessel may be found to be a party to a contract between the bunker trader and charterer.

The International Convention for the Unification of Certain Rules of Law Relating to Maritime Liens and Mortgages of 1926 (the “Lien Convention”) has enumerated in article 2 the claims that give rise to lien on the freight for the voyage during which the claim giving rise to the lien arises, on the accessories of the vessel and freight accrued since the commencement of the voyage.

The Maritime Code has adopted wording similar to that of the Lien Convention. Article 84 of the Maritime Code exhaustively lists the maritime liens on the ships. The claim for “necessaries” listed at article 84 is defined as follows:

“Debts arising out of contracts made by the master, and operations carried out by him outside the port of registration of the vessel within the scope of his lawful powers for an actual requirement dictated by the maintenance of the vessel or the continuance of its voyage, whether or not the master is also the owner of the vessel, or whether the debt is due to him, or to persons undertaking supply, or lenders, persons who have repaired the vessel, or other contractors.”

Bunker supplies will, therefore, be considered as “necessaries” for the ship and/or the voyage.

In this context it must be noted that under UAE Law, unlike English Law, a claimant having a claim secured by a maritime lien will not have an automatic right to arrest the vessel in the UAE territorial waters. He will only have this right if his claim falls within the list of maritime debts defined in Article 115 of the Maritime Code.

Will invoicing to master and owners change the situation?

It is common practice in the bunker industry to issue invoices to the “master and/or owners and/or operators and/or managers and/or charterers c/o” (or similar wording), followed by the name of the person or company actually ordering the bunkers. Does this type of invoicing give the bunker trader the right to arrest the vessel for unpaid bunkers even if ordered by the time charterer of the vessel?

In principle, the invoicing method cannot change the contractual relationship of the bunker supply which is between the bunker supplier and the charterer. The general rule under every legal system is that a contractual claim, such as one for the sale of bunkers, is a claim “in personam”, against a particular person who is a party to the supply contract. Thus, under many systems of law, a claim for the supply of bunkers to a time-charterer cannot be enforced against the ship.

However, even though the obligation to provide and pay for bunkers under a time charterer rests with the defaulting charterer, and the bunker supplier does not have privity of contract with the vessel and its owner, the owners and their ships are still vulnerable to action in many jurisdictions.

Therefore, invoicing to the “master and owners” and including all sorts of clauses in general trading conditions as mentioned could help in changing the position of the unpaid bunker trader and makes sense from his point of view but will not have a legal impact on the bunker supply contractual

relationship.

Recommendations to bunker traders

The starting point is to conduct a risk assessment for each supply. Any new customer, shipping operator with bad credit history or shipping operator that does not have a repeated presence in the jurisdiction might be identified as a potential credit risk. In addition, dealing with single ship companies might be regarded as a potential credit risk. It might be appropriate to require upfront payment or at least a substantial deposit for any such supplies.

The next most important thing is to establish a solid legal foundation for the supply, namely a well drafted contract with good terms and conditions. These terms and conditions will provide the legal foundation for many rights of enforcement that a bunker trader might not have under general law. Issues involving the terms and conditions of the contract can include retention of title (the bunkers remain the property of the supplier until paid) and the enforcement of rights against additional parties. In fact, bunker supply terms and conditions often try to address this very issue by saying that any supply is made jointly to the person ordering the supply and to the owner/vessel and that enforcement action can be taken against any or all of them. Therefore, the lack of privity between the owner and the bunker trader may be overcome if notice of the terms and conditions of the supply contract is given to the owner.

Some bunker traders try to obtain the benefit of the maritime lien recognised under the US law by stating in their terms and conditions that US law will apply to the contract. In the UAE, this type of clause does not add anything in this regard since bunker claims give rise to a maritime lien and the bunker trader should, therefore, have a right to arrest the vessel as his claim is a maritime debt in accordance to article 115 of the Maritime Code.

It is paramount for bunker suppliers to ensure that they know that they are contracting with the actual shipowner. They also need to ensure that all the documents and communications reflect this accurately and beyond doubt. This is especially important when intermediaries are involved. Failure to do so could result in a situation where the bunker supplier ends up with no security for its claim and no hope of ever obtaining payment of its bunker invoice.

Bunker suppliers should also consider insisting that payment for the supply is guaranteed by another entity, such as a group parent or holding company. Of course, the financial standing of the guarantor must be well considered as a guarantee is only as good as the financial standing of the guarantor.

Recommendations to owners

P&I Clubs have warned their shipowner members to protect themselves from the increasing risk of claims for charterers' unpaid bunkers and recommended that any members, who may be exposed to such a risk, seek legal advice from local counsel regarding the matter prior to the vessel's entry into port.

As a precaution, and to avoid a maritime lien over their vessel, some owners insert in their charterparties an anti-lien clause with wording identical to that of clause 18 of the New York Produce Exchange (NYPE) form. This clause stipulates that *"Charterers will not suffer, nor permit to be continued, any lien or encumbrance incurred by them or their agents, which might have priority over the title and interest of the owners in the vessel"*. This anti-lien clause may also be amplified, as suggested by BIMCO, by the addition of the wording below:

"In no event shall Charterers procure, or permit to be procured, for the vessel, any supplies, necessaries or services without previously obtaining a statement signed by an authorized representative of the furnisher thereof, acknowledging that such supplies, necessaries or services

are being furnished on the credit of Charterers and not on the credit of the Vessel or of her Owners, and that the furnisher claims no maritime lien on the Vessel therefore”

However, the effect of such clauses on the creation of a lien remains unclear if not notified to the bunker trader, who has no contract with the owner of the vessel.

Other owners tend to send to bunker traders a prohibition of lien notice prior to the vessel being supplied with bunkers. In addition, masters are tending to stamp the bunker delivery receipt with clauses stipulating that bunkers are not for the account of the ship and are ordered solely for the account of the charterers and that no lien or any claim against the vessel or her owners can arise thereof.

Nevertheless, all these precautionary measures will still not prevent bunker traders from creating a lien on the vessel in every jurisdiction.

The nature of the bunker supply business places bunker suppliers and shipowners in a precarious position especially when the bunkers are ordered by the charterer of the vessel. Reconciling the conflicting interests of the maritime claimants and shipowners has always been a controversial issue. From the bunker trader's perspective, the right to arrest a ship is the single most valuable tool in enforcing his maritime claims and recovering his debts against ship owners and operators. From the viewpoint of shipowners and mortgagees, it is equally essential that a wrongful arrest, attachment, or injunction against a ship does not interrupt its legitimate trading. This struggle between two opposing interests has, for centuries, created a dichotomy, and the proper legal recourses are still being debated today.