Lessons Learnt from the O.W.Bunker Saga: A UAE perspective

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This article considers the case itself, how courts around the world have construed the O.W.Bunker contractual framework differently, the issues caused by this varying judicial interpretation and some of the potential legal solutions suggested in the market to avoid the double payment conundrum in the future. This article considers matters from a UAE perspective but in order to do so it is necessary to review the approach of the courts on an international basis.

The double payment demands

OW Bunker & Trading A/S and OW Supply & Trading A/S and its subsidiaries ("OWB") went into liquidation in November 2014. As a result, physical suppliers ("PS") across numerous jurisdictions moved quickly to demand payment directly from shipowner debtors for supply of fuel to their vessels and relied upon numerous causes of action to bring their respective claims. Ship arrests soon followed when immediate payment was not forthcoming.

In parallel the OWB entities in liquidation were not slow to issue payment demands on behalf of the OWB estate, pursuant to the terms of the respective sale contracts. It soon emerged that OWB had concluded, one year prior to its collapse, a revolving borrowing base credit facility for a sum of USD 700m from various lenders represented by ING Bank N.V ("ING") as the security agent. ING purported to have a valid security agreement over the trade receivables due to OWB from the shipowners and accordingly pursued shipowner debtors, often arresting their ships to recover the same debts demanded by PS.

For shipowner debtors, the dilemma as to which party to pay for the fuel supply remains. Most shipowners are willing to settle the dues but, understandably, do not want to pay for the same bunkers twice. As will be noted, the respective courts have sought to deal with this issue through various different applications of legal theory.

How have the courts ruled across the world?

England

The shipowners in (The Res Cogitans) [2015] EWHC 2022 (Comm) argued that the OWB sale contract with the shipowner purported to be a contract for the sale of goods falling under the Sales of Goods Act 1979 ("SOGA"). In order for a claimant to bring an action for the contract price under SOGA, title in the goods must have passed to the buyer for money consideration. The owners argued that title could not have passed from OWB to the shipowner for two reasons; firstly the PS still had property over the fuel by way of a retention of title clause and, secondly, because the fuel was mostly consumed prior to payment at the expiration of the 30 day credit period, at which point title in the goods would ordinarily pass. Since the goods were consumed during the 30 day credit period, there was, owners argued, nothing to pass title in at the expiration of the credit period.

The Court of Appeal took the view that the bunker supply contract between OWB and the shipowner was a 'hybrid' contract comprising, firstly, a license to consume the bunkers immediately upon delivery without

title having to pass, and secondly, a sale contract pertaining to the unconsumed bunkers on board when payment fell due at the expiration of the credit period. With regard to the license, the Court concluded that OWB's ability to pass title to the owners was irrelevant and that OWB's claim was a straight debt claim. However, the agreement to sell the unconsumed fuel at a later time would require the title to pass to the buyers upon payment and so the SOGA would apply to this element of the contract.

In our view, the Court of Appeal's application of legal theory represents quite a divergence from the contractual intentions of the parties. No doubt those working in the bunkering community would not describe their trade activities as the sale and purchase of licenses to consume fuel immediately and agreements to sell the remaining unconsumed fuel after the credit period expiration. It appears to be quite a creative decision in this respect and the Supreme Court may yet constue the contractual framework differently when the resultant appeal is heard.

Pending the outcome of the appeal ship ownerscan, reasonably conclude that the SOGA cannot be relied upon to avoid payment to OWB and OWB are deemed entitled to full payment. However, the decision does not prevent ships from being arrested in different jurisdictions and so the double payment conundrum persists.

Singapore

In Singapore, a consolidated interpleader application was filed by thirteen owners and charterers in Precious Shipping Public Co Ltd v OW Bunker Far East (Singapore) [2015] SGHC 187. Interpleader relief is designed for situations whereby a third party debtor wishes to pay a debt but is subject to two or more competing claims over the same debt. The competing claims must be adverse to one another and the court's decision should extinguish the non-legitimate claim(s) to provide legal certainty on liability. The third party debtor, as applicant, will pay the debt amount into the court in order that the court may determine entitlement to it.

In order for the Singapore High Court to make an order for interpleader relief, the applicant must first adduce evidence that there is prima facie evidence of competing claims. After assessing the PS's claims in bailment, retention of title, unjust enrichment, unlawful conversion of property and the option to exercise maritime liens in other jurisdictions, the court held that the PS had no case that could be defined as an adverse competing claim and that the PS was simply seeking to circumvent the insolvency procedure. To rule that the PS had a valid claim would, according to the court, be "unfair" and "unjust". Therefore, the interpleader application was dismissed and no order was made.

The Singapore Courts appear to have upheld the contractual intentions of the parties in this case by recognising the PS's potential claim, but limiting it to a liquidation claim against the OWB estate. Again, the double payment conundrum remains live because vessels who might pay OWB in Singapore may still be arrested by PS in other jurisdictions for the same sum.

Canada – Canpotex Shipping Services Limited v. Marine Petrobulk Ltd., [2015] FC 1108

Conversely, in September 2015, further to USD 600,000 being deposited by the charterer into court for interpleader relief, the Canadian Federal Court found that the PS was entitled to full payment and that OWB had no claim against the shipowner. Central to the decision was the finding that the PS General Terms and Conditions ("GTCs") bound both OWB and a charterer by virtue of the valid incorporation of the PS's GTCs into OWB's GTCs. The PS's GTCs provided for a right of arrest against the shipowner directly in the event of non-payment and had the effect of making the shipowner and OWB jointly and severally liable for the fuel. The PS's GTCs were also governed by Canadian law and Canadian law is unequivocal that intermediaries cannot claim against vessels where the intermediary has not paid the supplier for services delivered to the vessel. Upon OWB's failure to pay for the fuel, the valid incorporation of the PS's GTCs into the contract between the shipowner and OWB had the effect of creating a direct contractual right of action against the shipowner by the PS. Upon payment by the charterer of the contract price, the charterer was released from any further obligation to pay OWB because OWB was held to have breached

its contractual obligation to pay for the fuel.

The Court's ruling in this case is refreshingly practical and probably best reflects the contractual and commercial intentions of the parties. However, it is acknowledged that the case is limited because we do not know how the courts would rule if the PS's GTCs were not incorporated into OWB's GTCs.

United Arab Emirates

Unlike the common law jurisdictions mentioned above, the UAE adopts a civil law legal system. Under the civil law, the bunker delivery receipt ("BDR") has historically been recognised as a valid and binding contract on the shipowner in its own right, premised on Articles 135, 137(2) and 154 of the Commercial Maritime Code (Federal Law No. 26/1981 hereinafter the "CMC") which makes shipowners liable for contracts concluded by the Master on behalf of the vessel. For many years we have observed courts across the entire Gulf region rule in favour of the PS pursuant to the BDR and there is no reason to anticipate change because the courts in the Gulf, being paper-based, have always viewed the stamping of a BDR as proof of offer and acceptance in the formation of a contract.

After the collapse of OWB, many PS in the Gulf sought to recover unpaid supply dues from shipowners on the premise that the BDR constituted a contract under UAE law. This was contested by shipowners, OWB and ING because the notion of the BDR is derived from court trends, custom and practice, coupled with an interpretation of provisions of the CMC. We doubt whether the OWB branch in Dubai really was aware during day-to-day practice that a contract arose through stamping and signing of the BDR and it is difficult to measure how many PS were aware of this either.

At the end of 2015, the Khorfakkan Court of Appeal affirmed this interpretation of the law by giving credence to a PS claim under the BDR, deeming it to be a valid contract evidenced by the vessel seal and Master's signature. The Fujairah Court of First Instance recently ruled in a similar manner. Notably in the Khorfakkan case, ING's claim under the security instrument was rejected by virtue of OWB's inability to demonstrate its claim over the trade receivables in the first place. OWB failed at the first hurdle. However, this decision is subject to appeal to the Court of Cassation and can merely be considered as guidance, not precedent.

In our view, the UAE Court's application of legal theory is, probably, the most divergent from the actual contractual intentions of the parties involved. The intentions of the parties to establish a third contract between the shipowner and PS by way of BDR is tenuous at best, at least from the shipowners' perspective. It is most likely the shipowner believed he was contacting with OWB only.

One key issue is that OWB conducted business as full traders and invoiced for the principal sum plus their profit element. Had they invoiced for a brokerage or agency fee representing their actual mark-up only, then the community could probably have avoided this whole saga.

Lastly, it is noteworthy that most of the claims seen by the court follow from PS arrests whereby the principal sum only was claimed. In these instances, for the reasons mentioned above, we believe the PS will usually succeed. However, this does not mean OWB's claim falls away, it simply means they will be able to claim, independently, for their mark-up only. Had OWB brought the claims in the first place, perhaps the court would have ordered that the shipowner debtors make split payments accordingly.

Interpleader relief in the UAE

There is no legal provision under UAE law for interpleader relief actions, as seen in Singapore and the Canadian cases above. This means that shipowners who wish to pay their bunker invoices still have no way to pre-empt arrests and there have been few alternative solutions suggested.

Although it is not possible for the shipowner to avoid arrest in the UAE, the shipowner who has had its vessel arrested can reduce legal expenses by joining the intermediary or PS to the proceedings. At this

stage, the shipowner can request the court to receive the debt amount into court and for the court to decide whether the intermediary or the PS is entitled to it. The shipowner can then, in practice, reduce its involvement in the case by not attending hearings or making any submissions. Whilst not an interpleader action, it is perhaps the next best way to compel the intermediary and the PS to litigate and resolve the competing claim.

Is it 'business as usual' for the UAE bunkering community?

Yet again, we have observed that no company is too big to fail and the vulnerabilities hidden in long-standing industry practices can be exposed by the failing of one link in the contractual chain. The market has offered up some potential solutions as outlined below.

The OWB saga emphasised the risks involved when ordering bunkers through intermediaries. Loss prevention circulars have emerged from Protection & Indemnity clubs recommending that shipowners deal directly with PS, thus eradicating any risk of double payment demands. We consider it likely that shipowners with wider geographical trading limits may be slow to implement such changes because intermediaries often have access to markets that shipowners do not.

Another proposal is that shipowners should contract to split payments between the intermediary and PS and only to pay the mark-up and principal sum to the parties respectively. It would follow that if the shipowner cannot make payment for bunkers, or the intermediary goes into liquidation, the intermediary can only sue in contract for the profit element and not the full sum thus avoiding any risk of paying the principal sum twice. However, we believe this suggested solution only works legally and does not offer a commercial solution because the intermediary is unlikely to disclose its mark-up and agreeing to such a contractual arrangement would leave it at risk of being cut out of future transactions.

Finally, one last proposal that has been mooted involves amending the payment provisions in the contracts requiring the intermediary to pay the PS, or the preceding intermediary, before payment becomes due from the shipowner. In essence, the effect would be to provide the shipowner, as end buyer, the longest credit period and would ensure double payment demands would be avoided. If there is a longer sale chain then transacting parties would contract on back-to-back terms. As above, whilst this offers a workable legal solution, we do not consider that it is a commercial one. The proposal involves the shifting of risk of non-payment away from the PS to the intermediary in the instance that the shipowner defaults on payment. We do not envisage intermediaries accepting this transfer of risk.

In our view, intermediaries and PS could better align themselves in contract on their debt recovery strategies. For example, parties could agree from the outset that in the event of non-payment, the PS will refrain from pursuing the debtor if the intermediary pursues the recovery on behalf of both entities, sharing the cost of such recovery with the PS. This would avoid double payment demands upon the shipowner, would facilitate faster recovery and not disrupt the status quo.

To conclude, whilst there are some legal solutions on the table, few are commercially viable.

Considerations for all

The OWB saga continues and the courts have grappled with the application of legal theory to a a complex commercial structure in courts around the world. The decisions in England, Singapore, Canada and the UAE are indicative of the courts' collective failure to produce a globally uniform solution to a global bankruptcy. This failure is reflective of the intricate differences between the facts in each case and the legal theory applied in each jurisdiction.

What is clear, is that a one-size-fits-all solution is unlikely to be forthcoming and by the nature of the international business of shipowners, their ships are likely to remain at risk of arrest and double payment demands for some time.

Solutions have been proposed to improve industry practice in order to avoid a similar OWB situation from occurring again, however we have demonstrated how such suggested changes may be commercially inconvenient and improbable. If intermediaries and PS could better align themselves in their approach to debt recovery then this would certainly represent progress.