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Hans Jacob Bull

Professor, leader, mentor and friend

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Director's preface

This year's edition of SIMPLY is dedicated to Professor Hans Jacob Bull, who celebrates his 70th birthday in August 2011. The Institute will celebrate Hans Jacob's birthday with a seminar to be held on August 24, which will feature the topics of several of the articles published in this edition. We chose to celebrate Hans Jacob's birthday in this way because we knew that he did not want a *festschrift*. However, so many of Hans Jacob's friends wanted to honour him that this edition of Simply sets a record with a total of 16 articles.

Hans Jacob was born in Oslo on 18 August 1941. He was candidate of law (Norwegian master of law degree) in 1967, thereafter practising as an associate district judge and associate attorney before taking up a research fellowship at the Scandinavian Institute of Maritime Law in 1971. This was the start of a long and successful relationship with the Institute, where Hans Jacob has stayed ever since. Having served as assistant professor and then associate professor at the Institute, in 1988 he both obtained his doctor juris degree and took over his chair as a professor of law. The most significant step in his career occurred in 1989, when he was elected Director of the Institute, a position that he held until 2001. Even after stepping down from this position, Hans Jacob has stayed on at the Institute, where he remains to this day.

Needless to say, Hans Jacob's personality and attitude have had a strong influence on the Institute during his long "captaincy". Like previous directors, he aimed to make the Institute a meeting place for enthusiastic young researchers from all the Nordic countries, with a focus on friendliness, support, the sharing of ideas and tolerance. During his long term as director, he taught the next generation the very best lessons in leadership and compassion, showing us how to keep all the diverse inhabitants of an academic institute not only together, but happy to be so.

During Hans Jacob's time at the Institute, he has supervised projects undertaken by numerous research assistants, doctoral candidates and

colleagues. In this traditionally male-dominated field, he has given particular encouragement to female researchers at all levels, from research assistants to professors.

Despite his emphasis on supervising and helping young researchers, Hans Jacob has also managed to undertake his own research projects. Among his many books and articles – an overview of which you will find in the bibliography included in this edition of *Simply* – we would like particularly to mention *Scandinavian Maritime Law*, which for a decade has been the leading Scandinavian maritime law textbook. From recent years we should also mention the *Handbook in Hull Insurance* (2006), *Insurance Law* (2008) and the *Commentary to the Ship Safety Act* (2010). As well as summing up Hans Jacob's main legal interests, these three books also demonstrate his practical approach to the law, an approach that in turn is reflected in the general attitude at the Institute.

Hans Jacob's practical grasp of the law has also put him in great demand among Norway's legal community. In recent years his activities have included the chairmanships of the drafting committee for the Ship Safety Act (2007), of the Norwegian Marine Insurance Plan Committee from 1993 to 2007, and of the Norwegian Cargo Clauses Committee, which drafted the Cargo Clauses of 1995 and 2004. He has also authored numerous legal submissions and has acted as arbitrator in many disputes.

With such a busy working life, one could be justified in thinking that Hans Jacob would have no time for hobbies. This would be quite mistaken: another part of his life belongs in Alvdal, where he divides his time between the Kjell Aukrust Museum and the cross-country ski runs. But even here Hans Jacob is unable to rest his pen, as demonstrated by two articles in the Nord Østerdalen yearbook.

On a personal level, I have been fortunate enough to benefit from all the positive qualities described above. As we share a common interest in both general and marine insurance law, we have undertaken much research and practical work together. I am a great admirer of Hans Jacob's practical approach, logical thinking and his straightforward

and clear style. Hans Jacob has also been a mentor, advisor and friend for many years. His door is always open, and he combines his powers of legal reasoning with great wisdom. Even though he may now be approaching retirement, I sincerely hope that both the Institute and myself will be able benefit from his wisdom for many years to come.

On behalf of the Scandinavian Institute of Maritime Law, I congratulate Hans Jacob very warmly on the occasion of his birthday and wish him many more enjoyable and productive years at the Institute.

During 2010, the Institute has continued to pursue the research priorities of previous years. The ship safety project continues in cooperation with other research institutions in the fields of law and social sciences in Norway, the Nordic countries, Russia and elsewhere. The project, which is chaired by Professor Erik Røsæg, is currently employing several PhD candidates and research assistants. In particular we should mention that a new PhD candidate from Russia has joined the project. Many publications have already been generated by the project and more are forthcoming. The petroleum law department is also involved in the project, with one PhD candidate about to finish her thesis about safety in the petroleum sector. The project is financed from various sources, including the Norwegian Research Council, the Scandinavian Council of Ministers, the Norwegian Oil Industry Association and the Johan and Mimi Wessmann Minnefond.

More information about the project may be found at <http://www.jus.uio.no/nifs/forskning/prosjekter/sjosikkerhet/index.html>.

In the maritime law department we are also continuing our research into traditional maritime contract law, with a particular focus on multimodal contracts and the newly signed Rotterdam Rules. As a part of this, our third research assistant, who is funded by the Norwegian P&I club Skuld, has written a thesis about the risk exposure of P&I insurers for cargo damage, including potential exposure under the Rotterdam Rules. We are also extending our focus to include offshore charter parties.

Research during 2010 at the department of petroleum and energy

law has concentrated on energy-market issues (among others, one PhD candidate is working on multi-level governance in the energy sector, while another is writing about the design of, and trading rules for, green certificates schemes) and topics related to contract law (including contracts for the removal of decommissioned offshore installations and R&D contracts).

As in previous years, 25% of the Institute's funding for 2010 came from the Scandinavian Council of Ministers, for which we are, of course, extremely grateful. Our other main sponsors are:

- the Norwegian Oil Industry Association (OLF)
- the Ministry of Petroleum and Energy/the Research Council of Norway
- the Eckbo Foundation
- Johan and Mimi Wessmanns Minnefond
- Skuld.

We are very grateful to all our sponsors.

We would also like to express our gratitude to the numerous practitioners who help us year after year with lectures, student advice, information and examinations, in most cases without any fee. Their contribution is important in making the Institute what it is: a meeting place for young as well as established researchers, practitioners and students, all of whom combine open-minded enthusiasm for new knowledge with penetrating analysis. In particular, we are delighted with the way in which practitioners as well as researchers from other institutions have contributed to our specialised masters programmes. In 2010 these included the North Sea Energy Law Programme, organised jointly by the universities of Aberdeen, Copenhagen, Groningen and Oslo (by our petroleum law department), which offered high quality postgraduate level training for legal practitioners in the energy industry.

More than two dozen evening seminars were held during the year, as well as half-day seminars in cooperation with the Norwegian Shipowners' Association. In addition, the Institute both arranged and co-arranged several longer seminars than ran over periods of several days. The 24th Nordic Maritime Law Conference was held in Reykjavik

in August 2010, with 88 participants from the Nordic countries. The topics were “Piracy” and “Agreements on logistics”. Also in August 2010 the Ship Safety project cooperated with its Russian partners to organise a broadly defined seminar in Alta. Meanwhile, in May 2010, the Institute coordinated the Sixth European Colloquium on Maritime Law Research (ECMLR) in cooperation with the University of Swansea, focusing on the Rotterdam Rules. The planned Biannual Colloquium in Maritime Law (IBCML) in Southampton in the UK was finally held in October 2010 following a delay due to financial problems. The seminar was arranged cooperatively by the Institute, the University of Southampton, and the University of Tulane. The topic was “Maritime Conflict of Laws”. The annual European Energy Law Seminar (EELS), organised by Nederlandse Vereniging voor Energierecht and University of Groningen in cooperation with the Institute, took place in Noordwijk aan Zee in the Netherlands in April 2010.

We hope to be able to hold further joint seminars in the future.

Trine-Lise Wilhelmsen

Editor's preface

We are proud to present the 2010 edition of the Scandinavian Institute of Maritime and Petroleum Law Yearbook (Simply), which is dedicated to Professor Hans Jacob Bull on the occasion of his 70th birthday. The articles in this yearbook cover a variety of topics within international and European law and give readers an insight into Norwegian, Swedish, Finnish and Danish law. The yearbook includes articles by Hans Jacob's colleagues at the Institute and the Centre for European Law (also part of the Law Faculty of the University of Oslo), as well as by academics from the universities of Åbo, Stockholm, Gothenburg, Glasgow, Helsinki and Southern Denmark, who have all worked with Hans Jacob for many years.

We are also delighted to publish an article by Assistant Professor Marian Hoeks of the Erasmus University School of Law, Rotterdam, who gave a guest lecture at the Institute in the spring semester of 2010.

Professor Bull's commitment to his teaching and to helping his co-researchers by providing good and supportive advice has not hindered him from producing an impressive bibliography during the course of his career – both at the university and in connection with his participation in and chairing of law commissions, most notably on ship safety law.

The articles appear in alphabetical order by author. The collection begins with a contribution from Professor Finn Arnesen, who discusses whether the European Economic Area Agreement applies to activities beyond the territorial jurisdiction of Member States, as well as the subsequent Norwegian practice regarding the implementation of the EEA Agreement.

European law issues are also touched upon from different angles by other contributors. Professor Rosa Greaves and Svetlana Nasibyan write about EU competition law rules and their application in the maritime sector.

Professor Emeritus Erling Selvig analyses the interplay between the

rules of jurisdiction laid down in the Brussels I Regulation and Lugano Convention, on the one hand, and the Conventions on Limitation of Liability for Maritime Claims, on the other. He examines case law that partly resolves the complexities pertaining to forum shopping in cases involving the limitation of shipowners' liability and discusses the questions that the Brussels I/Lugano regime gives rise to in these types of cases.

Professor Hannu Honka writes about the MARPOL Convention Annex XI regulating air pollution from ships and discusses the relationship and possible conflicts between international treaties and EU law regulating the obligations of Member States with regard to shipping and environmental protection.

In his article on the new EU regulations on the rights of passengers to compensation from the carrier, Professor Erik Røsæg points out the considerable differences between the existing liability schemes in the relevant international conventions and also compares the application of the international conventions and EU law to passenger claims.

Three articles address various legal issues relating to the Rotterdam Rules, which create a uniform liability regime for the multimodal transportation of goods. The articles by Assistant Professor Marian Hoeks and Senior Researcher Ellen Eftestøl-Wilhelmsson provide a comprehensive description of the international conventions on the carriage of goods and discuss international and European efforts to create a uniform multimodal transport regulation. Professor Hoeks looks critically at Article 26 of the Rules, which establishes the "minimal network" rule, and at Article 82, which is aimed at avoiding conflicts with other conventions. She also discusses the interaction between the Rotterdam Rules and the Rome I Regulation.

Eftestøl-Wilhelmsson explores the relationship between the Member States' and the EU's competence to legislate within the area of international multimodal transport and studies the possible effects of the Rotterdam Rules on the EU's common transport policy.

Professor Svante Johansson examines yet another interesting aspect of the Rotterdam Rules, namely their impact on general average, and

investigates whether the Rules will result in the eventual decline of the concept of general average.

The article by Professor Emeritus Lars Gorton explores the linguistic aspects of commercial contracts and the implications of the legal formulations and statements contained therein.

Professor Emeritus Thor Falkanger analyses the complex issues that arise in cases where cargo has been lost during carriage by sea, in particular who is entitled to sue the maritime carrier under the Norwegian Disputes Act and the Norwegian Maritime Code.

Associate Professor Johan Schelin examines the road carrier's liability for cargo loss or damage in the light of *If v. Vikingstad* (Sweden, 2007) and discusses whether the carrier may incur other liability than carrier liability under the CMR rules (product liability) in connection with a contract for carriage of goods.

Tort law issues are addressed by Professor Peter Wetterstein, who considers whether and under what conditions interference with contractual rights could, under Finnish and Swedish tort law, give rise to a claim for compensation.

Petroleum law topics are addressed by Professors Ulf Hammer and Knut Kaasen. Professor Hammer examines the regulation of and legal issues pertaining to production licences as the main way of gaining access to the resources of the Norwegian Continental Shelf.

Professor Kaasen deals with legal issues pertaining to the payment obligations of companies subject to an obligation to set up a joint venture (under a Joint Operation Agreement) under the terms of a Norwegian production licence.

The Yearbook also contains two articles that shed light on legal problems relating to piracy. Professor Trine-Lise Wilhelmsen addresses insurance-related issues by examining the cargo owner's rights under the Norwegian Cargo Clauses to compensation by the insurer where the cargo has been captured by pirates.

Associate Professor Kristina Siig looks at the position under Danish law when dealing with compensation for occupational injury for (but not limited to) post-traumatic stress disorder suffered by crew members

following hijacking by pirates.

Last but not least, the Yearbook contains a bibliography of works by Professor Hans Jacob Bull, compiled by Librarians Kirsten Al-Araki and Inger Hamre.

The editorial committee is grateful to all the authors and peer reviewers for their contribution to Simply 2010.

Alla Pozdnakova

The EEA Agreement and activities off-shore

Finn Arnesen, Professor
Centre for European Law, University of Oslo

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1 Introduction

The vast extent of Norway's coastline suggests that activities associated with the sea, the sea's resources and the resources found under the seabed, should play a dominant role in Norway's economy. And indeed this is the case. These activities also give rise to a range of issues within almost all imaginable fields of the law.

The EEA Agreement is an association agreement between the European Community (now the European Union) and its Member States on the one hand and Iceland, Liechtenstein and Norway on the other. The agreement aims to establish a homogeneous European Economic Area, "with equal conditions of competition, and the respect of the same rules", *cf.* Article 1 EEA. Homogeneity in this context has a dual meaning. First, it implies that the EEA Agreement should be interpreted and applied in the same way throughout the EEA. Second, it implies that the provisions of the EEA Agreement should be given the same interpretation and application as the provisions of EU law they mirror.

One of the characteristics of the rules on the four freedoms, competition and State aid, as they follow from the Treaty on the Functioning of the European Union (TFEU), is that their application is not restricted to certain fields of activity. Thus almost all areas of domestic law relating to economic activities may be affected by one or more issues arising from EU law. Such EU-law issues, and the solutions to them, may sometimes come as a surprise. In addition, the enormous bulk of secondary legislation, although more limited in application, may have the same effect. This has inspired Thomas Wilhelmsson's readable essay "The Jack-in-the-Box Theory of European Community Law"¹ Given the aim of homogeneity embedded in the EEA Agreement, it seems fair to assume that the agreement has a similar effect in the legal regimes of Iceland, Liechtenstein and Norway. Here we will discuss whether this

¹ Wilhelmsson, Thomas: "Jack-in-the-Box Theory of European Community Law", in Krämer, L., Micklitz, H.-W. , Tonner, K. (eds.) *Law and Diffuse Interests in the European Legal Order*. Nomos Verlagsgesellschaft, Baden-Baden 1997, 177-194

assumption also holds true with regard to legal issues pertaining to Norwegian offshore activities, *i.e.*, activities taking place outside Norwegian territorial waters. Or is this particular Jack-in-the-box specific to the EEA?

2 A black-letter approach

Article 52 EU provides that the treaty applies to the contracting parties that are mentioned in the provision.² Since the provision only refers to the Member States, the issue whether the application of EU law is restricted to the territory of the Member States has been the subject of some debate and it has been argued that EU law only applies to the geographical areas over which the Member States exercise sovereignty, *i.e.*, have complete jurisdiction. The question has, however, long been settled, as the Court of Justice of the European Union has consistently held that the geographical scope of application of EU law follows that of the Member States' jurisdiction. Thus the scope of application of EU law is decided by functional, rather than geographical, criteria.

Article 126 EEA, however, provides that the EEA Agreement applies “to the territories to which the [TFEU] is applied and under the conditions laid down in that Treaty, and to the territories of Iceland, the Principality of Liechtenstein and the Kingdom of Norway”. The concept “territory” connotes under public international law the portion of land subject to the sovereign authority of a State, including the territorial waters. Thus, Article 126 EEA makes express reference to the geographical areas over which Iceland, Liechtenstein and Norway exercise sovereignty. Taking a black-letter approach, this means that the agreement refers only to those areas.

A comparison between the provisions of the TFEU and the equivalent mirrored provisions in the EEA Agreement confirms the impression given by Article 126 EEA. Where Article 45 (3) (c) TFEU provides

² This provision replaces Article 299 (1) ECT.

that the freedom of movement of workers entails the right “to stay in a Member State for the purpose of employment”, the corresponding provision of the EEA Agreement, Article 28 (3) (c) provides that the freedom entails the right “to stay in the territory of an [EU] Member State or an EFTA State”. Where Article 56 TFEU provides that there shall be no restrictions on freedom to provide services “within the Union”, Article 36 EEA provides that there shall be no restrictions on freedom to provide services “within the territory of the Contracting Parties”. Where Article 95 TFEU refers to “transport within the Union”, Article 50 EEA refers to “transport within the territory of the Contracting Parties”. Where Articles 101 and 102 TFEU refer to “the internal market”, Articles 53 and 54 EEA refer to “the territory covered by this Agreement”. Finally, where Article 108 TFEU refers to systems of aid existing in the Member States, EEA Article 62 refers to systems of State aid existing in “the territory of the Contracting Parties”.

Protocol 1 to the EEA Agreement, on horizontal adoptions, provides in paragraph 8 that references to the territory of the “Community” or of the “common market” in acts covered by the EEA Agreement shall be understood as references “to the territories of the Contracting Parties as defined in Article 126 EEA”.

Protocol 4 to the EEA Agreement, on rules of origin, provides in Article 4 (1) (j) that products extracted from marine soil or subsoil outside the EEA Member States’ territorial waters also have their origins within the EEA provided that the EEA Member States “have sole rights to work that soil or subsoil”. This indicates that the scope of application of the EEA Agreement may extend outside the territories of the EFTA States, as products extracted from such areas are deemed to have their origins in the EEA, and thus are subject to the freedom of movement. Mineral products, *i.e.*, oil and gas, extracted from the soil or seabed of the EEA States are however deemed to have their origin within the EEA pursuant to Protocol 4 Article 4 no. 1 (a). This provision does not contain the same proviso as paragraph (j) (“provided that they have sole rights to work that soil or subsoil”). Paragraph (j) was added by decision 38/2003 of the EEA Committee when the old text of Protocol 4 was re-

placed in order to reflect a number of changes of a technical nature that had been made since the EEA Agreement was ratified.

The general underlying principle in the EEA Agreement is that of homogeneity between EU law and the law of the EEA within the scope of application of the EEA Agreement. Accordingly one could argue that where the provisions of, respectively, EU law and the EEA Agreement differ in how they address the same issue, this principle should cause such differences to be regarded as mishaps and not accorded any relevance. Such an argument ignores, however, the fact that when homogeneity is a guiding principle, differences in wordings are more likely than not also intended to reflect differences in substance. Bearing in mind both the debate over the geographical application of EU law, and the fact that substantive economic activities are taking place under Norwegian jurisdiction but outside Norwegian territory, one might just as well argue that the differences in wording between the EEA Agreement and the Treaty on the European Union/TFEU on the subject of geographical application are intentional.

Thus, and even though one provision of Protocol 4 may be read as implying the opposite, it seems fair to conclude that a “black-letter approach” suggests that, as far as the EFTA States are concerned, the EEA Agreement does not apply to activities subject to their jurisdiction but taking place outside their territories.

3 Subsequent practice of the parties to the EEA Agreement

3.1 The inclusion of the Hydrocarbons Licensing Directive (Directive 94/22/EC)

Subsequent practice in the application of a treaty that establishes the agreement of the parties regarding its interpretation is, according to the Vienna Convention on the Law of Treaties Article 31, a means to establish the meaning of a treaty. As the EEA Agreement was concluded with the Member States of the EU as well as with the European Community (now the EU), the agreement does not fall within the scope of the Vienna Convention. It is, however, generally accepted that the Vienna Convention on this point reiterates general principles of treaty interpretation.

Directive 94/22/EC on the conditions for granting and using authorisations for the prospection, exploration and production of hydrocarbons was included in the EEA Agreement by decision 19/95 of the EEA Committee. The directive concerns authorisations for activities that in the case of a number of EEA States take place outside their territories and also contains a reference to the United Nations Convention on the Law of the Seas. Thus there is an implication that the directive also applies outside the territorial waters of the EEA States. The directive does have, however, general geographical application, and was for that reason to be included in the EEA Agreement. However, a joint declaration adopted by the parties to the EEA Agreement in connection with the decision to include Directive 94/22/EC in the agreement implies that the parties were of the opinion that the directive, when adopted in an EEA context, would apply to the regulation of activities taking place on the continental shelves of the EEA States.

3.2 The National Insurance Act – social insurance on the continental shelf

The white paper Ot.prp. no. 16 (2000-2001) contained a proposal that the Norwegian National Insurance Act should be amended to the effect that people not resident in Norway, but employed in the petroleum activities on the Norwegian sector of the continental shelf, should be obligatory members of Norway's national insurance scheme. Thus it was also proposed that the provisions of Annex VI nos. 1 and 2 to the EEA Agreement should apply *mutatis mutandis* to such workers.

The interesting point here is the proposal that the provisions in the Annex should apply *mutatis mutandis*. The background to the proposal was a reasoned opinion from the EFTA Surveillance Authority (the ESA), stating that a failure to accord non-resident workers the same rights to social benefits as resident workers constituted a breach of the EEA Agreement. The response of the Norwegian government suggests that it was of the opinion that the EEA Agreement did not apply to activities taking place on the continental shelf, *i.e.*, outside the "territory". The ESA had, for its part, adopted a functional approach to the issue, in line with the approach under EU law. This approach was clearly not shared by the Norwegian government.³ Thus, according to the government, the proposed amendment was not motivated by any obligation flowing from the EEA Agreement, but by considerations relating to fairness.⁴ The proposal was adopted by the Norwegian parliament.

3.3 Amendments to the Act on cash benefits for infants

A proposal to amend the Act on cash benefits for infants to the effect that it should apply, like the National Insurance Act, *mutatis mutandis* to workers in the petroleum sector on the Norwegian continental shelf was presented in the white paper Ot.prp. no. 58 (2003-2004). Again the

³ Ot.prp. no. 16 (2000-2001) p. 4.

⁴ Ot.prp. no. 16 (2000-2001) p. 13.

occasio legis was a note from the ESA, and again Norway submitted that the EEA Agreement did not apply to activities on the continental shelf, *i.e.*, activities not taking place on the “territory”.⁵ And once again the Norwegian authorities found that considerations pertaining to fairness mandated an amendment to the effect that the relevant provisions of the EEA Agreement should apply *mutatis mutandis*.

3.4 Amendments to the Norwegian fisheries act

The Norwegian Fisheries Act was amended as from January 2007. The amendment concerned manning requirements, and the requirement that the captain and at least half of the crew should be of Norwegian nationality was replaced by a requirement that the captain and at least half of the crew should be resident in a coastal municipality. Once again the *occasio legis* was a reasoned opinion from the ESA, dated 2 April, 2004.⁶

The ESA had become interested in the issue by way of a complaint from the unsuccessful defendant in a case decided by Agder Court of Appeal. Here a shipowner had been found guilty of breaching the manning requirements of the Fisheries Act.⁷ During the court proceedings, the shipowner had submitted that the manning requirements were incompatible with the EEA Agreement’s rules on free movement of workers. The Appeals Court found this submission to be irrelevant, as the fishing had taken place outside Norwegian territorial waters, and thus outside the geographical scope of the EEA Agreement.

The Frostating Appeals Court found, however, in favour of the shipowner in another case where the fishing took place within the Norwegian exclusive economic zone (EEZ). The court was of the opinion that taking Article 126 EEA literally was to adopt an overly formalistic approach.⁸

⁵ Ot.prp. no. 58 (2003-2004) p. 2 and p. 3.

⁶ The opinion is attached to Ot.prp. no. 99 (2005-2006).

⁷ LA-2001-1152.

⁸ LF-2006-24118.

In their correspondence with the ESA, the Norwegian authorities maintained that the manning requirements should be regarded as part of Norwegian fisheries policy, and thus outside the material scope of the EEA Agreement. In addition, the arguments pertaining to the geographical application of the EEA Agreement were put forward.

The *travaux préparatoires* show that the main reasoning behind the amendments to the Fisheries Act was a desire to establish and maintain a close connection between fisheries resources and the coastal population, and the view was that this would be better achieved by residence than nationality requirements.⁹

4 Conclusion

There may be little doubt that the Norwegian position, at least since the implementation of Directive 94/22/EC, has been that the EEA Agreement does not apply outside Norwegian “territory”. It is also interesting to observe that the ESA has not challenged this position in court, even though it has had opportunities to do so.

It may be that both Norway and the ESA would like to keep the lid of this particular Jack-in-the-box firmly closed.

⁹ Ot.prp. no. 99 (2005-2006) point 4.0

Regulating European multimodal transport

European Union competence under the Lisbon
Treaty

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1 Introduction

Since the early 1990s, the European Commission has been examining different options for regulating multimodal transport carrier liability¹ in the European Union (the EU). One option under consideration has been the formation of a regional liability regime for European international multimodal transport, while another has been the potential implementation of proposed international instruments. These efforts to achieve an operable legal regime to regulate carrier liability in European international multimodal transport are part of the European transport policy on sustainable freight, in which boosting multimodal transport has been a core objective.²

Traditionally international transport law has come within the competence of sovereign States and as such has developed multilaterally and has been handled through different bodies within the United Nations, such as the United Nations Commission on International Trade Law (UNCITRAL). If the EU were to become involved in the area of international multimodal transport, it would interfere with the Member States' traditional sovereign rights if it were to enter into multilateral agreements in this area. Currently this issue is highly topical as the United Nations Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea ("the Rotterdam Rules" or "RR"), which regulates multimodal transports that include a sea leg,³ has entered into force and is open for signature and ratification by both the EU and its

¹ Multimodal carriage is normally defined as carriage governed a single contract that involves at least two modes of transport. See Ralph de Wit *Multimodal Transport Carrier Liability and Documentation*, 1995 p.1. By contrast, a unimodal contract of carriage regulates carriage performed by a single mode of transport. Issues relating to liability in unimodal international carriage are regulated by international conventions that, once ratified, impose mandatory regimes.

² http://ec.europa.eu/transport/sustainable/index_en.htm

³ A full text version of the Rotterdam Rules is available on the UNCITRAL website: http://www.uncitral.org/pdf/english/texts/transport/rotterdam_rules/09-85608-Ebook.pdf.

Member States.⁴

If all the Member States ratify the Rotterdam Rules, at least some of the problems relating to carrier liability in European international multimodal transport will be resolved. Even so, problems relating to liability in multimodal transport chains without a sea leg will remain. Accordingly the achievement of a homogenous liability regime for all European multimodal transports will probably require EU intervention at some point.

This article will address the legal questions arising from the interplay between the EU and its Member States with regard to the competence of the EU to legislate in the area of European international multimodal transport.⁵ Section 3 outlines how general questions concerning transport competence have been resolved in EU legislation since the Lisbon Treaty entered into force. Since both the EU and the Member States have competence to sign and ratify the Rotterdam Rules, the impact of the Rotterdam Rules on the EU's competence regarding the regulation of European multimodal transport will be addressed in section 4. Finally section 5 presents some conclusions. Firstly, however, section 2 presents an introduction to the EU transport policy that is driving the ambition to legislate.

⁴ As of January 2011 the following EU Member States had signed the Convention: Denmark, Greece, France, Luxembourg, Netherlands, Poland and Spain. Nordic EU members Finland and Sweden have not signed, nor have non-members Norway and Iceland. Internationally it is noteworthy that the United States has signed, but not China. Spain was the first country to ratify the convention on 19 January 2011; <http://treaties.un.org/doc/Publication/CN/2011/CN.21.2011-Eng.pdf>.

⁵ This is a question of EU internal competence. The question of external competence will not be discussed in this article. The issue of regulating international multimodal transport is the subject of further research within the framework of the Helsinki-based InterTran research project, see: <http://www.helsinki.fi/katti/english/InterTran-project.htm>.

2 Why should the EU legislate in the area of international multimodal transport?

2.1 The lack of an international legal regime

Within the EU the question of how to regulate multimodal transport has been a subject of deliberation since the early 1990s. The reason for this interest is that the Commission considers multimodal transport to represent the future of freight transport.⁶ According to the Commission, multimodal transport is more environmentally friendly than and should replace, for example, road transport, which at the moment is growing faster than any other transport mode in Europe, leading to congestion in central Europe as well as to the growth of a transport industry that is considered both inefficient and polluting.⁷

At present there is no international legal regime in operation and the liability of the multimodal carrier in international transport is governed by a jigsaw made up of the existing unimodal conventions and standard form contracts. The lack of an international legal regime to regulate liability in multimodal transport has been seen as a bottleneck preventing a desired increase in European multimodal transport and, accordingly, as an issue that the Commission saw as needing to be dealt with.⁸ One option would be to provide the transport industry with a predictable and user-friendly liability regime and the Commission has been investigating whether a regional regime to regulate multimodal transport liability could offer a solution to the problems associated with the lack of predictability caused in turn by the lack of applicable international

⁶ http://ec.europa.eu/transport/sustainable/index_en.htm

⁷ This has been stated by the European Commission in numerous reports and documents. See, e.g., *Intermodality and intermodal freight transport in the European Union*. COM(97)243 at 13. An overview of policy issues has been presented in SIMPLY previously, see Ellen Eftestøl-Wilhelmsson, *EU intermodal transport and carrier liability – content and context*. SIMPLY 2007 pp. 133-166.

⁸ COM(97) at 26.

regimes.⁹

Several internationally well-known legal experts have been involved in the pursuit of an appropriate liability regime for European multimodal transport, among them *Professor Hans Jacob Bull* of the Scandinavian Institute of Maritime Law. Professor Bull was a member of the first group of legal experts appointed by the Commission with a mandate to consider the future of a regional legal liability regime in European multimodal carriage. The group published the results of its work in “Intermodal Transportation and Carrier Liability” in 1999.¹⁰ After discussing the problems associated with the lack of a coherent international liability regime and considering earlier attempts at unification, this document discussed a possible future regional legal instrument for the EU. Without drawing any conclusions on the content of such a regime, the group was clearly of the opinion that a regional legal instrument would have advantages, particularly in resolving the question of carrier liability during multimodal transport.

Subsequently two other groups of legal experts have been appointed to examine the question further. In 2005 the second expert group followed up the work of Professor Bull and his colleagues and proposed a European opt-out uniform liability regime with a harmonised liability limit of 17 SDR (the so-called ISIC or EU proposal).¹¹ This proposal never resulted in any legislative initiative from the Commission and a third group of legal experts was appointed to examine the possibility of an EU-wide regime in the area of multimodal transport liability. This group published its work in 2009 and proposed a mandatory liability

⁹ There is more on this topic in the White Paper European Transport Policy for 2010: Time to decide COM (2001) 370 and in its mid-term review Keep Europe moving – Sustainable mobility for our continent COM (2006) 314.

¹⁰ Intermodal Transportation and Carrier Liability. Study co-funded by the European Commission, Director General for Transport, DGVII, June 1999.

¹¹ Integrated Services in the Intermodal Chain (ISIC) Final Report Task B: Intermodal liability and documentation. Research report commissioned by the European Commission – DG TREN provided by an independent panel of legal experts. Published by ECORYS Nederland BV, Rotterdam 2005.

regime, with declaratory liability limits.¹² The latter proposal differs in approach from other international conventions in the area of transport law, and seems unlikely to be the subject of further deliberations.

The failure of the different expert proposals has been due partly to the difficulty of finding a solution that is acceptable to all stakeholders, but also to changes in the international situation.

2.2 The Rotterdam Rules may change the picture

Since 1999, when Professor Bull and his colleagues started the legal debate on a regional regime for multimodal European transport, there have been dramatic developments in the international arena. In September 2008, the Rotterdam Rules were adopted by the General Assembly. The Convention was signed by more than 20 States (including several EU Member States) in Rotterdam on 20 September 2009. As of February 2011, a single State, Spain, had ratified the Convention. Several States have appointed maritime law commissions with mandates to explore how the Convention could be implemented into their national legal systems.¹³

The Rotterdam Rules aim to regulate multimodal transports that include a sea leg through the provision of a modified network liability system. It is not clear that this system will fulfil the demands of the Commission as far as predictability is concerned. This is because of the rather complex system of rules on applicability laid down in Articles 82

¹² Study on the details and added value of establishing an (optional) single transport (electronic) document for all carriage of goods, irrespective of mode, as well as a standard liability clause (voluntary liability regime), with regard to their ability to facilitate multimodal freight transport and enhance the framework offered by multimodal waybills and/or multimodal manifests. The study was carried out for the Directorate-General for Energy and Transport in the European Commission and expresses the opinion of Gomez-Acebo & Pombo, Abogados SCP.

¹³ The Norwegian Maritime Law Commission has been appointed by the Norwegian Ministry of Justice and is chaired by Professor Erik Røsæg of the Scandinavian Institute of Maritime Law. Information on the work of the Commission and other Law Commissions is available at <http://folk.uio.no/erikro/WWW/sjolov/index.html>.

and 26 RR.¹⁴ On the other hand, the Rotterdam Rules provide a solution for so-called “undisclosed” damage, losses or delay-causing situations, and thus leave no situation unregulated.¹⁵ This is, of course, only true if the multimodal transport in question includes a sea leg. A multimodal transport performed, for example, via road, rail and inland waterway, will not be regulated by the Rotterdam Rules.

Whether or not the Rotterdam Rules are capable of satisfying the Commission’s requirements for a predictable liability regime is a matter for further debate. Clearly a crucial factor is the international success of the Convention. If the Rotterdam Rules are not accepted by all, or most of, the Member States, the EU will still need to consider regional solutions. In any event, the Rotterdam Rules do not apply to multimodal transports with no sea leg, which leaves some questions regarding international multimodal carrier liability unresolved. Unless the Member States take the latter issue into consideration, legal initiatives on a Community level may be necessary, as long as the EU has competence to act in the area of international transport law. The question of competence is regulated by the Treaty of Lisbon. This Treaty entered into force on 1 December 2009, and is discussed in general terms below.

3 EU competence in the area of international transport

3.1 Shared and restricted by certain principles

Following the entry into force of the Treaty of Lisbon, the competence of the EU is governed by the Treaty on European Union (the TEU) and

¹⁴ See Haak *Carriage Preceding or Subsequent to Sea Carriage under the Rotterdam Rules*. European Journal of Commercial Contract Law (EJCCL) no. 1/2, 2010 and Hoaks *Multimodal Transport Law. The Law Applicable to the Multimodal Contract for the Carriage of Goods*. Wolters Kluwer 2010, at pp. 338-353.

¹⁵ See Eftestøl-Wilhelmsson *The Rotterdam Rules in a European Multimodal Context*. Journal of International Maritime Law (JIML) no. 16, 2010 pp. 274-288.

the Treaty on the Functioning of the European Union (the TFEU).¹⁶ These treaties represent the foundations of the European Union and carry the same legal weight.¹⁷ The EU replaces and succeeds the previous European Community and has a legal personality.¹⁸ The competence of the EU as a legal person is, however, limited by certain fundamental principles of EU Law.

In accordance with the principle of conferral established in Article 5 TEU, the EU's competences are conferred on it by its Member States. The Union has no competence as of right, which means that unless the Treaties contain explicit agreement to the contrary, areas of policy remain within the sphere of the Member States' competence and outside the competence of the EU.¹⁹ This was also the case earlier, but the rule was stated explicitly for the first time in the failed Treaty establishing a Constitution for Europe²⁰ and was then carried over into its replacement, the Treaty of Lisbon.

According to the TFEU, the competence of the EU can be either exclusive or shared.²¹ In the area of transport, the EU has been granted shared competence.²² Shared competence means that both the EU and the Member States may *legislate and adopt legally binding acts* in the relevant area.²³ Obviously such shared competence could lead to conflicts of legally binding norms. For this reason, the mechanism by which competence is shared is governed in the Treaties.

With regard to the Member States, their competence to legislate is restricted by the activity of the Union: the Member States shall exercise their competence to the extent that the Union has not exercised its

¹⁶ Consolidated versions of the Treaty on European Union (TEU) as amended by the Treaty of Lisbon, and the Treaty on the Functioning of the European Union (TFEU) are published in OJ C 83, 30.3.2010, 1.

¹⁷ article 1 (2) TFEU.

¹⁸ Article 47 TFEU .

¹⁹ Article 5 (1) and (2) TEU.

²⁰ Treaty Establishing a Constitution for Europe Article 1-1, published in OJ C 310, 16.12.2004.

²¹ Article 2 (1) and (2) TFEU .

²² Article 4 (1) g TFEU.

²³ Article 2 (2) TFEU.

competence or to the extent that the Union has decided to cease exercising its competence.²⁴ If the Member States have conferred a competence on the Union, and the Union makes use of its competence, it will be contrary to EU legislation to exercise that competence on a national level.²⁵ So far the EU has not legislated in the area of multimodal transport liability. Consequently the competence, for example, to ratify and implement the Rotterdam Rules lies for the time being with the Member States.

With regard to the EU, even where competence has been conferred in an area, this competence is not unlimited, but is restricted by other principles of EU law. Both the Member States and the Union have a duty of loyal cooperation. This is set out both in case law from the European Court of Justice (the ECJ)²⁶ and in the Lisbon Treaty. According to Article 4(3) TEU, the Union and the Member States shall “in full mutual respect, assist each other in carrying out tasks which flow from the Treaties.” This duty of cooperation flows from the requirement of unity in the international representation of the Community.²⁷ In the area of shared competence, the competences of the Union are in addition limited by the principles of subsidiarity and proportionality.²⁸ Accord-

²⁴ Article 2 (2) TFEU, third and fourth sentences.

²⁵ This was also stated in the so-called ERTA judgment from the ECJ: *Commission of the European Communities v. Council of the European Communities*, European Agreement on Road Transport (ERTA), Case 22-70 [1971] ECR 263.

²⁶ Case C-25/94 *Commission v. Council* [1996] ECR I-1469 para 48 “It must be remembered that where it is apparent that the subject-matter of an agreement or convention falls partly within the competence of the Community and partly within that of its Member States, it is essential to ensure close cooperation between the Member States and the Community institutions, both in the process of negotiation and conclusion and in the fulfillment of the commitments entered into. That obligation to cooperate flows from the requirement of unity in the international representation of the Community (Ruling 1/78 [1978] ECR 2151, paragraphs 34 to 36, Opinion 2/91 [1993] ECR I-1061, paragraph 36, and Opinion 1/94 [1994] ECR I-5267, paragraph 108). The Community institutions and the Member States must take all necessary steps to ensure the best possible cooperation in that regard (Opinion 2/91, paragraph 38)”.

²⁷ L.c.

²⁸ Article 5 (3) and (4) TEU. More generally on the distribution of powers between the EU and the Member States, see Moens and Trone *Commercial Law of the European Union*. Springer, Dordrecht, Heidelberg, London, New York, 2010 at pp 26-30.

ding to the principle of subsidiarity the EU shall act

“...only and in so far as the objectives of the proposed action cannot be sufficiently achieved by the Member State, either at central level or at regional and local level, but can rather, by reason of the scale of effects of the proposed action, be better achieved at EU level.”²⁹

This principle also accords with previous case law from the ECJ to the effect that the EU has competence to legislate if the objective of the proposed action will be better achieved at Community level,³⁰ and cannot be sufficiently achieved by the Member States individually.³¹ The action should also not go beyond what is necessary to achieve the objective pursued.³² The latter rule accords with the principle of proportionality, which states that the content and form of the EU action shall not exceed what is necessary in order to achieve the objectives of the Treaties.³³ However, according to the ECJ

“...it should be noted that the Community legislature must be allowed a broad discretion in an area ..., which involves political, economic and social choices on its part, and in which it is called on to undertake complex assessments. Consequently, the legality of a measure adopted in that area can be affected only if the measure is manifestly inappropriate having regard to the objective which the competent institutions are seeking to pursue...”³⁴

In other words, the EU has quite a wide authority (*c.f.*, “must be allowed

²⁹ Article 5 (3) TEU.

³⁰ Case C-491/01 *The Queen v. Secretary of State for Health, ex parte British American Tobacco (Investments) Ltd and Imperial Tobacco Ltd.* at 180.

³¹ *Op.cit* at 182.

³² *Op.cit* at 184.

³³ See Article 5 (4) TEU and Joined Cases C-453/03, C-11/04, C-12/04 and C-194/04 *ABNA Ltd and Others v Secretary of State for Health and Others*: “According to settled case-law, the principle of proportionality, which is one of the general principles of Community law, requires that measures implemented through Community provisions be appropriate for attaining the objective pursued and must not go beyond what is necessary to achieve it...” at 68.

³⁴ *Op.cit* at 69.

a broad discretion”) to decide when it is necessary to pass legislation in an area and will only exceed its powers if the measure is “manifestly inappropriate” in relation to the objective pursued. Accordingly the objective being pursued by the relevant legislation (in our context, a regional liability regime for European multimodal transport), must form part of the European policy in question, which in the area of transport is specified in Title VI, Articles 90-100 TFEU.

3.2 Within the framework of a Common Transport Policy

According to Article 90 TFEU, the objectives of the Treaties in the matter of transport shall be accomplished within the framework of a *Common Transport Policy*.

The wording in this respect differs little from what has been agreed since the Treaty of Rome, in which transport had its own title.³⁵ However, progress in the area of transport was initially very slow. It was not until the ECJ intervened in 1985, ruling in a landmark decision that the Council had failed to act, that the Member States had to accept that the Community had competence to act in the area of transport law.³⁶

As mentioned above, the EU is experiencing a constant growth in transport, and particularly in road transport, which has led to traffic congestion and traffic-related environmental damage. Today transport (of passengers and goods) generates almost a quarter of all greenhouse gas emissions in the EU.³⁷ The EU’s current transport policy is thus leaning towards a model of *sustainable mobility* with a target of increasing the share of multimodal transports within the Union. Sustainable transport is not mentioned directly in Title VI TFEU, but Article 11

³⁵ Treaty of Rome, 1957 Title IV, Article 74.

³⁶ ECJ 1985, *European Parliament v. Council of the European Communities* C-13/183[1985] ECR.

³⁷ http://europa.eu/scadplus/glossary/common_transport_policy_en.htm

TFEU contains a provision on sustainable development

“Environmental protection requirements must be integrated into the definition and implementation of the Union’s policies and activities, in particular with a view to promoting sustainable development.”

There should accordingly be no doubt whatsoever that the EU has both a right and an obligation to implement sustainability in its transport policy.³⁸ Some steps have already been taken. As early as 1992, in the first White Paper on the future development of the common transport policy, sustainable mobility was launched as an objective for the common transport policy.³⁹ Another benchmark was the 2001 White Paper *European Transport Policy for 2010: Time to decide*⁴⁰ in which the Commission recognised the imbalance between the development of different modes of transport as one of the biggest challenges facing the Union and consequently launched the idea of multimodal transport as a transport alternative that could improve the quality of transport in the EU. The concept of providing the industry with a uniform liability regime was launched as a tool to increase the attractiveness of multimodal services,⁴¹ and is thus clearly part of the Common Transport Policy.

The content of such a liability regime has however been the subject of constant debate. A crucial question has been whether the EU needs a

³⁸ On sustainable development as a normative imperative, see Sjøfjell: *Towards a Sustainable European Company Law: A Normative Analysis of the Objectives of EU Law, with the Takeover Directive as a Test Case*. Kluwer Law International, 2009

³⁹ COM (1992) 494 final at p 13.

⁴⁰ COM (2001) 370.

⁴¹ “... at present, different regimes apply to the liability of intermodal operators not only as between Member States but also to the different modal stages of an intermodal journey. As a United Nations Convention on multimodal international transport of goods was adopted on 24 May 1980 but has not yet come into force, an investigation is needed of the extent to which a more uniform approach would increase the attractiveness of multimodal services. Should it appear desirable, the different methods of realizing that objective will then require evaluation, bearing in mind the Community interest in seeing rules applicable to the operators being applied also to those from third countries, particularly those from the European Economic Area and Eastern and Central Europe”. COM (2001) 370 at 109.

predictable liability regime in which the same rules on liability apply regardless of where in the multimodal transport chain the damage, loss or delay-causing event occurs or whether the EU can be satisfied with a modified network system as provided by the Rotterdam Rules. This would have the advantage that the same liability regime would apply worldwide – provided, of course, that the Rotterdam Rules become an international success. It is clear that the Commission has modified its policy in this area in line with developments internationally. After intensive discussions with the Member States and other stakeholders, the Commission presented in 2006 a mid-term review of its 2001 White Paper. Here we find a somewhat revised agenda. In its mid-term review the Commission decided to “develop a framework strategy for freight transport logistics in Europe, followed by broad consultation and leading to an action plan.”⁴² In 2007 the Freight Transport Logistics Action Plan was launched.⁴³ On the question of liability, the Commission recognised in the action plan that multimodal transport suffered from friction costs induced by the absence of a uniform, cross-modal liability regime. However, in addition to the idea of a *uniform liability system* for regional international multimodal transport, the Commission also intended to start a process to examine whether a *modified network liability system* (as provided by the Rotterdam Rules) could operate to provide a predictable liability regime. Proposals were scheduled to be presented in 2009 or 2010, but so far none have appeared. Regarding the issue of competence, the result of the Commission’s deliberations is irrelevant, as whatever the Commission decides, the proposal will be in line with the Common Transport Policy and thus within the competence of the EU.

One question we may ask, however, is whether there is any difference in EU competence regarding transport by sea and air on the one hand and transport by rail, road and inland waterways on the other. The competences concerning these respective forms of transport are regula-

⁴² COM (2006) 314 final. *Keep Europe moving - Sustainable mobility for our continent - mid-term review of the European Commission’s 2001 Transport White paper* at 7(1).

⁴³ COM (2007) 607 final.

ted by different Treaty provisions. Transport by rail, road and inland waterways is governed by Article 100(1), while transport by sea and air is governed by Article 100(2). The difference between the first and second paragraphs is that the provisions of Title VI “shall” apply to transport by road, rail and inland waterway, whilst according to Article 100(2), which governs sea and air transport, the European Parliament and the Council “may lay down appropriate provisions”. It is however clear that the difference in wording has no impact on the question of competence. Article 100(2) provides the European Parliament and Council with the necessary competence to legislate in the area of sea and air transport.⁴⁴ We should also note that the procedural requirements for enacting legislation are the same for all modes of transport: appropriate provisions shall or may be laid down to be accomplished in accordance with ordinary legislative procedures, after consulting the Economic and Social Committee and the Committee of the Regions.⁴⁵

4 The impact of the Rotterdam Rules

4.1 The Rotterdam Rules may change the Common Transport Policy

As mentioned above, the principle of subsidiarity limits the competence of the EU even where a competence has been conferred on it by the Member States. The EU should only legislate if the objective of the proposed action will be better achieved at Community level and cannot be sufficiently achieved by the Member States individually. However, the

⁴⁴ The Lisbon Treaty here accords with the EC Treaty Article 80 and previous case law from the ECJ, such as the French merchant seamen case: *Commission v. French Republic*, C-167/73, [1974] ECR 359 and the Open Skies judgment, *Commission v. Germany*, C-476/98 [2002] ECR I-9885.

⁴⁵ For sea and air transport this follows from Article 100(2), while for transport by rail, road and inland waterways it follows from Article 91.1. The ordinary legislative procedure is governed by Article 294 TFEU.

EU has a broad discretion on the subject. With regard to the potential adoption of a regional liability regime for European multimodal transport, the Commission has carried out preparations in close collaboration with the Member States and other stakeholders. As the question is politically sensitive and the Member States have diverging interests in the area, it seems fair to conclude that until now the Commission has been correct in assuming that a harmonised legal instrument, providing predictable liability rules for international European multimodal transport, most likely could not be achieved on a Member State level and thus in starting preparations for a regional multimodal liability regime.⁴⁶ Accordingly the project to develop a regional liability regime has not violated the principle of subsidiarity.⁴⁷

However, the Rotterdam Rules might change the background to the Commission's exploration of the need for a regional European regime on carrier liability in multimodal transport. Everything depends upon the international success of the Convention. If it is ratified by most or all of the Member States, the picture may change. One could argue that such an assumption by the Commission would then apply only to multimodal transports *with no sea leg*, which fall outside the scope of the Rotterdam Rules.⁴⁸ Regarding multimodal transports *with a sea leg*, one might, in such a situation, question the need for a European project on a regional regime. If the Member States ratify and implement the Rotterdam Rules, they will implement a liability system for international multimodal transport and it is highly unlikely that the EU as such would then decide on a different regime. From a legal point of view, however, the EU would have the competence to legislate differently providing it did so in line with the Common Transport Policy.⁴⁹ The key to the EU's competence in the field of multimodal transport liability is, in other words, the content of the Common Transport Policy, and as mentioned above in section 2.3, this has still not been finalised.

⁴⁶ See section 2 above.

⁴⁷ See section 3.1 above.

⁴⁸ Rotterdam Rules Article 1.1 RR.

⁴⁹ Articles 90 and 91(1) TFEU.

4.2 Open for signature and ratification for both the Member States and the EU

Currently, however, the EU is not limited to the option of passing internal legislation on multimodal carrier liability, as both the EU and its Member States now have the possibility to enter into an international agreement in the area of international multimodal transport liability. Article 93(1) RR grants the EU, as a regional economic integration organisation, the right to sign, ratify, accept, approve or accede to the Convention and, according to Article 216(1) TFEU⁵⁰ the EU has competence to enter into such an agreement.⁵¹

If the EU were to make use of this competence to sign and ratify the Rotterdam Rules, the Convention would become binding on all EU institutions as well as on the Member States⁵² and thus would form an integral part of EU law. Such a choice would implement the Rotterdam Rules coherently within the EU, which would be more efficient than implementation by each Member State on a unilateral basis. On the other hand, this method would allow less flexibility to the Member States and might interfere with their national interests. The EU as a legal person has to date not taken any steps towards signing or ratifying the Rotterdam Rules. The only official statement on the subject to emerge from an EU institution has been a resolution from the European

⁵⁰ Article 216 (1): The Union may conclude an agreement with one or more third countries or international organisations where the Treaties so provide or where the conclusion of an agreement is necessary in order to achieve, within the framework of the Union's policies, one of the objectives referred to in the Treaties, or is provided for in a legally binding Union act or is likely to affect common rules or alter their scope.

⁵¹ Article 216 hereby codifies what has been developed by the ECJ as the principle of "parallelism": if there is an internal competence of the Union there also is an external competence, meaning that the EU has competence to enter into international agreements. As outlined above the EU has internal competence to act in the area of international multimodal transport law and consequently also has external competence to enter into an international agreement such as the Rotterdam Rules. Wouters, Coppens, De Meester *The European Union's External Relations after the Lisbon Treaty* pp. 144 - 203, in Griller, Ziller *The Lisbon Treaty. EU Constitutionalism without a Constitution*. SpringerWienNewYork 2008, at p. 168.

⁵² Article 216(2) TFEU.

Parliament encouraging the *Member States* to sign the Convention.⁵³

Obviously the Member States have the right to sign and ratify the Rotterdam Rules.⁵⁴ So far 21 states, including eight EU Member States, have signed the Rotterdam Rules, which accordingly have entered into force.⁵⁵ On 19 January 2011, Spain became the first State, both internationally and on a European level, to ratify the Rotterdam Rules. If a Member State enters into an international agreement, the starting point is that this does not affect EU law.⁵⁶ Accordingly ratification of the Rotterdam Rules by a Member State does not make the rules part of EU law, but instead part of the national law of the ratifying Member State. This implies that the Rotterdam Rules will not be subject to the principles of EU law,⁵⁷ nor will the ECJ have jurisdiction to give any authoritative interpretations regarding them in preliminary rulings.⁵⁸ The ECJ does however have competence to decide on the meaning of the Rotterdam Rules, in the same way as it can decide on the meaning of other parts of national law in order to determine whether there has been a breach of EU law.⁵⁹ As long as the EU does not enact any legislation in the area of multimodal transport liability and does not sign up to the Convention, the risk of conflicts with EU law is slight.

If, however, the EU chooses to legislate in the area of multimodal

⁵³ European Parliament report on strategic goals and recommendations for the EU's maritime transport policy until 2018. (2009/2095(INI)).

⁵⁴ Article 88(1) and (2) RR.

⁵⁵ Of the EU Member States, Denmark, France, Greece, Luxembourg, the Netherlands, Poland, Spain and Switzerland have signed the Rotterdam Rules, see footnote 4 above.

⁵⁶ There are several exceptions from this that will not be discussed here, but that are the subject of further research. The problems are outlined regarding maritime law in general by Rosas *EU Law and International Agreements Concluded by EU Member States, with Particular Emphasis on Maritime Law*. Paper presented at a seminar on Environmental Liabilities in Ports and Coastal Areas in Korpoström, Finland, 11-13 August 2010 arranged by the Institute of Maritime and Commercial Law at Åbo Akademi University. To be published in 2011 by the Institute of Maritime and Commercial Law, Åbo Akademi University, at 5.

⁵⁷ Op.cit. at 2.

⁵⁸ Op cit. at 2 with reference to unreported case law: Case C-533/08 *TNT Express Nederland*, judgment of 4 May 2010 para 61.

⁵⁹ Op.cit at 2.

transport liability, the picture will change. As mentioned above, the competence of the Member States is restricted by the activity of the EU: the Member States may only exercise their competence to the extent that the Union has not exercised its competence or to the extent that the Union has decided to cease exercising its competence.⁶⁰ If the EU decides on a regional multimodal liability regime *different* from the modified network liability system of the Rotterdam Rules, then the Member States will not be allowed to derogate from this EU law obligation by entering into an agreement with one or several third States, such as by ratifying the Rotterdam Rules.⁶¹ On the other hand, if the EU decides on a European regional liability regime in line with the Rotterdam Rules, this will be binding on the Member States and certainly make the harmonising of the Rotterdam Rules in Europe more effective.

5 Conclusions

The above discussion of the *competence* of the EU as a legal person to regulate European international multimodal transport shows that the EU has a conferred competence to act in the area of international transport law, subject to the restrictions imposed by some fundamental principles of EU law such as those of subsidiarity and proportionality. For the purposes of regulating multimodal transport liability, the most significant limitation on the EU's competence to act is that it is limited to implementing the *Common Transport Policy*. In this regard the Commission is still exploring what kind of liability system would be best suited to the EU: the modified network liability system of the Rotterdam Rules or a voluntary uniform liability system as proposed by a group of legal experts acting on the instruction of the Commission. The answer

⁶⁰ Article 2 (2) TFEU, third and fourth sentences.

⁶¹ Rosas *supra* fn. 47 with a reference to a different view presented by Klabbers in *Treaty Conflict and the European Union*. Cambridge University Press, 2009.

to this question is completely dependent on the international success of the Rotterdam Rules.

As regards the Member States, they have conferred the competence to act in the area of international transport law on the EU. Although this competence is shared, the Member States' right to legislate is lost as soon as the EU regulates the issue. This is expressed in Article 2(2) TFEU and follows from the supranational character of EU law. In the area of international multimodal transport liability any legislation from the EU will in other words restrict the sovereignty of the Member States in this area.

Cargo damage – who is entitled to sue the maritime carrier?

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1 The problem

When cargo transported by sea, under a contract to which the rules in Chapter 13 of the Norwegian Maritime Code of 1994 apply, is damaged while in the possession of the carrier, as a starting point the carrier is liable for the damage. The damage may range from severe – perhaps even the total loss of the cargo – to negligible and may occur at any stage of the transport process: when the carrier has possession of the cargo prior to loading, during the processes of loading, carriage or discharging, or even after completion of discharge before a receiver takes possession. In some cases the damage may develop gradually: an example would be fruit that is not properly cared for before, during or after carriage.

When such damage has either occurred or is alleged to have occurred, who is entitled to sue the carrier?¹ Answering this question becomes more complex when the carriage is documented by a negotiable bill of lading, in particular when cargo referred to in such a document is sold during the period of carriage.

The discussion in this article – which primarily concerns procedural law – assumes that Norwegian law applies and that the suit is brought before a Norwegian court that in principle is competent to hear the case. The relevant legislation is Act no. 90 of 2005 on mediation and procedure in civil disputes (the Disputes Act) – replacing the Civil Procedure Act of 1915 – and the Maritime Code of 1994 no. 39 (the MC).²

The general principles concerning the right to sue will be outlined in

¹ The damage may be caused by, e.g., the mate or a stevedore. However we shall not discuss possible suits against such persons, which on principle are based in tort, but with extensive protection for the tortfeasor, as the law provides that he may plead the same protection as that to which the carrier is entitled to *vis-à-vis* his contractual counterparty, cf. the Maritime Code of 1994 Section 282 (2).

² Both acts have been unofficially translated into English and these translations have been used in this article. For the English version of the MC see *Marlus* no. 393 (2010) and for the Disputes Act see <http://www.ub.uio.no/cgi-bin/ujur/ulov/sok.cgi>. The other translations in this article are by the author.

Section 2 below. The closely related discussion in Section 3 deals with the simple situation of cargo being carried under a sea waybill and takes as its starting point the receiver who is also the sender.³ Our discussion in Section 4 of the position where a bill of lading is used first requires an outline in 4.1 of the general effects of the issuance of a negotiable bill of lading. We then analyse the right to sue when a bill of lading has been issued and possibly transferred.

In order to simplify matters, we make a general assumption that the contractual carrier is also the performing carrier. In Section 5, however, we briefly consider the position where the performing and contracting carriers are different persons.

2 Generally on the right to sue

The pre-condition for bringing a suit is, of course, that the defendant has venue in Norway in accordance with the rules in the Disputes Act Chapter 4 (see Section 4-3 on international venue, Section 4-4 on ordinary venue, Section 4-5 on venue elected by the claimant, and Section 4-6 on agreed venue).⁴ Assuming there is proper venue, Section 1-3 of the Disputes Act lays down a further requirement for bringing a case before the Norwegian courts:

(1) An action may be brought before the courts for legal claims.

(2) The claimant must show a genuine need to have the claim

³ the MC is, *cf.* Section 251: *ca* The terminology in *rrrier*: “the person who enters into a contract with a sender for the carriage of general cargo by sea”; *sender*: “the person who enters into a contract with a carrier for the carriage of general cargo by sea”; *shipper*: “the person who delivers the cargo for carriage”. “Receiver” is not defined in the same way, but is, obviously, the person who takes possession of the goods at the port of discharge.

⁴ Here we shall only mention that Section 4-4 on “ordinary venue” states that a natural person has venue where he has his “habitual residence”, while “undertakings registered in the Register of Business Enterprises have their ordinary venue at the place where the head office of the undertaking is located according to such registration”.

determined against the defendant. This shall be determined based on a total assessment of the relevance of the claim and the parties' connection to the claim.

According to sub-paragraph (1), the claim must be of such a nature that the decision depends upon *the application of legal rules*⁵. This is clearly the situation where a cargo owner is claiming compensation for cargo damage, regardless of whether the claim is formulated as being of a contractual or non-contractual nature. Sub-paragraph (2) requires there to be a *connection* to the subject-matter of the dispute on the side of both the claimant and the defendant. What this means in our context is that a court case in respect of damaged cargo cannot be started by simply anyone: a claimant will only be entitled to do so if he has a special reason for bringing his suit, *i.e.*, there has to be a connection between the claimant and the damage. Whether such a connection is sufficiently strong will have to be determined on the basis of an overall assessment. As a general rule, the requirements of Section 1-3 must be satisfied through the whole period of the litigation. If this is not so, the case will be dismissed.⁶

Clearly, *the cargo owner*, claiming that his cargo has been damaged while in the possession of the carrier, has a right to sue the carrier. The same applies where there are several owners: where A and B jointly own the cargo, they may jointly sue the carrier. A (or B) may also sue the carrier separately, but each only in respect of his own interest in the cargo.⁷ In quasi-corporate situations, however, it seems to some extent

⁵ See Schei *et al.*, *Twisteloven* (2007) p. 41.

⁶ See Schei *et al.*, *op. cit.* p. 84.

⁷ *E.g.*, where A owns 20 per cent of the cargo and 50 per cent of the cargo is damaged, A's claim will relate to 10 per cent of the cargo.

to have been accepted that A may appear as claimant on behalf of both.⁸

Where the cargo owner is a limited company, a shareholder may be said to have an interest in the cargo. Such an indirect interest is not, however, sufficient.⁹ The situation is different where A has a right *derived* from the owner. A typical example would be where A has a secured interest in the cargo (*e.g.*, through a pledge or a maritime lien on the goods). Clearly, A cannot demand judgment for the owner's (B's) loss, but he is entitled to demand judgment for his own loss – which may involve a decision that he (A) has/had a secured interest even if the defendant contests that B (from whom the secured interest derives) is/was the owner of the cargo.¹⁰

Naturally, it is the claimant who must show that the requirements of Section 1-3 are complied with.

An essential point is that the decision as to whether the suit shall be accepted depends, basically, upon the legal and factual *assertions* of the claimant:

“The court shall base its decision on the claimant’s assertions regarding the facts and the rules of law on which he builds his material claim. Whether the facts and the legal views expressed are true, falls within the decision on the merits of the case” (Schei *op. cit.* p. 80).

This distinction between assertions and merits may sometimes be

⁸ See Skoghøy, *Twistemål* (2nd ed. 2001) p. 337: “A participant in a legal entity not organised as an independent legal person has such a close connection to the rights and obligations of the entity that, according to my mind, there is nothing preventing him from claiming judgment for [the joint owners] against the defendant.” The participant may have formal, written authorisation from the others, but an implied authorisation may also suffice, see Rt. 1938 p. 392: a co-owner – who was the driving force in a loosely organised project that could not be considered as a legal person – was “considered to have the authority from the other co-owners to collect on behalf of all of them amounts due under contracts which he had concluded regarding sale of parts, and to file a suit in connection herewith”.

⁹ Schei *et al.*, *op. cit.* p. 58.

¹⁰ See Schei *et al.*, *op. cit.* p. 59.

difficult,¹¹ but hardly in the present context. See for instance Rt. 2005 p. 999, where the Court of Appeal – with the approval of the Supreme Court – stated:

“In this litigation the appealing party asserts that it has a claim against the respondent. The claim is said to have been acquired from Joker Invest based upon a contract. The Court accepts this assertion of having a claim against the respondent as sufficient connection to the object of litigation. The question whether the claim is founded, including the question of whether the transfer is valid, is part of the substantive issue. Accordingly it will also be part of the trial on the merits who, as against a limited company, is entitled to plead company law rules on invalidity.”

Accordingly we can conclude that if the situation as asserted by the claimant does not meet the requirements of Section 1-3 the case will be dismissed.¹²

The question whether the defendant has a sufficiently strong connection comes up more rarely, because the claimant will, in his own interest, pursue his claim against “the person against whom he finds he has a claim” (*Schei op. cit.* p. 54). If the Court finds that the defendant is not liable – which in our context would mean not liable for cargo damage – the Court will not dismiss the case, but give judgment in favour of the defendant.

¹¹ See *Schei et al., op. cit.* pp. 81-83.

¹² The court may also decide to dismiss the case at a later stage. The requirements of Section 1-3 must be fulfilled, as previously stated, during the entire court proceedings, *i.e.*, up to the time when the court makes its decision on the merits. However, if the claim is paid and “the case thus has become ‘without object’ it may be better to declare the litigation terminated [Norwegian: *heve saken*] than to dismiss the case, *cf.* [the Disputes Act] Section 19-1 (2) (b)” (*Schei et al., op. cit.* p. 84).

3 The simple situation: carriage under a sea waybill

We start with a straightforward scenario: no bill of lading is issued and carriage is subject to a non-negotiable sea waybill, issued to the shipper. Two situations need to be considered.

3.1 Cargo is discharged and delivered – allegedly in a damaged condition

3.1.1 Starting points – claim based on ownership

We assume that the cargo was discharged at the port of destination and thereafter delivered in accordance with the ordinary rules on delivery, *i.e.*, to the consignee named in the sea waybill or to the party to whom the right of receiving has been transferred, *cf.* MC Section 308 (2).¹³ If at the time of delivery the cargo is claimed to have been damaged, a claim may be brought by the receiver on the basis of either ownership or a derived lesser right than ownership (typically a security interest).

Where the receiver (A) bases his claim on ownership, is it sufficient for him to say (assert) that he is the owner? In many cases it will be reasonably clear that A is indeed the owner: the sea waybill will state that A is both shipper and consignee. But the cargo may have been sold and there may be number of reasons seriously to question A's ownership. This is not, however, a preliminary issue, see, *e. g.*, Rt. 2005 p. 534 (paragraph 21):

“It is a condition for deciding the substantive issue that the suit concerns a legal claim and that the claimant has a legal interest in obtaining a judgment for the claim, *cf.* Civil Procedure Act,

¹³ The sub-paragraph reads: “Even after a sea waybill has been issued, the sender can decide to have the goods delivered to someone other than the consignee named in the document. This does not apply if the sender has waived this right as against the carrier or if the consignee has already asserted his or her right.” See Falkanger & Bull, *Sjørett* (7th ed. 2010) p. 318, *cf.* pp. 318-319.

Sections 53 and 54.¹⁴ When deciding whether the suit shall be allowed [not dismissed], the court shall not, however, try the substance of the claim presented and whether the claimant is the holder of this claim, but shall accept the assertions of the claimant. Whether the claimant in fact has such a claim as asserted is a material question which he is entitled to have decided on its merits, insofar as his interest in the outcome is protected by the material rules on which he has based his claim.”¹⁵

Where the cargo has been sold *en route* the damage may have occurred either before or after the transfer of ownership – or there may be doubt as to exactly when the damage occurred. Is this relevant if A as buyer files suit against the carrier?

The general rule is that ownership to goods is freely transferable and that a transfer of ownership includes all the rights of the transferor.¹⁶ This is so even when litigation concerning the goods is pending.¹⁷ Suppose, for example, the cargo is damaged, *e.g.*, during loading. The cargo owner may have a claim against the carrier and when he thereafter sells the goods, all his rights – including a potential claim for cargo damage – are transferred to the buyer, unless there are specific restrictions in the sales agreement, such as a proviso that the seller shall handle the claim for cargo damage against the carrier.¹⁸ In the absence of any such restrictions, the sale does not make the situation any more problematic than if A had continued to own the cargo during the entire carriage. In other words, the buyer’s suit against the carrier cannot be dismissed on formal grounds.

¹⁴ The Civil Procedure Act 1915 (applicable before the Disputes Act entered into force) used the term “legal interest” as the decisive criterion; the present criterion is said to have the same scope, *cf.* Schei *et al.*, *op. cit.* p. 34: “in all essential respects the same”.

¹⁵ The reservation in the concluding words (*insofar etc.*) appears to be of no relevance under the Disputes Act (Schei *et al.* p. 82); in any case, it is of no importance in regard to the questions discussed in this article.

¹⁶ See, *e.g.*, Hagstrøm, *Obligasjonsrett* (2003) pp. 863-865.

¹⁷ See, *e.g.*, Skeie, *Den norske civilprocess I* (2nd ed. 1939) p. 283 on *res litigosa*.

¹⁸ This may be the case, *e.g.*, where a defined element of the cargo is lost (*e.g.*, one of three containers goes overboard in heavy weather). In that case the natural object of the sale will be the remaining two intact containers.

Here we may encounter the distinction between ownership and the right to acquire ownership. Whether the buyer has acquired ownership – *i.e.*, whether ownership has passed to him or whether he has a conditional right to acquire ownership – is in a suit against the carrier a substantive question, which may become more acute should a third party intervene and also claim ownership.¹⁹ The important point is that even a buyer to whom ownership has not passed is protected and has a right to sue the carrier – see generally Augdahl, *Den norske obligasjonretts almindelig del* (5th ed. 1978) pp. 414-415 and Hagstrøm *op. cit.* pp. 825 *et seq.*

The buyer may, however, decide not to sue the carrier but rather to seek redress under the sales contract, provided, of course, that the goods as received do not conform with the provisions of the sales contract. Then the question of exactly when the damage occurred becomes important: was it before or after the risk passed from seller to buyer? If the seller bears the risk, settling the matter with the buyer and compensating him, is the seller (the sender) now entitled to sue the carrier? As stated above, under the sales contract the seller will normally have transferred all rights connected with the goods. Through the settlement with the buyer, however, the right to sue must be considered to be transferred back to the seller, as now the seller satisfies the requirements of the Disputes Act Section 1-3. But in this case the carrier will have the possibility of pleading that the loss occurred after the risk passed to the buyer. If this assertion proves correct, the buyer had no claim against the seller and the seller's subsequent claim against the carrier will fail (unless the buyer's acceptance of payment from the seller has the implied effect of transferring all the buyer's claims to the seller).

3.1.2 Suit is commenced prior to or after a sale from A to B

Suppose that, prior to the sale, A had sued the carrier for cargo damage. If at the time of sale there is a final decision in favour of the carrier, such

¹⁹ On the right to intervene, see the Disputes Act Section 15-3.

decision will be binding also on the buyer B.²⁰

If the damage is only discovered after the sale, the seller will no longer be in a position to commence litigation against the carrier, see Rt. 1989 p. 338: the Court of Appeal had accepted that a seller of real property could act as claimant where there was an agreement between him and the buyer that the seller “for the time being” should appear as owner, and where, in any event, the seller was authorised to start litigation (eviction proceedings) on behalf of the real owner. The Supreme Court did not agree:

“ ... the general rule is that a party who does not assert that he himself is the owner of the claim brought before the Court, cannot – except on special grounds – act as claimant in his own name The requirements of the Civil Procedure Act regarding the description of a party are, of course, based upon a principle of truth. The person named as a party has to be the real party, *i.e.*, he must assert possession of the claim that he is bringing in his own name.”

A good illustration of this is provided in Rt. 1969 at p. 1032. Here an importer of cars sued the freight forwarder for damage to cars caused by a collapsed roof due to heavy snow. During the preparatory stages of the proceedings it emerged that the claimant had been fully compensated by his insurers and was bringing the suit on their behalf. The case was then dismissed. The majority in the Supreme Court remarked that:

“... a party who does not assert the right to the claim presented, cannot, unless there are specific grounds for doing so, act as claimant on behalf of another party ... In the present case the insured had obtained full compensation before the suit commenced, and the insurer has with definitive effect subrogated the entire claim the insured may have against a third party.”

The dissenting judge agreed with the general rule, but found that the claimant had “such a reasonable connection to the issue that he is entit-

²⁰ The former Civil Procedure Act 1915 Section 65 (2) stated this explicitly. See Hov, *Rettergang I* (2010) p. 409.

led to have the issue tried on the merits”.

3.1.3 The goods are sold while a court case is pending

We will now consider the situation where the sale takes place before a final decision is handed down on the merits of the case.

One possibility is that the sale does not initiate any procedural action on the part either of the claimant or the respondent. This suggests the following line of reasoning: where the claimant divests himself of all rights to the cargo by selling it, the requirements of the Disputes Act Section 1-3 are no longer fulfilled and the case should be dismissed. However, under the Civil Procedure Act 1915 this was not so: Section 65 (2) implied that the litigation could continue with the original parties, stating that in such circumstances the decision “is binding also for the successor”. No similar stipulation is found in the Disputes Act, but the *travaux préparatoires* show that no change in the law was intended. Accordingly the litigation can continue between the original parties.²¹

Obviously, there may be a number of reasons for a change in the claimant’s position. The seller will usually prefer to leave the case to the buyer,²² but there is no legal mechanism whereby the seller can retract unilaterally from the litigation, forcing the buyer to act as sole claimant.²³ Nor can the seller, it has been argued, demand that the buyer be made a co-claimant.²⁴ The buyer, however, has the possibility to seek to be joined as a party, see the Disputes Act Section 15-3 (1) on the right of a third party to “be joined as a party to the proceedings”, subject to

²¹ See Hov, *Rettergang I* (2010) p. 409 and Schei *et al.*, *op. cit.* p. 855. The former is of the opinion that the decision is not binding on the buyer (pp. 409-410): “Clumsy handling of the case” should not prejudice the buyer. Schei *et al.* p. 854 state, however, that the rule in the Disputes Act Section 19-15 (1) second sentence on “derived legal force summarizes and maintains the former non-statutory rule” – whereof the former Section 65 (2) was an example (p. 855).

²² There may be arguments to the contrary: the seller may fear that the buyer will not argue the case properly, which may have repercussions for the buyer/seller relationship.

²³ Hov *op. cit.* pp. 406-407, but seller and buyer may *agree* that the case shall be continued solely by the buyer, subject to the approval of the defendant.

²⁴ Hov *op. cit.* pp. 495-496.

submitting an independent statement of claim. This requirement is understood as being met when the buyer “demands judgment *to the benefit of himself* even though he in principle demands the same as the one from whom he derives his right” (Hov *op. cit.* p. 404).

Finally, we should mention that if the buyer is not made a party in the ongoing litigation, he has the possibility of intervening and acquiring the status of “an intervening party”, *cf.* the Disputes Act Section 15-7: A person “who by virtue of his own legal status has a real interest in one of the parties winning” may intervene, and as an intervening party he is entitled to “take procedural steps for the benefit of the party who is to benefit from the support. Such procedural steps shall not be contrary to those of the party”.

3.1.4 Claims based upon lesser rights than ownership

A security interest is the typical example of a lesser right than ownership which may be asserted if the cargo arrives damaged. For the sake of simplicity we will consider the example of a bank that has a lien/pledge/mortgage²⁵ on the cargo. The bank – asserting a security interest – may sue the carrier, either separately or jointly with the (person asserting to be the) owner. The general rules for being accepted as joint claimants are set out in the Disputes Act Section 15-2: the owner and the bank clearly have the possibility to operate in concert, *cf.* the loosely defined requirement that the claims should be “so closely connected that they should be heard in the same action”.

3.2 Cargo is totally lost en route

A total loss may occur for instance in heavy weather: the ship becomes a wreck and her cargo is totally lost.

The person asserting ownership of the cargo prior to its destruction may sue the carrier, regardless of whether he was the original owner (the sender/shipper) or the buyer of the cargo. In some cases the owner’s

²⁵ The Norwegian term “*panterett*” covers all of these forms of security, and for the sake of simplicity we use the term *mortgage*, and *mortgagee* for the beneficiary.

claim may even have been transferred after the loss. In such a situation the acquirer will be entitled to sue the carrier. This is typically the case where the cargo insurers have compensated the owner – regardless of whether there is a formal transfer or the company has acquired the claim on the basis of *cessio legis*.²⁶

In short, the rules are the same as those stated above in connection with damage to the cargo. And the same is true regarding a mortgagee or a buyer who had not acquired ownership prior to the loss.

4 Cargo transported under a bill of lading

4.1 Preliminaries

The bill of lading is in many ways a peculiar document that has important legal consequences not only for the issuer and the holder, but often also for third parties. In our context, it is sufficient to bear in mind the following.

The bill of lading is issued by the carrier. It contains his receipt for goods received, which are usually stated to be loaded on board the ship, and his promise to transport the goods to a named port and there deliver them to the person who presents the bill of lading and according to its terms is entitled to receive the goods. These characteristics facilitate the sale of the goods: a buyer paying the purchase price against obtaining possession of the bill of lading can be certain that no one else will take delivery of the goods at the port of destination. In addition, the description of the goods in the bill of lading gives him a (limited) possibility of ascertaining that the goods conform to the sales

²⁶ See, Rt. 1969 p. 1032, as mentioned in 3.1.2 above.

contract.²⁷ Transfer of the bill of lading – the physical handing over combined with written assignment if the bill of lading is not a bearer bill – has the effect that the new holder now has the exclusive right to demand delivery from the carrier. In many instances ownership is transferred simultaneously, but this is not necessarily the case. The bill of lading may for instance be transferred to a bank under a letter of credit arrangement.²⁸ In other words, whether ownership passes on transfer of the bill of lading is a question that has to be decided in the light of the circumstances of the case, see, *e.g.*, the Supreme Court decision in Rt. 1903 at p. 724 where the judge, speaking for the majority of the court, concluded after having stated the facts: “I find that what has happened sufficiently clearly shows that it was the intention of [A] to transfer ownership of the goods to [B]” (p. 724). But such transfer is dependent upon A in fact being the owner of the goods. If A is named as owner in the bill of lading and B acquires the bill of lading believing in good faith that he will thereby acquire ownership of the goods, this will be no defence against an ownership claim presented by C.²⁹

4.2 The right to sue when a bill of lading is issued

We will consider three situations: (i) the bill of lading has not been presented to the carrier, typically because the cargo has been totally lost; (ii) the bill of lading has been presented and the cargo has been delivered; and (iii) the carrier is not willing to deliver (release) the cargo.

²⁷ The smooth operation of this system presupposes, of course, that the carrier follows the rules, *i.e.*, he provides an adequate description of the goods and delivers them only to the person entitled to them (and is liable if he does not do so and in such circumstances has sufficient resources to cover the ensuing claim). See MC Sections 292-306.

²⁸ The buyer’s bank, having opened a letter of credit in favour of the seller, pays the purchase amount against receipt (*i.a.*) of the bill of lading – and may in turn give possession of the bill to the buyer, on credit terms or against payment.

²⁹ But if C derives his asserted ownership from the same person as A, there will be a dispute over conflicting rights arising from a double sale, which C – not having secured possession of the goods – is very likely to lose, *cf.* MC Section 306.

4.3 Total loss of cargo

If the cargo is lost *en route* a number of claimants may be envisaged: the holder of the bill of lading (in his capacity as owner or, for instance, mortgagee); the previous holder of the bill of lading; or a party not asserting any connection to the bill of lading. The person holding the bill of lading is in an advantageous position, but since our question concerns the right to sue, the assertion of ownership is decisive. The previous holder may also meet the requirements of the Disputes Act Section 1-3: he may for instance assert that he is still the owner, and that the actual holder is a mortgagee or his agent. And the person who has no connection with the bill of lading may for instance claim that someone has disposed illegally of goods belonging to him, or that the goods have been sold to him by the sender, before or after the issuance of the bill of lading.³⁰

The situation where the goods have been delivered without presentation of the bill of lading may be considered a special variety of loss of goods: the holder of the bill of lading demands delivery of the goods but gets nothing because the goods have already been released to another. There is no difficulty here in stating that the holder of the bill of lading meets the requirements of the Disputes Act Section 1-3, regardless of whether he asserts himself to be the owner, acting on behalf of the owner, or the mortgagee.

4.4 The bill of lading has been presented and the cargo has been delivered

We assume here that the goods have been released to A by the carrier following presentation by A of the bill of lading, whereafter the goods are found to be damaged. The obvious claimant is A, but as in 4.3 above one can envisage other possible claimants, for instance B asserting himself to be the true owner of the goods.

³⁰ Clearly the substantive rules applicable in these examples may vary – *e.g.*, the holder of the bill of lading will rely upon the contractual rules in the MC while the owner who has been subject to illegality may have to rely upon tort rules.

4.5 The carrier refuses to release the goods

The carrier may allege a right of retention, for example to retain possession of the goods until his claim for freight and other items is covered. Whether the carrier has such a right may in many instances be doubtful, both regarding the type of claim and the sums demanded. The holder of the bill of lading is the obvious claimant in this situation, but rights asserted by others may be sufficient to form the basis of a suit. This is particularly true of a person claiming that his goods have been subject to transportation without his consent.

5 Some additional remarks regarding the situation when carriage is performed by a carrier with whom the cargo owner has no contract

Under the agreement whereby A undertakes to have the goods transported by sea, while the actual transport may be performed by means of a vessel belonging to A, a number of scenarios may involve the use of a vessel belonging to B – for part or all of the voyage. We will, however, restrict the present discussion to the situation where the primary obligation is to provide transport by means of A's vessel, but with an option for A to make use of a vessel belonging to a third party. Let us assume that this option has been exercised and that B has become the performing carrier.³¹ In the context of liner shipping, the transport will proceed as follows: the cargo is received at A's terminal and loaded on board by A's servants, but under the supervision of B's master and crew; at the port of discharge the order of events is reversed, ending with A

³¹ The issuance of a bill of lading may complicate matters, because the bill of lading may be binding on the performing carrier B, *cf.* Falkanger & Bull *op. cit.* pp. 327-331. Here we assume that there is no direct contractual relationship between B and the cargo owner.

delivering the goods to the cargo owner.

The following remarks concern only the situation where the goods arrive damaged. As above, we start with cargo being transported under a sea waybill, issued by and binding on the liner operator.

The cargo owner can, of course, start proceedings against A. He can also sue B, claiming that the damage either occurred while B had possession of the goods or was a consequence of what happened during that period. The suit against B is basically a suit in tort, but MC Section 286 has for all practical purposes made it contractual, see Section 286 (1) first sentence: "A sub-carrier is liable for such part of the carriage as he or she performs, pursuant to the same rules as the carrier." And in a suit against the carrier the cargo owner cannot evade the contractual rules protecting the carrier by basing the claim on tort, see MC Section 282.

A number of considerations, in particular uncertainty with regard to the exact time when the damage occurred, may argue in favour of suing A and B jointly, which is permissible under the Disputes Act Section 15-2. It should be noted, however, that if A and B are held jointly and severally liable (MC Section 287 (1)), the total liability which can be imposed on them "shall not exceed the limits of liability according to Section 280 [with unit and kilo limitation rules], unless the contrary follows from Section 283 [on loss of the limitation privilege]" (MC Section 287 (2)).

Words, drafting and the law

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“If it had grown up”, she said to herself,
“it would have made a dreadfully ugly child:
But it makes rather a handsome pig, I think.”
(Alice in *Alice’s Adventures in Wonderland*)

1 Some introductory remarks

Hans Jacob Bull has for many years performed various functions at the Scandinavian Institute of Maritime Law (NIFS), University of Oslo, having served as director of the Institute for a considerable period. His primary fields of research have been maritime law including, above all, marine insurance law. Particularly in the case of maritime law, we have a common interest, and over the years our various interests have coincided at a number of points. One such point lies at the intersection of maritime law, sales law, insurance law and the law related to payments and financial undertakings.

Since Hans Jacob will shortly retire from his position at NIFS and the university, it has been decided that this volume of *Simply* will be in his honour, and I am very happy to have been allowed to participate with a small contribution.¹ My choice of topic is neither maritime law nor insurance law, but rather a spectrum of legal questions that may arise in connection with the use of various words that are to some extent found in, and in relation to, insurance. These various words are, however, more commonly related to various payment undertakings and types of financial security and their respective relationships with the underlying contract.

As Samuel Johnson once said, language is the dress of thought, and words may often present lawyers with a dilemma. Words and phrases that are used for different purposes may gradually come to have various

¹ Let me also take this opportunity to extend to Hans Jacob and his colleagues at NIFS my thanks for many years of informative and congenial cooperation.

legal meaning with different implications.² Words do not necessarily mean the same thing when used by the legislator and by the contract draftsman. When drafting a contract, the use of certain terminology may make certain rules applicable, while the use of other words may result in the application of other rules. Sometimes it may be hard to determine the legal significance (if any) of certain words, because in a contractual context they may have to be understood in the light of the surrounding circumstances. Against this background I will discuss something of the relationship between the significance of words, the role of custom and trade practice and the role of law.

As is well known, a distinction is normally made between instructions, statements and undertakings, although it is not always easy to distinguish between a statement and an undertaking.³ It is, however, also important to bear in mind the fact that the words used may have to be construed in the context of various data relevant to their interpretation, such as items regarded as being implied and the behaviour of the parties (although this is generally less true in common law jurisdictions than under Swedish law).⁴

Swedish law will naturally form the basis for this little legal excursion, but I will also make occasional reference to other legal systems for the purposes of illustration.

² Words may have a particular meaning in one context but not in another. Words that may have certain implications when used in legislation may, when used in a contract, also have to be understood in the context of other facts.

³ For example, loan agreements commonly contain both “representations” and “covenants”. These terms have different legal implications, but where certain legal techniques are applied, a representation may actually have more or less the same effect as a covenant. See, e.g., Cranston, *Principles of banking law*, 2nd ed. London 2002 and Wood, *Law and practice of international finance*, London 2008. Even if this terminology is not used in exactly the same way in other legal systems, it does seem to be recognised at least in international loan agreements.

⁴ There are certainly several differences between the Scandinavian and English approaches to interpreting contracts. One example concerns the courts’ willingness (or not) to fill in “gaps”, but having said that, it appears that the fundamental differences in approach have been lessening to some extent.

2 Law and usage and the significance of words

We will take an insurance contract as our point of departure. Insurance normally involves an undertaking by the insurer to pay out a sum of money in the event the insured has a valid claim under the insurance policy.⁵ Roughly speaking, insurance involves an undertaking by the insurer to cover an economic loss incurred by the insured. The insurance may relate to an underlying agreement, such as a sales agreement, that contains certain agreed conditions.⁶ The insurance undertaking normally contains a promise by the insurer to cover, either generally or on specific terms, such risks as the insured party may encounter, whether this is the risk of loss or damage to an insured item, or the risk of the insured encountering liability, *etc.* One particular type of insurance, credit insurance, covers losses that may be encountered under a financial agreement. This type of insurance may be drafted in words that are similar to those of a financial guarantee.

In several other types of agreements we find similar, although not identical types of undertakings, *e.g.*, in connection with payments and

⁵ As stated in *Black's Law Dictionary*, 4th. ed. 1951: "An /insurance/ contract whereby, for a stipulated consideration, one party undertakes to compensate the other for loss on a specified subject by specified perils."

⁶ Taking a sales contract as an example, there will often be a clause setting out which of the parties is to bear certain costs and risks. The parties will, for example, often agree on a particular Incoterms clause (Incoterms as drafted by the ICC, the most recent version as amended in 2010) to specify the particular allocation of costs and risk as between the seller and the buyer.

certain financial undertakings.⁷ Many of these types of transactions have their roots in *lex mercatoria* and have often developed step-by-step into their present form. During this process of change and amendment, legislation has sometimes been introduced in order to give the original transactions a more precise and solid legal foundation.

So this is the area we are navigating in an attempt to establish how words and phrases may be carried into different areas of the law. In the following I provide some examples, as well as analysing some of these undertakings in the light of various legal frameworks. In doing so I also try to illustrate how various undertakings may stem from different backgrounds and then may gradually develop from undertakings of a more general character to take on more specific functions. By drafting an undertaking or a statement in a particular way and by using particular phrases, the parties will often intend certain rules to apply.⁸

Sometimes, however, the parties may not have foreseen the precise effect of the words used in a particular case. They may have misunderstood each other, or they may have misinterpreted a particular word in a particular situation or attributed to it different meanings. As a result we will also have to pay some attention to questions related to the con-

⁷ Credit insurance is a particular type of insurance taken out by an insured party at risk of encountering specific financial losses, *i.e.*, losses due to other types of events than physical events (such as damage to or loss of goods), political events, *force majeure* events. Risks under credit insurance have often proved very hard to determine precisely in advance, since the traditional insurance methods for determining risk are not available. Traditional insurance risks are predetermined and are absorbed in a different way than financial risks under, *e.g.*, a loan agreement, where the lender will have to assess the risk of default by the borrower. By lending the lender has parted with money, but in traditional insurance the insurer often has a limitation clause and will be liable to pay out only in certain agreed circumstances.

⁸ Related questions have been touched upon by Ingvarsson in *Borgensliknande säkerheter*, Stockholm 2000, in which, in chapter 14, he deals specifically with guarantees issued in the form of insurance. He also deals with the question whether a guarantee issued by an insurance company should be regarded as insurance or as a guarantee and concludes that this type of undertaking should rather be regarded as a form of insurance. My personal view, expressed in *Något om gränsdragningen mellan borgen och kreditförsäkring*, *Festskrift till Børge Dahl*, København 1994 p. 85 *et seq.*, is that the functions of the undertaking itself rather than the entity making the undertaking should be decisive. That view was not shared by the arbitrators in the case on which the article was based.

struction and interpretation of contracts.⁹

3 Different types of payment undertakings

3.1 Some general points

Payments and financial undertakings may have similar bases.¹⁰ Payments are basically primary in nature. In other words, the obligor has a primary duty to pay on certain terms and conditions, *e.g.*, the buyer's duty to pay under a sales contract, the borrower's under a loan agreement *etc.* This is also the case, for example, under a "note of indebtedness",¹¹ which might be worded along the following lines: "I shall (re)pay to you (NN) the amount of USD XX on ... day". Other undertaking can be

⁹ Words and phrases used in a contract may have precise meanings, but they may also have to be construed against the background in which they are applied. See, *e.g.*, regarding Swedish law, Ramberg, *Medveten avtalsotydighet*, JT 1989-90 s. 639, Ramberg & Ramberg, *Allmän avtalsrätt*, 8 ed. Stockholm 2010 p. 152 and Adlercreutz & Gorton, *Avtalsrätt II*, 6th ed. Lund 2010 p. 146 *et seq.*

¹⁰ I should emphasise that various new payment methods have been introduced during recent decades, see *e.g.* Arnesdotter, *Moderna betalningsmetoder: betalning och givning*, Stockholm 1995 and Lehrberg, *Moderna betalningsformer*, 3rd ed. 2005.

¹¹ Swedish law makes a distinction between an instruction to pay (*e.g.*, in connection with a bill of exchange) and an undertaking to pay (*e.g.*, under a promissory note). Since the late 1930s, the Nordic countries have had identical legislation on instruments that under these legal systems are considered to constitute promissory notes. The Swedish statute is known as *lag (1936:81) om skuldebrev*. Since the term "promissory note" may not have exactly the same meaning in Swedish law as in common law jurisdictions, parties involved in international transactions instead use the term "note of indebtedness", and for that reason I sometimes use this term here. See, *e.g.*, Rowe, *Bills of exchange and promissory notes in the law of international trade finance* (in *The law of international trade finance*, ed. N. Horn), Deventer 1999 p. 243 *et seq.* Rowe states that a bill of exchange is an order to another party to pay, but that a promissory note is a promise of payment by the person who signs it. Both documents are by their nature negotiable instruments. In Swedish law only documents issued in favour of "[a named person] or to order" or to "the bearer" are negotiable, but an "*enkelt skuldebrev*" ("I will pay to [a named person]") is not. In footnote 24 below I refer to a recent Swedish Supreme Court decision, in which it was held that the holder of a negotiable promissory note could not rely on the issuer's payment undertaking.

added to this very simple basic formula, such as the payment of interest, amortisation, *etc.*¹²

A financial security is often based on an underlying transaction. In other words, the security is consequential on an undertaking that is set out in the underlying transaction. As already mentioned, a payment is sometimes based on an instruction to pay (“pay to X the sum of ... against”). This was the case historically with letters of credit. A letter of credit was a document that a traveller could carry with him for presentation to a particular person who would make payment to the bearer (“pay to NN bearing this letter a sum of”) in return for the instructing party’s promise to reimburse the sum concerned.¹³ The same basic concept is embodied today in cheques and bills of exchange. The issuance of a cheque or bill of exchange is generally done in compliance with a requirement in an underlying transaction. Taking a functional approach, this is also the concept underlying modern letters of credit and on-demand guarantees (as well as suretyships), where an underlying transaction triggers the issuance of a letter of credit or a guarantee. Some of these instruments are independent of the underlying contract, others, however, are not.

If a payment takes place in advance or on a “Zug-um-Zug” basis (*i.e.*, payment is made upon counterperformance by the other party), there will not normally be any need for financial security, but in other cases a secondary payment undertaking may be called for. In other words, a second obligor promises to pay if the first obligor defaults on his contractual duty to do so.

Depending on how any such secondary payment undertaking is drafted, the second obligor may take on a payment duty that is *either* secondary to that of the primary obligor *or* primary, *i.e.*, on the same level as that of the primary obligor. Naturally this makes a difference. Such an undertaking is, however, basically an “accessory” to the under-

¹² Such a payment undertaking may be related to a specific plan of repayment such as “payable in X instalments each of ... USD XX and the payment of interest at the rate of Y percent above LIBOR until fully repaid”. It may also be repayable *on demand*.

¹³ See Gorton, *Rembursrätt*, Lund 1980, p. 26 *et seq.* with references

lying transaction, although the undertaking may also be designed as an *independent* undertaking, possibly drafted in a somewhat different way.¹⁴

Accordingly, depending on how the undertaking is drafted, the primary obligor and the secondary obligor may be liable to pay the payee (sometimes known as the beneficiary) in a certain sequence, *i.e.*, the primary obligor first, then – only if the latter defaults – the secondary obligor. In other cases the beneficiary may opt to direct his claim against either one of them. In some cases the guarantee may be of an independent nature, in which case the guarantor will be liable to make payment irrespective of the validity of the underlying transaction. In all cases the question of redress may also arise, so that payment liability ultimately rests with the party responsible under the various agreements.

Accordingly it will be necessary to evaluate the payment undertaking and the role of the financial security, which may sometimes be closer to, or even equivalent to, a payment undertaking.

4 Various statements/undertakings and the relevant legal frameworks

4.1 In general

A financial undertaking (whether a payment, a loan, a guarantee, a suretyship or other form of undertaking) may be given by any person, *i.e.*,

¹⁴ Some guarantees are commonly made out as “irrevocable, payable on demand and independent [from the underlying transaction]”, as will be further discussed below. “Independent” is the term used in the Uncitral international convention on independent guarantees and standby letters of credit.

by a private or legal person, or by a private or public entity.¹⁵ This means that there is a limited amount of legislation specifically regulating the various financial undertakings given, and so to a large extent they will have to be interpreted and construed in accordance with their wording and against the background of particular and general legal rules. These may include restrictions on the ability of certain entities to get involved in certain dealings, as well as rules on unreasonable contract terms. As a result the involvement of certain entities in particular dealings has been questioned, *e.g.*, on the basis of the doctrine of *ultra vires*, or because the person signing the document was not regarded as having authority to do so, or due to the “piercing the corporate veil” doctrine, or for another reason.¹⁶

To consider some somewhat similar examples in Swedish law (although not involving *ultra vires* questions), in case 1992 s. 375, the Supreme Court dealt with a situation that also involved to some extent the question of piercing the corporate veil. In this case a local authority had issued a letter of comfort spelling out its intention to retain its majority stake in a certain entity and also to maintain a long-term policy of operating the entity in such a manner as to enable it to fulfil its obligations *vis-à-vis* the bank. The questions arose whether the wording constituted an undertaking or not, whether the local authority was entitled to involve itself in such deal and whether, due to the “piercing the corporate veil” doctrine, the local authority would be liable. The Supreme Court discussed the use and the relevance of letters of comfort, but found that the bank was fully aware of the situation and could have

¹⁵ A general survey of personal financial security is found in the study on Personal Security (PEL Pers. Sec.) in one of the books in the *Principles of European Law* project, Munich 2007, prepared by U. Drobnig. There are provisions on dependent personal security (suretyship guarantees), as well as independent personal security (indemnities/independent guarantees). In the study, reference is made to the UCP, the URDG, as well as to the Convention on Independent Guarantees, see p. 321 *et seq.*, which will all be discussed further below.

¹⁶ In English law the *ultra vires* question was considered in a couple of cases during the 1990s, namely *Hazell v. Hammersmith and Fulham London Borough Council* /1992/ 2 AC 1 and *Kleinwort Benson v. Lincoln City Council* /1999/ 2 AC 349. Related questions have been discussed by McCormack, *Legal risk in the financial markets*, Oxford 2006 pp. 35 *et seq.*

protected its interests by demanding better financial security. The court concluded that under the circumstances there was no liability on the part of the local authority.

Under Swedish law the question of authority in connection with financial undertakings and banks has been illustrated in two cases from 2001 and 2002. In the first case (NJA 2001 p. 191), the Supreme Court concluded that a bank officer (a branch manager) was authorised to bind the bank when releasing some private guarantors from their guarantee undertaking *vis-à-vis* the bank. In the second case (NJA 2002 p. 244), however, a bank officer holding a similar position but in a smaller branch was considered not to have bound the bank when issuing a bank guarantee for a substantial amount. This was because the transaction was regarded as both unusual and unusually large for a relatively small branch.¹⁷

Below I will discuss some of the wording used in connection with letters of comfort and financial undertakings.

4.2 Letters of comfort

Although not generally designed to constitute definitive payment undertakings, we should mention “letters of comfort” in this context.¹⁸ The main reason for starting our discussion with the “letter of comfort” is that it has no clear legal significance, and so its legal effect will depend on its wording and other circumstances. This is an area where there is no solution to be found in legislation in either Swedish or English law, which means the court has to fall back on principles for the interpreta-

¹⁷ The first case dealt with an ordinary suretyship, while the latter concerned the issuance of an on-demand guarantee.

¹⁸ Letters of comfort are sometimes referred to as letters of awareness or letters of intent. The terminology varies and the contents and functions of any particular document are often not very precise. It is questionable whether they really comprise a contractual undertaking or should rather be considered as statements lacking any precise legal contractual implications. In Nordic legal doctrine works on this topic include Røsaeg, *Garantier eller fattigmans trøst? Støtteerklæringer i selskapsforhold av typen “comfort letters”*, Oslo 1992, but reference can also be made to Iversen, *Støtteerklæringer*, København 1994 and Gäverth, *Stödbrev – borgensliknande handlingar utställda företrädesvis för svagt kapitaliserade bolag*, Uppsala 1994.

tion of contracts.¹⁹ This is particularly difficult when the wording used does not necessarily imply a particular understanding between the parties, who in fact are often in disagreement as to they wish to achieve with their chosen wording, and also frequently on what (if anything) they have actually agreed. The court will then have to revert to general principles for the interpretation and construction of contracts. This means that different factors may have to be taken into consideration, such as the common intention of the parties, the wording used by the parties, implied undertakings *etc.* The Swedish case NJA 1995 p. 586 thus illustrates a different approach to that taken, as in *Kleinwort Benson v. Malaysia Mining*, under English law.

If the parties have used words signifying a clear undertaking, there will undoubtedly be a contractual obligation to that effect.²⁰ But a mere statement will hardly give rise to a legal obligation, although certain wording taken in the context of the surrounding circumstances could conceivably impose some kind of legal obligation, even if this is not contractual in nature.²¹ Alternatively, a statement may not have any legal consequence at all.

This means that the result when words are taken independently may

¹⁹ The situation is similar in the other Nordic countries, as it is in many other countries, *i.e.*, the significance of how a contract is drafted has to be determined taking into consideration the principles for interpreting contracts developed in different legal systems. See, *e.g.*, in Swedish Supreme court practice NJA 1992 p. 375, NJA 1994 p. 204 and NJA 1995 p. 586. English case law in this area is very sparse and the most widely discussed case is a Court of Appeal decision, *Kleinwort Benson v. Malaysia Mining Corporation /1989/ 1 Lloyd's Rep. 556*. The Court of Appeal held that the wording used did not constitute an undertaking but should rather be regarded as a statement that probably involved an undertaking for a short time after it was given. See, *i.a.*, Treitel, *An outline of the law of contract*. Oxford 6th ed. 2004 p. 60

²⁰ In NJA 1995 p. 586, the Swedish Supreme Court applied interpretative principles to come to the opposite conclusion to that reached by the English court in *Kleinwort Benson v. Malaysia Mining*, *i.e.*, that there was a binding undertaking, see footnote 20.

²¹ This seems to be the reasoning behind the Supreme Court decision in NJA 1994 p. 204. The first person in Swedish legal doctrine to deal with the topic was Knut Rodhe who, in *Moderbolags ansvar för dotterbolags skulder, Festskrift till Jan Hellner*, Stockholm 1994 pp. 481 *et seq.* and pp. 494 *et seq.* enumerated a number of phrases used when drafting letters of comfort. These different formulations may have different effects.

differ from the result when they are taken together with the common intention of the parties. In some circumstances a phrase may have no legal significance, but in view of the circumstances it may either cause some obligation to arise (“*culpa in contrahendo*” – a concept not generally accepted in English common law) or may even constitute an explicit undertaking.

4.3 “I shall pay to you”

The phrase quoted above would, in Swedish (Scandinavian) law, basically be covered by the Promissory Notes Act (*Lagen 1936:81 om skuldebrev*). It is a simple statement announcing the debtor’s undertaking to pay to the creditor a certain sum on a specific date (or dates), either on demand or in accordance with a repayment schedule.²² Such a payment undertaking often reflects the receipt of a loan, but it could also reflect, for example, an open credit under a sales agreement. The Act provides that the promissory note can be made out to a named person only (in which case it is not negotiable or transferable and will sometimes be referred to as a “note of indebtedness”), to a named person or to order or to the bearer. In the two latter cases a new holder of the note will have a direct claim against the debtor.

If the debt is in the form of a document made in favour of “[a named person] or to order” or to “the bearer”, the debtor has a primary duty to pay as agreed. Such a duty exists unless there is no valid underlying contract, for example, where the loan agreement is not enforceable for other reasons. This would be the case in a situation where the debtor has a counterclaim against the creditor *in specie*, for instance because the goods sold did not comply with the terms and conditions of the sales contract. This means that the payment undertaking may in some cases be subject to the validity of the creditor’s claim under the underlying transaction, but in general the holder in good faith of a note made “[to a named person] or to order” or to “the bearer” will be entitled to

²² Similarly the buyer may undertake to pay the seller in exchange for goods delivered. In Swedish law this follows from art. 48 of the Swedish Purchase Act, *cf.* also art. 49.

payment.²³

4.4 “We guarantee the due repayment by... to you”

In Swedish law, so-called personal guarantees (suretyships, in Swedish “*borgen*”) are governed by the rather rudimentary legal rules of the Swedish “commercial book” (“*HB*”).²⁴ There are also a number of academic books and articles dealing with related topics.²⁵ Swedish law, like a number of other legal systems, distinguishes between a joint guarantee (“*enkel borgen*” (*HB* 10:8)) and a joint and several guarantee (“*proprieborgen*” (10:9)). The former is the basic version, signifying a suretyship/guarantee that imposes on the surety a secondary duty to pay the payee (the beneficiary) in the event the primary obligor fails to pay. Thus it is a guarantee of a secondary nature: its function is to make sure that the beneficiary gets paid, but only if the primary debtor fails to do so. In Swedish law this means that the party entitled to performance must use all reasonable measures against the primary debtor before turning to the surety, although the creditor does not have to wait for the bankruptcy of the debtor, since the debtor’s inability to pay will suffice to allow the creditor to claim against the surety.

²³ In an interesting Swedish case (case no. T 4904-08), the Supreme Court decided in a decision dated 16 September 2010 that the negotiability of a promissory note under certain circumstances ceases when the promissory note has been transferred in such a way that the obligor has not been in a position to have it returned. The case concerned promissory notes that had been signed by the debtor several years previously and had been transferred to another holder. The question was whether the debtor under a negotiable promissory note was entitled to claim that it had already been paid. Pursuant to art. 15 of the Promissory Notes Act, a debtor could do this only if the holder could be proved to have been aware that payment had already been made. However, the Supreme Court held that, under circumstances such as those at hand, holders of promissory notes (at least if they were financial institutions) would have to prove that payment had not been made. This is an example of the court modifying legislative provisions.

²⁴ Known as *Handelsbalken* and containing some few sections on personal guarantees in 10:8 - 10:12.

²⁵ See *i.a.* Bergström, *Några problem rörande bankgaranti. i Teori och praxis. Skrifter tillägnade Hjalmar Karlgren*, Stockholm 1964 p. 21 *et seq.*, *Lenlander, Kredit och säkerhet. Lärobok i krediträtt*. 9. ed. Uppsala 2006 p. 37 *et seq.* and *Walin, Borgen och tredjemansrätt*, 3. ed. Stockholm 2002 p. 25 *et seq.*

Although the legislation appears to deal with private persons acting as sureties (guarantors), it may also involve suretyships (guarantees) issued by legal entities, especially banks. Banks always charge a fee for issuing a guarantee, whereas a private person acting as a surety would rarely request any remuneration. This is a difference of some practical significance.²⁶

4.5 “We guarantee as for our own debt the due repayment by to you”

In contrast to the situation with a joint guarantee (“*enkel borgen*”), the wording (as quoted above) of a joint and several guarantee (“*proprieborgen*”) makes the guarantor (the surety) and the primary debtor equally liable to pay the beneficiary. Thus the beneficiary is entitled to turn towards either of the two for payment – there is no requirement first to demand payment from the primary debtor. In practice, however, a bank as payee would normally first pursue the primary debtor for payment before claiming from the surety.²⁷ This is also how banks generally describe the situation when negotiating a “*proprieborgen*”, but the law is clear on the fact that the payee could turn against either.²⁸ A “*proprieborgen*” is, however, dependent on (“accessory to”) the validity of the underlying transaction.

4.6 “We guarantee the due performance by ... under the...”

In general a suretyship is a financial guarantee, *i.e.*, the guarantor is liable to pay an amount of money, *e.g.*, the debt of the primary debtor.

²⁶ See the discussion in Bergström p. 21 *et seq.*

²⁷ In Norway the *Lov om finansavtaler of finansoppdrag (Finansavtaleloven)* from June 25, 1999 and July 1, 2000 contains a number of rather detailed provisions on suretyships and the relationship between the parties involved.

²⁸ Another possible question is whether banks, by stating that they would not first claim payment from the surety, create a trade practice to this effect, preventing them from falling back on the primary undertaking by the surety.

A guarantee may, however, also consist of the surety's secondary undertaking to perform *in specie* in accordance with the primary obligor's duty to perform its contractual obligations. Consequently, the guarantor may, depending on the drafting of the guarantee and other circumstances, either have a duty to perform the contract *in specie* or to pay damages if the primary obligor fails to do so.

It is not always clear whether a guarantee is of one type or the other. Nor is it always clear whether the undertaking is only of a secondary nature (*i.e.*, the guarantor will only become liable if it becomes clear that the primary obligor will not perform). A guarantee may sometimes clearly set out that it is a guarantee *in specie*. Parent company guarantees given for the performance of a subsidiary may sometimes be of this type, and guarantees may also be given by particular companies undertaking to perform an underlying contract if the primary obligor fails to perform.

Banks do not normally issue this type of undertaking, since they would not agree to perform *in specie*, but only by providing financial compensation. However it is not unusual for the World Bank, when lending money to construction projects, to request a substitute construction firm to undertake to step in and perform the contract if the first contractor defaults.²⁹

4.7 “We shall pay to....against the presentation of the following documents.”

In letters of credit (documentary credits) the payment statement made by the bank (the opening bank or the issuing bank, or the confirming bank as the case may be³⁰) sets out the bank's obligation to pay the beneficiary (often the seller), against the presentation by the latter of certain enumerated documents (such as an invoice, insurance documents, transport documents *etc.*), either a fixed amount of money or an

²⁹ In project finance and PP projects, the financiers fairly commonly demand the inclusion in the contract documentation of a so-called “step-in rights” clause, entitling them to take over the project if the debtor defaults.

³⁰ The issuing or opening bank promises to pay irrevocably and the confirming bank adds its independent payment undertaking, see definitions and art. 7 of the UCP 600.

amount of money subject to a stated maximum. This payment method should already have been agreed between the seller and the buyer in the sales contract. This contract should form the basis for the drafting of the letter of credit by the opening bank when issuing the credit. Consequently the bank steps into the shoes of the buyer as the primary payor. The bank's undertaking in this case not only provides security for the payment, but is an immediate promise of payment, provided that the beneficiary presents the correct documents. In this sense the bank's undertaking differs from those discussed previously. The bank will, of course have a redress claim against the buyer.³¹

The way a letter of credit is drafted reflects the trading nature of the document, *i.e.*, it is a payment device entitling the seller (the beneficiary) to receive the price of the goods in exchange for presentation of the agreed documents.³² Under the prevailing rules (presently the UCP 600), the documents presented should conform with the requirements of the letter of credit as well as those of the UCP 600,³³ to which most letters of credit refer.

The question of conforming documents is probably the single most disputed issue in relation to letters of credit, and also concerns the issue of fraud either under or in the document itself. This is also an area where we may encounter a variety of national material or procedural

³¹ In practice a bank, when undertaking to issue the letter of credit, will either demand payment of the relevant amount into an account or grant a specific credit to the buyer. Alternatively the buyer may use an existing credit facility.

³² In Gorton, *Sammanflätade avtal – några reflektioner, särskilt med avseende på relationen mellan köp och remburs*. The Stockholm Centre for Commercial Law Årsbok I, Stockholm 2008 p. 55 contains a discussion on the relationship between the letter of credit and the underlying transaction. As follows from arts 4 and 5 of the UCP 600, the letter of credit is explicitly separate from the underlying transaction, although the underlying transaction is the basis for the letter of credit.

³³ See *i.a.* Kurkela, *Letters of credit and bank guarantees under international trade law*, 2nd ed. Oxford 2008 and his comments with respect to art. 14 (standard for examination), art. 15 (complying presentation) and art. 16 (discrepant documents, waiver and notice) in UCP 600.

legal rules.³⁴

4.8 “We shall pay you unconditionally and on first demand”.

The phrase quoted above basically reflects the wording of a so-called on-demand guarantee.³⁵ Generally an on-demand guarantee will refer to an underlying transaction, which might be a loan, a sale, a construction contract or virtually anything else. Like a letter of credit, however, it is *independent* from the underlying contract. In the URDG this follows from art. 5 and 6.³⁶

Although the wording used is for all practical purposes that of a primary obligation, the function of an on-demand guarantee is secondary in nature. It is not intended to be used as an immediate payment undertaking, but rather to provide financial security if the primary debtor fails to pay.³⁷ The guarantee’s wording, however, makes it an immediate payment undertaking, and the guarantor cannot refuse to pay on the grounds that the claim should first have been directed towards the primary debtor.³⁸ The wording appears close to that of documents referred to above as promissory notes or notes of indebtedness. The words “first demand” entitle the holder to demand payment on first demand, while the word “unconditionally” makes the guarantee an independent undertaking, *i.e.*, the beneficiary is entitled to payment whether or not the underlying transaction is enforceable, as well as in

³⁴ See *i.a.* Schmitthoff, *International and procedural aspects of letters of credit* (in *The law of international trade finance*, ed. by N. Horn) p. 227 *et seq.* Related questions concerning fraud often arise in connection with documents presented, see *e.g.* also Gorton, *Seller’s or shipper’s fraud* (in *Maritime fraud*, ed. by K. Grönfors, Gothenburg 1984 – Swedish Maritime Law Association no. 64) p. 27 *et seq.*

³⁵ See Bertrams, *Bank guarantees in international trade*. 3rd rev. ed. ICC 2004, which also refers to ISP 98, the International Standby Practices. Bertram’s book is probably the most comprehensive available on bank guarantees.

³⁶ Cf. corresponding articles in UCP 600 4 and 5.

³⁷ We should mention that on-demand guarantees, at least in some instances, were developed to function as an alternative to advance payments.

³⁸ The URDG, in articles 14, 15 and 16, contains provisions for making a call under the guarantee.

circumstances where there is a breach of contract or similar.³⁹

As long as there was no particular regulation with respect to on-demand guarantees, national courts had to deal with the legal problems arising out of them, taking as their point of departure the law relating to payment undertakings, the law related to suretyships, the principles for the interpretation of contracts *etc.*

In the only Swedish Supreme Court case⁴⁰ so far to deal with on-demand guarantees, the following wording had been discussed by the parties:

“As security for a short tum [*sic.*, presumably “short term”] credit facility which you have granted to Mr ___ Bank hereby unconditionally and irrevocably guarantee as for your debt the amount of”

This type of wording is frequently used in on-demand guarantees. In this case the undertaking was not signed. There was also another undertaking, which was the one central to the case:

“Subsequent to a sales agreement made concerning the acquisition of shares in /company/ between you as seller and /Y company/ as buyer, we undertake to pay at the earliest on 1988-09-022 on your

³⁹ Here again it is fundamentally important to recognise that the duty to pay out under the guarantee does *not* mean that a wrongful demand may *not* be questioned in relation to the underlying transaction. The effect of the duty to pay out is that the beneficiary is entitled to obtain the money and keep it until his right to the money under the underlying transaction has been determined. In this sense the guarantee does give the beneficiary the same financial security as an advance payment. See the English case *Cargill v. Bangladesh* /1996/ 2 Lloyd’s Rep. 524. Should the guarantee cover liability under a liquidated damages clause, the payment under the guarantee will be affected by the underlying transaction only in the rare circumstances that the liquidated damages clause is set aside.

⁴⁰ In Swedish law, where very few Supreme Court cases have involved on-demand guarantees or, for that matter, letters of credit, the Supreme Court judgment in NJA 2002 p. 244 concerned an on-demand guarantee. This case has been discussed by, among others, Håstad, *Något om demand-garantier*, in *Festskrift till Lars Gorton*, Lund 2007 p. 185 *et seq.*

first written demand the amount of SEK....⁴¹

Again these words illustrate the relative proximity of an on-demand guarantee to a promissory note payable on demand. The Swedish Supreme Court in this case accepted the independent nature of this type of guarantee. In its discussion the court also referred to the importance of the then-prevailing URDG 458 and the UNCITRAL Convention on Independent Guarantees and Stand-by Letters of Credit, neither of which was, however, applicable to the case. Their mention in the court's reasoning was intended to illustrate the nature and functions of on-demand guarantees.

On-demand guarantees have been in use for at least 30-40 years, but have not been regulated by any particular rules. This means that when determining the effect of the words used, a court has to decide on the relevant legal framework (by looking at, *e.g.*, the wording, case law, other similar transaction types *etc.*). This is also how on-demand guarantees have evolved and how they have been interpreted against a background of promissory notes, suretyships, letters of credit *etc.* Various courts have also had to determine issues concerning fraud and abuse.⁴²

4.9 Standby letters of credit

Another beast in our collection is the standby letter of credit (or standby credit), which is for all practical purposes an on-demand guarantee dressed up as a letter of credit. Standby credits developed in the United States, where banking regulation stopped banks from issuing guarantees

⁴¹ The Swedish text says: "*Mot bakgrund av att köpeavtal träffats om förvärv av aktier i /company) mellan Er såsom säljare och /Y bolage/ såsom köpare, förbinder vi oss att tidigast 1988-09-22 på er första skriftliga anmodan erlägga SEK.....*" This text is apparently close to that found in promissory notes.

⁴² This is illustrated in the English case *Edward Owen v. Barclays Bank International* /1978/1 Lloyd's Rep. 166 (*cf.* at p. 171 .2). The case of *Turkiye Is Bank v. Bank of China* /1998/ 1 Lloyd's Rep. also referred to the Owen test. See also Debattista, *Performance bonds and letters of credit: a cracked mirror image*. In *Festskrift till Jan Ramberg*, Stockholm 1996, p. 101 *et seq.*, where the author discusses the similarities and differences between fraud in connection with letters of credit and abuse in connection with on-demand guarantees.

as a separate business, causing the banks instead to operate an equivalent business based on standby credits.⁴³ Standby credits are nowadays offered by many banks as an alternative to on-demand guarantees. Standby credits are also covered by the UCP 600, although their functions are not identical to those of on-demand guarantees (thus they are not intended to be payment undertakings). They cannot be drafted as primary undertakings, but the intention is to provide financial security rather than a payment undertaking. They are thus not the equivalent of traditional letters of credit.⁴⁴ Standby credits are furthermore covered by the URDG 758, and the Convention on Independent Guarantees and Stand-by Letters of Credit is drafted to apply also to standby credits. Furthermore, a dedicated set of principles has been developed for standby credits, namely the International Standby Practices 98 (ISP 98).

4.10 “We shall indemnify you”

Some mention should also be made of so-called “indemnities” or “hold harmless” clauses, which may have a function similar to that of a guarantee, although in other cases they may operate similarly to exemption clauses.⁴⁵

In English law, such indemnity clauses have been described as “clauses by which one party undertakes to indemnify the other party for any liability incurred by the latter in the performance of a contract; for example where equipment is hired out with a driver and the contract provides that the hirer is to indemnify for any liability incurred by the owner as a result of the driver’s negligence. In Swedish law, it follows as a general principle of obligatory law that a contracting party will not be able to contract out of his liability in case of intentional or (probably)

⁴³ See *e.g.* art. 1 in UCP 600.

⁴⁴ Standby credits developed in the US, see *e.g.* Gorton, *Rembursrätt i.a.* p. 42 and 116 and Kurkela p.

⁴⁵ See *Anson’s law of contract* (by J. Beatson) where related questions are discussed on p. 78 *et seq.*

gross negligence/recklessness.⁴⁶

No particular legislative framework exists with respect to indemnities, but like “letters of comfort” they have to be understood and interpreted in accordance with their wording and other relevant data.

An indemnity may thus have to be distinguished from a guarantee, but may also have to be seen, in Swedish law, in the light of section 36 of the Swedish Contract Act and, in English law, of the Unfair Contract Terms Act. In English law, the doctrine of consideration may also be significant.

Suretyships and guarantees sometimes contain specific clauses with regard to indemnities but, as mentioned above, it will otherwise follow from general principles of mandatory law that a guarantor who has made a payment to the creditor is entitled to take over the creditor’s claim against the primary debtor. In the UCP 600, article 13 explicitly provides for bank-to-bank reimbursement arrangements.

We should also mention the use of letters of indemnity (often known as back letters) in connection with the ocean carriage of goods and practices concerning transport documents. The issuance of clean bills of lading has for decades often involved the issuance of a back letter by the shipper. The carrier may thus have issued a clean bill of lading to the shipper in exchange for a back letter. This back letter sets out a promise to hold the carrier harmless for all consequences of having issued the clean document, even though it should have been marked with a reservation.⁴⁷ In many jurisdictions this practice is illegal, and the Swedish Maritime Code at 13:51 contains provisions to similar effect. A carrier may also in connection with the delivery of cargo without presentation of a bill of lading request the cargo receiver to undertake to indemnify the carrier for all consequences thereof. This undertaking may sometimes also be backed by a bank guarantee.⁴⁸

⁴⁶ Treitel p. 105. See also McKendrick, *Contract law*, 7th ed. London 2007 p. 237 *et seq.* and 245.

⁴⁷ *I.a.*, Grönfors, *Inledning till transporträtten*, 2, ed. Stockholm 1989, p. 102.

⁴⁸ Regarding this practice see, *i.a.*, Gorton, *Transporträtt. En översikt*. 2nd ed. Stockholm 2003 p. 80.

5 Legislation, case law, *lex mercatoria* and contract law

5.1 Some general points

As we have seen, the use of the various words discussed above may lead us into different areas of the law. In some cases and in some countries legislation applies, while in other cases the words' meanings and functions have to be determined on the basis of the law of contract. In some instances the rules that have developed – whether contained in legislation, case law or standard terms – go back to *lex mercatoria* and have evolved into specialised transactions and documents used for trading and financing.

Although many jurisdictions have general contract legislation, this is not the case, for instance, in English law. Specific aspects of English contract law are, however, regulated by statutes such as the Unreasonable Contract Terms Act, the Misrepresentation Act and the Contracts (Rights of Third Parties) Act. All the Nordic countries have more-or-less identical Contracts Acts (with rules on contractual formation, contractual invalidity and authority to enter into contracts), but there is no legislation concerning the interpretation (or construction) of contracts.⁴⁹ In these jurisdictions the principles applied for the interpretation of contracts have developed entirely in case law.⁵⁰

Contract law is the basis for the understanding of most of the undertakings discussed in this article. Thus the law of contract forms an overall framework for many of these instruments. Even where a parti-

⁴⁹ Those acts were introduced in the 1910s and the 1920s. Cf. *Avtalslagen 90 år* (ed. B. Flodgren, L. Gorton, E. Lindell-Frantz & P. Samuelsson), p. 9. We should also mention, however, that much case law has been needed to establish the precise details of contract law, even where the issues are covered by legislation.

⁵⁰ This means that Nordic textbooks on contract law, like English textbooks, contain large sections setting out the principles for the construction and interpretation of contracts. It is worth mentioning that the PICC as well as the PECL contain particular sections on the interpretation of contracts.

cular financial product is regulated by specific legislation or rules or standard forms, the law of contract may also have to be applied in order fully to understand the transaction or document. Accordingly the meaning of a suretyship may have to be construed in accordance with principles derived from the law of contract. Similarly, a letter of credit, although principally regulated by the UCP, like a guarantee regulated by the URDG, may have to be supplemented by applying principles from the law of contract.⁵¹

In the legal area we are dealing with here, the current rules may have rather different roots. In some cases there is specific legislation (sometimes developed out of principles stemming from *lex mercatoria* and later developed into national law as well as into international conventions, which have then been adopted in many national jurisdictions). Thus the bill of exchange has its roots in *lex mercatoria*, but the relevant principles have subsequently been embodied in specific legislation. Later the need for harmonisation resulted in efforts to effect international conventions.

There is thus presently much national legislation on bills of exchange, sometimes based on one of the international conventions, but in some countries none of the international conventions have been adopted. In English law, the Bills of Exchange Act was passed as early as 1909 and is a very comprehensive piece of legislation. With regard to promissory notes, the Nordic countries have their own near-identical statutes, following the adoption of the Swedish Promissory Notes Act in 1936.⁵²

In other cases, as we have seen, specific national rules have developed, e.g., in relation to the traditional suretyship. In some cases, however, (basically where particular trade practices are involved) we can follow

⁵¹ Somewhat haphazardly, we could refer here to the English case *Credit Agricole v. Muslim Bank* /2000/ 1 Lloyd's Rep. 275, where the court used interpretative methods, and to the Swedish case NJA 1983 p. 332, where the Supreme Court applied Section 36 of the Swedish Contracts Act to set aside a provision in a letter of credit.

⁵² It is worth mentioning that the Promissory Notes Act introduced the first general clause allowing a court to modify contractual provisions under certain circumstances. Its wording was narrower than that used in 1976, when the so-called general clause was introduced into the Contracts Act as Article 36.

the evolution of particular sets of international rules.

Some special mention should be made of letters of credit and on-demand guarantees and the surrounding legal frameworks. I have chosen these documents in particular as the relevant legal frameworks have developed differently and over different periods of time.

5.2 Letters of credit

5.2.1 Some general points

Letters of credit have developed within *lex mercatoria* and are subject to specific legislation only in some countries (in the United States, for example, chapter 5 of the Uniform Commercial Code contains rules on letters of credit issued, and used for interstate commerce, within the United States).

There is an enormous volume of English case law in this particular area, as well as much case law in France, Germany and the United States. For much of the 19th and early 20th centuries London was the dominant financial centre and since then English case law has had a particular impact on the development of financial law. The Uniform Custom and Practices (UCP) relating to letters of credit were designed by the International Chamber of Commerce (ICC). The first set of these rules was introduced in 1933. Since then they have been revised on several occasions up to the present UCP 600⁵³. Contracting parties are generally careful to refer to the UCP in order to make them applicable to the particular contractual relationship.⁵⁴

One legal consideration is of particular relevance in the context of letters of credit and on-demand guarantees, and this concerns their independence from the underlying contract. As mentioned already “ordinary” guarantees/suretyships are dependent on the underlying transaction, *i.e.*, if the transaction is invalid then the guarantee will be

⁵³ 1951, 1962, 1973, 1984, 1992 and most recently in 2006.

⁵⁴ It has been suggested that application of the UCP might be regarded as trading practice even if no reference is made.

also. With respect to letters of credit and on-demand guarantees this is not the case, and here the independence of the respective instruments will mean that claims for payment under them are valid even if the underlying transaction is, for various reasons, not.⁵⁵ Here again the close legal proximity of letters of credit, on-demand guarantees and promissory notes is obvious.⁵⁶

There are, however, limits to this rule, which developed in relation to letters of credit. If fraud by the beneficiary can be proven, it may be possible to persuade a court to issue an injunction (not available in all jurisdictions) forbidding payment by the bank under the letter of credit.⁵⁷

There have been similar discussions with respect to on-demand guarantees, for example in English law in *Edward Owen v. Barclays Bank International* and *R.D. Harbottle (Mercantile) Ltd v. National Westminster Bank et al.*⁵⁸ In these cases the English courts established the particular nature of on-demand guarantees. Whether the arguments put forward by the English courts in connection with letters of credit and on-demand guarantees should be based on the same considerations has been discussed by Debattista.⁵⁹

5.2.2 Trading letters of credit.

It would appear that banks, when undertaking to issue a letter of credit,

⁵⁵ See e.g. Gorton, *Rebursrätt* p. 114 *et seq.*

⁵⁶ It is thus important to bear in mind that a letter of credit (as well as an on-demand guarantee for that matter) is based on, but at the same time separate from, the underlying transaction. This means that a letter of credit should be judged in its own right, even though the legal effects of the underlying transaction will persist with respect to the parties to it.

⁵⁷ See Schmitthoff, *International and procedural aspects of letters of credit*, where he also discusses the role of the UCP as trade practice, and Kurkela, p. 120 *et seq.* and 173 *et seq.*

⁵⁸ /1978/ 1 Lloyd's Rep. 166 and /1977/ 2 All E.R. 862 respectively.

⁵⁹ Debattista, *Performance bonds and letters of credit*. Charles Debattista argues that the English courts have developed a reasoning whereby, without good legal foundation, on-demand guarantees have been treated in the same way as letters of credit with respect to the abuse of on-demand guarantees and fraud in connection with letters of credit. In his view, this line of reasoning is not absolutely convincing.

always refer to the UCP. However, the parties to the underlying transaction (often a sales contract) may not always be so careful. Accordingly there may be a conflict between the contract in the underlying transaction (with no reference to the UCP) and the letter of credit (which almost invariably includes such a reference). Could a party to the underlying transaction refuse to accept a letter of credit opened by a bank that referred to the UCP? Probably not, but why is this? Would the argument be that commercial parties should be aware that the UCP is the generally accepted set of rules regulating letters of credit? Would the argument be that the UCP is “commercial usage”? Or that the principles underlying the UCP amount to some kind of general legal principles? On the one hand, we tend to believe that the UCP are not commercial usage (even if they are described as uniform custom and practices) or that they are not, by way of generally accepted principles, accepted as having such a character. As mentioned, one particularly difficult point concerns fraud in, or in connection with, letters of credit. Although the problem initially developed in connection with letters of credit, similar problems have arisen with respect to on-demand guarantees, although the true similarity of the problems has been questioned.⁶⁰

5.2.3 Standby letters of credit

As mentioned above, standby letters of credit (or standby credits) are a particular type of legal instrument that developed out of the trading letter of credit, but with a view to providing the banks with another vehicle to meet a similar need to that filled by on-demand guarantees.⁶¹ Standby credits have a somewhat different history to trading letters of credit, in that they were introduced by US banks as an alternative to bank guarantees, which banks under the then-existing banking legislation were allowed to issue as a separate business undertaking. Today many international banks offer their customers a choice of standby credits or on-demand guarantees, and, as mentioned above, these in-

⁶⁰ See Debattista.

⁶¹ Standby credits have been described by, among many others Bertrams, who refers to ISP 98 and Kurkela.

struments are subject to separate sets of rules.⁶²

Standby credits are also dealt with in the Convention on Independent Guarantees and Stand-by Letters of Credit.

5.3 On-demand guarantees

Compared to the trading letter of credit, on-demand guarantees are a different kettle of fish. Should the on-demand guarantee be regarded as derived from the law of surety or from the law related to promissory notes (or notes of indebtedness)? Or should it be regarded as something else entirely? As mentioned above, the on-demand guarantee has three basic attributes: it is irrevocable, unconditional (independent) and payable on demand.⁶³

Some features of suretyship extend far back into legal history and the concept seems to have developed in national law, rather than in *lex mercatoria*. The general use of suretyships does not indicate a particular relationship with *lex mercatoria*. Should the on-demand guarantee be regarded as a particular form of suretyship/guarantee, in which case a court may have to look for legal “guidance” in the law of contract, the law related to suretyships *etc.*? Undoubtedly the documents have a common ancestry, and the on-demand guarantee might be seen as a particular type of suretyship from which a fundamental attribute has been removed, namely, dependence on the underlying transaction. On the other hand, the on-demand guarantee has developed in a different context. Should it rather be seen as a particular legal animal that has evolved out of either the promissory note or the letter of credit? For practical purposes this does not really matter, but I think the question serves to illustrate how in the financial markets a number of new instruments have developed over the course of time that have slightly different characteristics compared to other instruments.

However, present day guarantees (whether in the form of bank gua-

⁶² ISP 98.

⁶³ Following the principles of the Swedish Contract Act, an offer is binding upon the offeror unless a “subject” of some kind was included in the offer making it subject to the occurrence of certain events.

rantees, demand guarantees *etc.*), seem to be instruments which have developed to satisfy mercantile needs. In this sense some of the guarantees used in today's trades have mercantile features, but it is doubtful whether they can really be described as instruments developed in *lex mercatoria*.

In English law the terms "bond" and "guarantee" seem to be used interchangeably, but it has been suggested that the guarantee and the bond are in fact different legal animals in that the bond is actually independent whereas the guarantee is not.⁶⁴ For a non-specialist in common law, it is difficult to determine whether there really is such a fundamental distinction between the two concepts, but the language used should probably be decisive. The URDG 758 (as for that matter its predecessor the URDG 458) cover "guarantees" even if they are intended to be independent in nature. This is clear from the Introduction to the URDG 758.

In this sense, and provided the above observation is correct, it is natural for the on-demand guarantee covered by the URDG to be regarded as closer to the letter of credit than to the suretyship. There is now a relative similarity between the URDG 758 and the UCP 600 which did not exist between the UCP 500 and the URDG 458. When drafting the URDG 758, the draftsmen also had before them the newly revised UCP 600 and apparently considered the resemblance between the two sets of rules to be useful in practice for the users. This does not necessarily mean, however, that the URDG 758 should be regarded as being more derived from the old *lex mercatoria* than the URDG 458.⁶⁵ In all circumstances, considerations concerning national rules will play an important role.

We should also mention that UNCITRAL, when drafting the Convention on Independent Guarantees, took account of the independent nature of the guarantee and tried to limit the possibility of its abuse to a greater extent than was done in the URDG 458. The solutions chosen

⁶⁴ See for example Dalby, *A performance bond deconstructed*, in *Business Law International*, vol. 11 no. 2, p. 105 *et seq.* The word "bond", however, is also used in a different context as the term for a payment undertaking through bonds traded (Swedish "*obligationer*").

⁶⁵ I am convinced that the URDG 758 cannot currently be regarded as trade usage.

in the Convention in this respect are quite complex and have created some uncertainty regarding how the wording should be applied. This uncertainty has not been received favourably in the market. Accordingly, the general view is that this convention will not be widely adopted.

6 Some concluding remarks

This study has tried to indicate the effect of the use of certain formulations in some specific situations. Most of the phrases are well known to the lawyers and businessmen involved in these transactions and I think that we generally like to believe that we are aware of their legal meanings and effects, at least in the most common situations. This is certainly also true for most court cases, but what has been said above implies that drafting parties should be careful when applying certain words and phrases, since they may be understood in different way than the parties – or at any rate one of them – intended.

The wording used may have different implications in different contexts: some considerations may lead to the application of certain rules, while a slight change of wording may make other rules applicable. In some cases a particular piece of legislation may be decisive, while in other cases particular practices or standard terms may become applicable.

This means, for example, that when the parties agree that there will be an on-demand guarantee, the wording “as for its own debt” should be avoided, since this particular wording will make the guarantee dependent on the underlying transaction. Undoubtedly situations may arise in contractual negotiations where the parties’ promotion of their respective interests results in wording that implies both scenarios. This is what had happened in a case before the Swedish Court of Appeal.⁶⁶ In this case the document contained the wording both of an on-demand guarantee and of a joint and several guarantee. Since the parties ulti-

⁶⁶ The Court of Appeal for Skåne and Blekinge, October 22, 1999.

mately agreed that the instrument should be regarded as an on-demand guarantee, the court did not have to resolve the question.

Let us conclude by referring to the loan agreements for the building of the bridge between Malmö and Copenhagen where the Danish and Swedish governments each had to sign a guarantee *vis-à-vis* the lenders.

The Information Memorandum issued on September 21, 1995 and registered in accordance with English rules states:

“Øresundskonsortiet (established pursuant to a Treaty between the Kingdom of Denmark and the Kingdom of Sweden) Programme for the issuance of debt instruments, guaranteed (to the extent that the issuer is legally liable to pay) by the Kingdom of Denmark and the Kingdom of Sweden.”

The text of the guarantee says in section 2:

“2.1. The Guarantors hereby jointly and severally guarantee to the Holders of the Instruments that if for any reason the Issuer shall fail to pay any Guaranteed Sum when and as the same becomes due and payable the Guarantors shall, within four Business Days of written demand by a Holder upon both Guarantors and the Issuer and stating that such sum was not paid on the due date in respect of an Instrument, unconditionally pay that sum.”

Here the independent nature of the guarantee is quite plain, a fact that is further emphasised in section 2.3:

“The Guarantee shall be unconditional, subject to its express terms, and the Guarantors hereby waive any requirement that a Holder should first make demand (other than the presentation of the relevant Instruments) upon or seek to enforce any claim against the Issuer before seeking to enforce this Guarantee....”

Clearly the intention of the parties (or at any rate one of them) is for this guarantee not to operate as an independent guarantee, but rather as a suretyship, *i.e.*, allowing creditors to turn to the guarantor but only

after having claimed payment initially from the principal debtor. In spite of the other contradictory words used in the guarantee, these words may be sufficient to make it an “ordinary” (simple) suretyship rather than an on-demand guarantee.

I would for my part interpret this guarantee as an on-demand guarantee, but always subject to the limitation of what the issuer is liable to pay. Undoubtedly the wording used reflects negotiations between parties during which the lenders requested an unconditional, on-demand guarantee and the guarantors have not fully accepted this, insisting on a reservation that makes the guarantee *de facto* dependent on what the issuer is liable to pay. This indicates, however, the relative complexity of negotiations involving the choices of wording, expressions and concepts in various contexts.

EU rules of competition and the maritime industry

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1 Introduction

The maritime transport industry held a privileged position in respect of the application of the EU Competition rules namely Articles 101 and 102 of the Treaty on the Functioning of the European Union (TFEU)¹ to its market arrangements and market conduct until 1986 when specific secondary legislation² was adopted to apply Articles 101 and 102 TFEU to this industry.³ That privileged position was held even after 1986 and only recently has the maritime sector been subject to the full force of the EU competition rules.⁴

In the middle of the 1980s the then European Economic Community reinvented itself and replaced the concept of a common market with that of an internal market described to be ‘an area without internal frontiers in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of this Treaty’.⁵ The EU competition legislative measures, that were adopted in the so-called 1986 maritime package of legislative measures, granted privileges to undertakings offering maritime transport services (*i.e.* shipping companies) which were not available to other market operators. Moreover, it was only in the first decade of the twenty-first century, in 2006, that finally the maritime transport industry was deprived of its privileged position. Since 2006 the application of the EU competition rules to the maritime transport industry are the same

¹ Throughout this article the new numbering of the EU competition provisions will be used. The Treaty on the Functioning of the European Union (TFEU) renumbered Articles 81 and 82 EC Treaty as Articles 101 and 102 TFEU.

² Council Regulation 4056/86 OJ [1986] L378/4.

³ Article 101 prohibits agreements between undertakings which are anti-competitive and Article 102 prohibits abusive market conduct by undertakings holding a dominant position in a particular relevant market.

⁴ Council Regulation 1419/2006 OJ [2006] L269/1 repealing Regulation 4056/86.

⁵ Article 26 TFEU.

as for other market operators.⁶

This article seeks to map out the application of the EU competition rules to the maritime industry over a period of almost 50 years by examining some of the European Commission's decisions applying the rules of competition to the maritime transport sector and by considering the relevant case law of the European Court of Justice (the ECJ). The chapter will first, explain how the maritime transport industry was excluded from the operation of the EU competition rules until 1986. Secondly, it will set out and comment on the secondary legislation that was adopted in the mid-1980s in order to apply the EU rules on competition to the maritime transport sector. Thirdly, it will analyse selectively the application of the EU rules on competition to this mode of transport in the following twenty years. In the final part of the article some concluding observations will be set out as to the future relationship between the EU rules on competition and maritime transport arrangements and market conduct.

2 Maritime transport services and the EU competition rules

EU competition policy seeks to ensure that all transport markets operate efficiently and competitively.⁷ Undertakings operate in a globalised market where cooperation and international trade is an integral part of that market. The transport industry facilitates international trade. Thus, it is not surprising that a state's economy is highly dependent on the well functioning

⁶ Regulation 1/2003 OJ 2003 L1/1, which repealed and replaced Regulation 17/62 OJ 1962-65 Sp Ed p.87 on the implementation of Articles 101 and 102 TFEU, now applies to all maritime transport services including cabotage and international tramp vessel services.

⁷ In Case 156/77 *Commission v Belgium* [1978] ECR 1881 the European Court of Justice ruled that the EU competition rules apply to all economic sectors including transport. However, until a specific procedural regulation applying the rules to the maritime sector (Regulation 4056/86) was adopted, there was no procedural means to implement the rules effectively in the market for maritime transport services.

transport industry. The importance of the transport industry to the economy of the Member States cannot be underestimated as the industry is indispensable as an ancillary activity to other industrial sectors.⁸

Furthermore, the transport industry has several distinctive features⁹ which require regulation at national level and has resulted in national public authorities playing a regulatory role in the administration of the transport industry. Thus when the European Economic Community was established it was clear that the transport industry could not automatically be subject to every general rule set out in the EC Treaty. Thus, a separate title was inserted into the EC Treaty setting out the legal basis for the creation of a Common Transport Policy with the objective of liberalising the transport market. In fact, transport policy remained, until the mid-1980s, mainly under the control of the Member States. Various attempts by the European Commission (the Commission) to break the deadlock failed. As far as maritime transport services are concerned the position is aggravated by the fact that the EU Treaty expressly provides that positive action of the EU Council is required before any measure adopted as part of the Common Transport Policy applies to the maritime sector.

The implementation of the EU competition rules to the transport industry underwent various reforms and changes. The first Council Regulation that introduced procedural rules to implement the EU competition rules and thus to regulate undertakings' market conduct was Council Regulation 17 which was adopted in 1962.¹⁰ However, Regulation 141/62¹¹ suspended the application of Regulation 17 to the transport industry¹² until the adoption of Regulation 1017/68 which

⁸ See for further details R Greaves, *EC Transport Law*, 2000 Longman, pp 1-2.

⁹ *Ibid* at p 1.

¹⁰ See note 6 above.

¹¹ EEC: Council Regulation No 141/62 OJ Sp Ed 1959-62 p.291 exempting transport from the application of Council Regulation No 17, but not from the application of Articles 101 and 102 TFEU.

¹² Article 1 specifically provided that Regulation 17 should not be applicable to the transport sector.

applied the competition rules to inland transport.¹³ Only when Regulation 4056/86¹⁴ was adopted did the maritime transport sector come within the generally applicable EU competition law framework.

However, some EU measures were adopted prior to 1986 which had an impact on how maritime services were provided. The 1974 United Nations Code of Conduct for Liner Conferences¹⁵ caused an immediate problem for the EU given that it permitted cargo sharing,¹⁶ a practice clearly anti-competitive and prohibited by Article 101(1) TFEU. In order to assist the Member States to fulfil their international obligations the EU adopted Regulation 954/79¹⁷ to lay down rules for the operation of the Code amongst the Member States. The Regulation provides for a definition of 'national shipping lines' which complies with the rules of the TFEU on the right of establishment. Member States, therefore, cannot discriminate between different vessels operating shipping lines established on their territory. In addition, the Regulation provides for a redistribution, on a commercial basis, of the volume of cargo to which all shipping lines of the Member States participating in the trade are entitled under the Code, irrespective of whether they have status of 'national shipping line' as defined by the Code. Finally the Regulation prohibits the application of certain provisions of the Code, such as the 40:40:20 trade-sharing rule¹⁸ in conference trade, between Member States.

¹³ OJ Sp Ed 1968 I p.302.

¹⁴ See note 2 above.

¹⁵ Liner conference is a group of carriers of cargo on a particular route within geographical limits, and which have an agreement within the framework of which they operate under uniform or common freight rates and other agreed conditions with respect to the provisions of liner services.

¹⁶ The UN Code regulates cargo sharing by providing that the national shipping lines of each contracting state are entitled to a 40% share of the traffic, with 20% available for cross-traders (the 40:40:20 rule).

¹⁷ OJ [1979] L121/1.

¹⁸ See note 16 above.

3 The post-1986 competition legislative measures

The 1986 maritime package of four legislative measures¹⁹ had several objectives including the opening up of the international maritime transport market and the implementation of the EU competition rules in this market. The first measure, Regulation 4055/86,²⁰ sought to open up the maritime transport market by applying the EU principle of freedom to provide services to international maritime transport, that is, transport between Member States and between Member States and third countries.²¹ As far as maritime cabotage services²² were concerned, these were excluded from the scope of Regulation 4055/86 but a few years later, in 1992, a specific regulation was adopted to open up these services to competition.²³ Thus by 1992 the legislative regime to open up the maritime transport services market to competition was complete.

The second measure that was adopted was Regulation 4056/86²⁴ which, as already stated above, applied only to international maritime transport services from or to one or more EU ports (Article 1(2)). The Regulation provided for deregulation, legal certainty, furtherance of EU integration objectives and clarification of the position of maritime transport users. It was a unique, hybrid, EU competition legislative measure which sought to reach a fair balance between shipowners and users. The Regulation not only provided the means for the application of the EU competition rules to the maritime transport sector (*i.e.* proce-

¹⁹ Apart from Regulations 4055/86 and 4056/86 which are considered in this paper, the other 2 regulations in the package were: Regulation 4057/86 OJ [1986] L378/14 on unfair practices of non-EU countries and Regulation 4058/86 OJ [1986] L378/21 laying down rules on coordinated action to safeguard free access to cargoes in ocean trade.

²⁰ OJ [1986] L378/1.

²¹ See note 8 above, R Greaves, *EC Transport Law*, pp 70-71.

²² Coastal shipping services provided within one Member State.

²³ Council Regulation 3577/92 OJ [1992] L364/7.

²⁴ See note 2 above.

dural rules for applying for an individual exemption from the prohibition of Article 101(1) TFEU) but also provided an exception for certain technical agreements (Article 2) and contained a block exemption²⁵ for agreements between users themselves or between users and conferences (Article 6) and for liner conference agreements (Article 5).²⁶

The exemption for agreements between users and conferences, and for the liner conference agreements, was controversial given that these agreements concerned not only conditions and quality of liner services but rates (*i.e.* price-fixing agreements) and, in the case of liner agreements, capacity regulation (*i.e.* market sharing agreements). These are two categories of arrangements which are expressly prohibited in Article 101 TFEU. Thus, Regulation 4056/86 specified detailed provisions as to when the liner conferences themselves could be exempt *en bloc* from the prohibition of Article 101(1) TFEU. The result was that the EU competition rules were applied to the maritime transport industry in a different manner from that applied to other industries. As the block exemption was only available to liner conferences, a further regulation, Commission Regulation 870/95²⁷ was adopted to exempt other types of maritime arrangements such as consortia which became common between liner shipping undertakings. Consortia agreements were entered into between liner conferences that, as a consequence of the development of containerization, began to offer door-to-door transport services combining land with sea transport, or better know now as multimodal transport.

Following the extensive modernisation of the general EU competition law²⁸

²⁵ Block exemption regulations permit agreements which comply with specified conditions and obligations set out in Article 101(3) TFEU to be exempted from the prohibition of Art 101(1) TFEU.

²⁶ See note 15 above.

²⁷ OJ [1995] L89/7. This Regulation has been repealed and replaced by Commission Regulation 906/2009 OJ [2009] L256/31.

²⁸ A more economic approach to how the EU competition policy led the Commission to modernise the existing competition legislative measures.

and enforcement regime,²⁹ the Commission initiated a review of Regulation 4056/86, which included extensive consultations with carriers and transport users. At the end of this exercise the Commission concluded that there was no evidence that the conference system of price agreements had led to efficiencies or stability as to freight rates or shipping services. Thus, the Commission decided that there was no longer a justification in treating the maritime industry in a different manner from other international industries. The result was the adoption of Regulation 1419/2006³⁰ repealing Regulation 4056/86 and bringing maritime transport within the general EU competition law enforcement regime, which had been recently modernized and enforced in accordance with Regulation 1/2003.³¹ A transitional period of two years was granted to liner conferences which met the conditions of the block exemption Regulation on 18 October 2006, the date the new Regulation came into force. Thus the industry had two years to comply with the new circumstances. However, as far as consortium agreements were concerned the Commission decided that a block exemption regulation should continue to regulate these types of agreements and adopted a new measure, namely Regulation 906/2009.³²

It is submitted that even now maritime transport services remain 'special' in the context of the application of EU competition rules. This is demonstrated by the fact that the Commission issued Guidelines on the application of Article 101 TFEU to maritime transport services³³ when the sector lost its privileged status. These Guidelines are intended to help undertakings and associations of undertakings operating these services, mainly if operated to and/or from a port or ports in the Euro-

²⁹ The adoption of Regulation 1/2003 (see note 6 above) replacing Regulation 17/62 abolished the notification procedure that had been operated since 1962 allowing undertakings operating anti-competitive agreements to seek from the Commission an individual exemption from the prohibition of Article 101(1) TFEU. The Regulation also decentralised the enforcement of the EU competition rules by allowing national competition authorities to enforce the whole of Articles 101 and 102 TFEU.

³⁰ See note 4 above.

³¹ See note 6 above.

³² See note 27 above.

³³ OJ [2008] C245/2.

pean Union, to assess whether their agreements are compatible with Article 101 TFEU. The Guidelines set out the principles that the European Commission will follow when defining markets and assessing maritime transport agreements concerning the provision of liner shipping services, cabotage and international tramp services. The Guidelines do not apply to the other modes of transport.

A further consequence of this change in the enforcement of EU competition rules for the maritime industry is that international tramp shipping services and cabotage services are now subject to the operation of Regulation 1/2003. Tramp shipping services involve the carriage of cargo to a designated destination, normally on a charter basis. These services do not generally operate to a fixed regular schedule and the freight rates are freely negotiated. The provisions of Regulation 4056/86 did not apply to these two types of maritime services so there was no regulation conferring the necessary enforcement powers on the European Commission. Indeed, in the absence of such a regulation, national competition authorities and national courts could have enforced the EU competition rules but these powers were never exercised.

4 The application of the EU competition rules to the maritime transport sector 1986-2006

During this period of 20 years the Commission issued about 10 decisions mostly concerning practices of liner conferences,³⁴ some decisions concerning practices adopted by ferry operators³⁵ and, more recently,

³⁴ E.G.: *French-West African Shipowners' Committees* OJ 1992 L 134/1; *CEWAL, COWAC and UKWAL* OJ 1993 L34/20; *TAA*, Decision 94/980 (OJ 1994 L376/1); *FEFC*, Decision 94/985 (OJ 1994 L378/17); *TACA*, Decision 99/243 (OJ 1999 L95/1); *EATA*, Decision 99/485 (OJ 1999 L193/23); *FETTCSA*, Decision 2000/627 (OJ 2000 L268/1); *Revised TACA*, Decision 2003/68 (OJ 2003 L26/53).

³⁵ E.g.: *Greek Ferries* Decision OJ 1999 L109/24; *P&O/Stena* Decision OJ 1999 L163/61.

the first competition decision in respect of ship classification societies.³⁶ This section of the chapter will discuss primarily the first four Commission decisions addressed to liner conferences which were adopted in the early 1990s. All four decisions were appealed to the General Court and a further appeal on law was made to the ECJ in one case.³⁷ The commentary on other Commission Decisions will be briefer and simply highlighting some points of interest.

The very first Commission decision for substantive violation of competition rules was in *French-West African Shipowners' Committees*, adopted in 1992.³⁸ This Decision led to a debate as to what factors the Commission should take into account when applying competition rules to the maritime transport services market, thereby, upholding a balance between preserving competition and promoting maritime transport development. The infringement was brought to the Commission's attention via a complaint under Article 10 of Regulation 4056/86. The issue under consideration related to the practices of the shipping companies which were transporting general cargo between French ports and the ports serving 11 West African and Central African states. In order to carry out these operations, the shipping companies formed groupings, known as 'shipowners' committees'.

The Commission found the shipowners' agreements (albeit they were not identical) had a common purpose. The Commission contended that all agreements secured a 'balanced distribution of trade' between the French and African carriers based on the UN Code of Conduct for Liner Conferences³⁹ and covered all products carried out by the liners.⁴⁰ In addition to these, the agreements included a mecha-

³⁶ OJ 2010 C2/5 for a summary of the Decision.

³⁷ See note 56 below.

³⁸ OJ [1992] L 134/1. It should be noted that prior to this Decision, the Commission had adopted decisions imposing several fines on shipping companies for the supply of incorrect information in response to the Commission's request in *Secretama* (OJ [1991] L35/23) and for failure to submit to investigations in *UKWAL* and *MEWAC* (OJ [1992] L121/45 and OJ [1993] L20/6, respectively).

³⁹ See note 16 above.

⁴⁰ See note 38 above, para.17.

nism to ensure that members of the committees did not exceed the quotas allocated to them, in which case, a repeated infringement would lead to fines.

The parties to the agreement tried to justify their conduct by arguing that they followed the obligations imposed by public authorities. The Commission rejected this argument on the grounds that the UN Code of Conduct was a mere recommendation as to how the conferences should operate and, therefore, it did not advocate or impose on the conferences an obligation to follow the 40:40:20 cargo rule strictly. Furthermore, the Commission also stated that the agreements under consideration were agreements concluded by private undertakings and, therefore, the agreements could not be regarded as a 'public' cartel established as a result of government action.⁴¹

In assessing whether to exempt the agreements, the Commission found that, contrary to Regulation 4056/86, the objectives of the agreements had commercial interests and did not fix common rates and conditions of carriage.⁴² Therefore, the liner conference block exemption regulation did not apply. In carrying out the assessment as to whether an individual exemption under Article 101(3) TFEU could be granted, the Commission found that the agreements did not satisfy the four conditions set out in the Treaty article. Although cargo-sharing arrangements of liner conferences provide regular, adequate and efficient maritime services that take consumers' interests into account, in the present case, the Commission established that cargo-sharing agreements with non-conference lines do not bring the above benefits. In fact, they protect the members of conference from outside competition. Therefore, the members of this liner conference clearly went beyond what was permitted by Article 101(3) TFEU.

In the investigation the Commission also examined whether the conduct of the members of the conference amounted to a violation of Article 102 TFEU. In order for Article 102 TFEU to apply the Commis-

⁴¹ Rosa Greaves 'French-West African Shipowners' Committees' (Case and Comment), EC Competition Rules and Maritime Transport, (1992) LMCLQ 459 at p. 462.

⁴² See note 38 above, paras.44-45.

sion had to demonstrate that the undertakings were in a dominant position in the relevant market and that their conduct was an abuse within the meaning of the EU competition rules. The Commission contended that although some of the members of the shipowners' committees were separate legal entities, they were still connected to each other by being subject to the control of the committees whose function was to ensure that the monthly allocation of cargoes was maintained. This assessment led the Commission to conclude that the participating undertakings held a collective dominant position. In the assessment of the abuse of their dominant position, the Commission concluded that the behaviour of the shipping companies eliminated effective competition from non-committee shipping lines, thereby, violating Article 102 TFEU. The Commission, in particular, claimed that the participating undertakings abused their dominant position by fining members for exceeding allocated quotas through informing the African authorities, and also by co-opting third party shipping lines, the cross traders, on the acceptance of the conditions which protected the national lines.⁴³

The Commission issued a formal Decision under Article 11(1) of Regulation 4056/86 and required the undertakings concerned to end the agreements immediately. The Commission also imposed various fines on the undertakings who participated in the anti-competitive conduct.

Thus, the first Commission decision applying EU competition rules to practices in the maritime transport services market demonstrated that the Commission intended to apply the rules vigorously when conferences went beyond what was permitted under the block exemption Regulation. In other words, the block exemption permitted the members of the conference to fix uniform rates among each other but not with non-conference members.

In the same year, the Commission published another decision, the *CEWAL* Decision,⁴⁴ addressed to several shipping conferences (*CEWAL*,

⁴³ See note 41 above Rosa Greaves 'French-West African Shipowners' Committees' at p.464.

⁴⁴ OJ [1993] L34/20.

COWAC and UKWAL) operating a route between Europe and West and Central Africa. In 1987, the Commission had received complaints⁴⁵ asking for the abolition of arbitrary cargo allocation claimed to exist in trade between West Africa and the EU⁴⁶ and asking the Commission to secure a free access to the trade of non-conference shipping companies, that is, third parties not being members of the shipping conference. The *CEWAL* is linked to the *French-West African Shipowners' Committees* Decision, albeit with certain minor differences. It is of more general application as it is directed against all the activities of the Euro-African shipping conferences.

The Commission found that various loyalty agreements were concluded between the shipping companies which involved various deferred rebates to ensure that independent shipping companies operating outside of the conference were excluded from the conferences' respective areas of activity.⁴⁷ The Commission found that these agreements constituted the violation of Article 101 TFEU as the members of the conferences were involved in trade-sharing agreements with the effect of dividing the market among the conferences' members and excluding the independent companies from operating in the ports in question. This led to the partitioning of the European Atlantic coast into several separate areas. These activities clearly operated in contravention of Article 101 TFEU.

The Commission concluded that the block exemption regulation was not applicable as the agreements were not technical agreements⁴⁸ and they did not have as their objective to fix common or uniform

⁴⁵ The Commission acted on a complaint from the AIWASI (Association of Independent West African Shipping Interests) which is an informal association that represents independent shipping interests in the EU.

⁴⁶ The difference between this complaint and the complaint in the *French West African Shipowners' Committees* Decision lies in the fact the complaint arose in the latter case in relation to the shipping route between France and West and Central Africa; while, in the former investigation, the complaint related to the EU as a whole.

⁴⁷ The conferences' areas of activity stretch from the EU ports (excluding the Mediterranean coast) and the coast of West Africa (from Mauritania to Angola).

⁴⁸ These agreements are exempted under Article 2 of Regulation 4056/86, see note 2 above.

prices between conferences.⁴⁹ The Commission also found that these agreements could not benefit from an individual exemption under Article 101(3) TFEU. This Decision illustrates that the Commission treated the agreements entered into by shipping companies, operating within conferences, just like any other type of harmful horizontal hard-core cartel. The fact that the conferences operated under general rules, block exemption did not prevent a finding that the market-sharing agreements or the agreements that limit the supply of services entered into by the members of the conferences could not be held to infringe the EU competition rules.

As far as Article 102 TFEU is concerned, the Commission concluded that the agreements between the members of the conferences constituted an abuse of collective dominant position within the relevant market. Article 8 of the Regulation 4056/86 makes it clear that nothing in the Regulation affects the application of Article 102 to shipping companies holding a dominant position on a defined market. Interestingly, the Commission noted that although some of CEWAL's activities were authorised by the block exemption, it did not prevent the application of Article 102 TFEU to these same activities.

In assessing whether there was evidence of an abuse of dominant position, the Commission strongly condemned CEWAL's 'creation' of the 'fighting ships'⁵⁰ method directed at the elimination of the competitors. This behaviour constituted an abuse of dominant position with the aim of eliminating a horizontal competitor. The Commission ordered undertakings to end the infringement and imposed fines on them.

The participating companies challenged the Commission's Decision before the General Court and asked for an annulment of the Decision

⁴⁹ *Ibid*, Article 3.

⁵⁰ The term 'fighting ship' is used in maritime law to describe the practice of what is known as 'predatory pricing' in competition law, *i.e.* a vessel belonging to the conferences would sail in competition with the non-conference ship offering lower tariffs. 'Predatory pricing' is heavily condemned in competition law.

entirely or, alternatively, to reduce the fines.⁵¹ The parties contended that there was no infringement of Article 101 TFEU and submitted that the main objective of the shipping conferences was to rationalize maritime transport services; thus the benefits afforded by the system justified certain restriction of competition. They supported their argument by claiming that Article 3 of Regulation 4056/86 granted an exemption for all activities of shipping conferences. The General Court ruled that the exemption from the prohibition of Article 101(1) must be 'strictly interpreted'.⁵² Furthermore, the General Court concluded that in order for the Article 3(c) of Regulation 4056/86 to apply, the practices in question must relate to the coordination or allocation of sailings or calls 'among members of the conference'.⁵³ In this case, however, the practices involved cargo allocation agreements between conferences; therefore, the agreements in question qualified neither for the exemption under Regulation 4056/86 nor for an individual exemption under Article 101(3).⁵⁴ For such reasons, the General Court held that the Commission did not err in finding the violation of Article 101 TFEU.

In relation to the application of Article 102 TFEU, the applicants challenged the Commission's findings and interpretation of the meaning of a collective dominant position. It was argued that a notion of a collective dominant position is applied only in exceptional circumstances, that is, where undertakings collectively abuse their individual dominant positions. However, the most interesting part of the plea was an argument that the application of both Article 101 and 102 TFEU to the same proceedings was inappropriate. The General Court rejected that argument, holding that it is a settled case-law that Article 102 TFEU can be applied to cases in which undertakings possess collective dominant position and abuse it. Although, the General Court pointed

⁵¹ Joined Cases T-24/93 et al, *Compagnie Maritime Belge Transports SA & Others v Commission* [1996] ECR II-201.

⁵² *Ibid* para 48.

⁵³ *Ibid* para.49.

⁵⁴ The grant of the individual exemption under Article 101(3) TFEU was refused because the General Court agreed with the Commission that none of the actual aims of a shipping conference were found to be beneficial.

out that certain links which lead the companies to adopt the same conduct must exist in order for a collective dominant position to be established, such a link had been established by the Commission by the evidence that CEWAL was a liner conference which is 'a group of two or more vessel-operating carriers'.⁵⁵ Thus, the General Court rejected the applicant's arguments and concluded that all the shipping companies did maintain each other within a liner conference and were able to implement common practices which could be regarded as unilateral conduct for the purposes of Article 102 TFEU .

It was, therefore, clearly held by the General Court that the block exemption Regulation should be interpreted strictly, a practice that the Commission had been following since its first decision. This ruling had a significant impact on further decisions as it gave the Commission more confidence in subjecting the activities of the maritime transport sector to scrutiny under the EU competition rules. It also gave the shipping companies an unmistakable message that the EU competition rules applied to their activities.

On appeal to the ECJ ⁵⁶ the main arguments of the parties were focussed on the General Court's confirmation of the violation of Article 102.⁵⁷ It was claimed that the General Court erred in ruling that both Articles 101 and 102 TFEU could be applied to the same market practices. The ECJ confirmed that both Treaty provisions could be applied to the same practices but the Court also stressed that each of the provisions have different objectives.⁵⁸

The ECJ's interpretation of Article 102 was an affirmation of already well established rules which have been applied to other markets. The ECJ confirmed that the General Court had been thorough and correct in assessing whether the three conditions of Article 102 applied to the conduct of these undertakings: namely, whether a dominant position in

⁵⁵ As defined in Article 1(3)(b) of Regulation 4056/86.

⁵⁶ Cases C-395/96 and C-396/96 P, *Compagnie Maritime Belge Transports SA and others v Commission* [2000] ECR I-1365.

⁵⁷ *Ibid*, paras.12-27.

⁵⁸ *Ibid*, para.33.

the relevant market has been established;⁵⁹ whether the conduct under scrutiny was an abuse of that dominance;⁶⁰ and whether the conduct affected trade between Member States. The ECJ confirmed that for collective dominance to be established there must be economic links that enable the undertakings concerned to act together.⁶¹ However, the Court stated that the mere existence of an agreement, decision or concerted practice⁶² does not necessarily show the existence of collective dominance.⁶³ According to the ECJ, it is the *implementation* of such agreements and its nature and terms that may lead to conclude that the undertakings appeared to outsiders as a collective dominant entity.⁶⁴ Although the applicants' submissions were rejected they were not entirely unsuccessful as the ECJ annulled, on procedural grounds the General Court's confirmation of the Commission's fines.⁶⁵ This was a judgment of significance on the interpretation of the concept of collective dominance well beyond the confines of the activities of maritime transport operators.

Interestingly, the *CEWAL* saga did not end on that note. The Commission, following the annulment of fines by the ECJ, issued another decision⁶⁶ imposing new fines on CEWAL based on the infringement of Article 102 TFEU. CEWAL appealed to the General Court,⁶⁷ arguing, *inter alia*, that the Commission violated the established principle to act within a reasonable period of time after the ECJ's judgment. The General Court, however, dismissed CEWAL pleas altogether ordering it to bear the costs of the proceedings.

The next two Commission decisions adopted in the early 1990s are

⁵⁹ If there is more than one undertaking that could hold and exploit a dominant position collectively.

⁶⁰ See note 56 above, para.40.

⁶¹ *Ibid*, para.42.

⁶² One of the elements of Article 101(1) TFEU.

⁶³ See note 56 above, para.43.

⁶⁴ *Ibid*, para.45.

⁶⁵ *Ibid*, para.146.

⁶⁶ *Compagnie Maritime Belge* OJ [2005] L 171/28.

⁶⁷ Case T-276/04, *Compagnie Maritime Belge SA v Commission* [2008] ECR-II 1277.

the *Trans-Atlantic Agreement (TAA)*⁶⁸ and the *Far Eastern Freight Conference (FEFC)*.⁶⁹ In both cases the Commission was faced with new developments in the maritime transport industry, namely the multimodal approach to carrying freight. In both Decisions, the Commission concluded that the agreements did not relate to the operation of liner conferences but concerned discussion on prices, conditions of carriage and capacity in both maritime and inland transport sectors. These were not agreements solely concerned with the provision of maritime transport services and, therefore, the maritime block exemption Regulation was not applicable to the agreements.

In the *TAA*⁷⁰, the Commission found that there were price-fixing agreements in the maritime and inland haulage sectors. As far as the agreements concerned the maritime sector, the Commission found also that non-utilization agreements had as their object or effect the restriction of competition which allowed the members of the TAA to restrict substantially the competitive capacity of each one of them vis-à-vis the others by limiting the volume that each one offers to the market.⁷¹ As far as the agreements concerned the inland sector, the Commission applied the regulation implementing the EU competition rules to inland transport⁷² and found that fixing the price rates and conditions of the inland transport services violated Article 101(1).⁷³

The Commission stated that the maritime block exemption is applicable only if the agreement in question is a liner conference agreement which operates ‘under uniform or common freights rates.’⁷⁴ The TAA, on the contrary, was found to be an agreement between a conference and outsiders wishing to maintain price flexibility.⁷⁵ In such a situation,

⁶⁸ OJ [1994] L 376/1

⁶⁹ OJ [1994] L378/17.

⁷⁰ See note 68 above.

⁷¹ *Ibid*, para.298.

⁷² Article 2 of Regulation 1017/68 p.302 repeats the restrictions of Article 101(1) TFEU for inland sector, see note 13 above.

⁷³ See note 68 above, para.313.

⁷⁴ *Ibid*, para.320.

⁷⁵ *Ibid*, para.343.

the possibility for external competition is significantly reduced. The TAA, therefore, resembles generic ‘price fixing’ agreement under EU competition law in which case the agreement cannot benefit from the block exemption.

In relation to the price fixing of inland haulage, the Commission concluded that Regulation 4056/86 in no way authorised liner conferences to permit their members to fix inland rates collectively.⁷⁶ In other words, the block exemption was to be interpreted narrowly as only applying to maritime rates. Moreover, the Commission also rejected the application of Article 101(3) arguing that none of the criteria set out therein was satisfied.⁷⁷

A striking feature of the TAA was the fact that the Commission, having established that the agreement deviated from the conventional definition of ‘liner conferences,’ proceeded to evaluate the agreement as a simple price-fixing agreement which is considered to be a hard-core violation of competition rules.⁷⁸ Another interesting issue raised in the TAA was the fact that it also involved inland price-fixing which the Commission held not to be within the scope of Regulation 4056/86.

The reasoning in the TAA links well with the next Commission decision which also included an agreement in inland price-fixing. In *Far Eastern Freight Conference*⁷⁹ (FEFC), the agreement related only to the inland transport services as a part of multimodal transport operation for the carriage of containerized cargo. The Commission found that these activities amounted to price-fixing in the inland transport services and they infringed Article 101(1) TFEU. The FEFC argued that these activities were exempted by Article 3 of Regulation 4056/86. As was already seen in the TAA Decision, the Commission rejected the submission that Regulation 4056/86 applied to inland transport services. The Commission, therefore, assessed whether the agreement could benefit

⁷⁶ *Ibid*, para.372.

⁷⁷ *Ibid*, paras 383-491.

⁷⁸ In such cases, when hard-core violation is found, no individual exemption under Article 101(3) TFEU is available.

⁷⁹ See note 69 above.

from an individual exemption under Article 101(3) and concluded that the FEFC did not meet the conditions for exemption. Although the development of multimodal transport may improve transport services, collective price-fixing for carrier haulage services did not. This Decision confirmed that the Commission considers maritime and inland transport services separate when applying EU competition rules.

The TAA and the FEFC sought judicial review from the General Court arguing, *inter alia*, against the Commission's interpretation of both the Regulation 4056/86 and Article 101(3) TFEU in relation to inland price-fixing. In the TAA judgment⁸⁰ the General Court concluded that Article 3 of Regulation 4056/86 applies only to the liner conferences and the TAA was not one for the purposes of the said regulation.⁸¹ Furthermore, the dismissal of this plea made it unnecessary to determine whether the capacity management programme and inland price-fixing would have been covered by the block exemption had the TAA satisfied the conditions to be regarded as a liner conference.⁸² This part of the ruling states that even if the TAA were a liner conference, the inland price-fixing would still not be exempted under Regulation 4056/86.

The General Court held that the block exemption Regulation must be strictly interpreted,⁸³ that is it 'cannot be interpreted broadly and progressively so as to cover all the agreements which shipping companies deem it useful, or even necessary, to adopt in order to adapt to market conditions'.⁸⁴ The General Court also made an interesting comment in relation to the interpretation of a 'liner conference'. It was noted that a liner conference enjoys an exemption from the EU competition rules only due to its stabilising effects in which case 'all the members of the conference [must] adopt uniform freight rates rather

⁸⁰ Case T-395/94, *Atlantic Container Line and others v Commission* (2002) ECR II-875.

⁸¹ *Ibid*, para.177.

⁸² *Ibid*, para.178.

⁸³ Citing Joined Cases T-24/93, *Compagnie Maritime Belge Transports SA v Commission*, see note 51 above.

⁸⁴ See note 80 above para.146.

than if there are several rates according to the members concerned'.⁸⁵ Thus horizontal price-fixing agreements are covered by the block exemption and it is acceptable for the internal competition among members of the conference to be eliminated. In this situation it is the external competition from non-conference shipping companies which is of the crucial importance.⁸⁶

In the *FEFC* case⁸⁷, the General Court once again rejected the argument that fixing rates for inland transport services fell within the scope of Regulation 4056/86. The General Court held⁸⁸ that the inland transport services are a separate market from maritime services even though they are part of intermodal transport between northern Europe and the Far East.⁸⁹

The General Court then repeated that Regulation 4056/86 is limited only 'to maritime transport services [...], that is, to transport by sea from port to port, and does not cover the inland on- or off-carriage of cargo supplied in combination with other services as part of an intermodal transport operation'.⁹⁰ It is submitted that this judgment ended all future ambiguities in relation to the scope of Regulation 4056/86. Although the applicant was not successful, the General Court did annul the symbolic fines imposed on the FEFC because no fines had been imposed on the TAA for the same kind of infringement.

After this period of intensive investigation by the Commission of agreements which covered both the inland and the sea leg of the journey, it is not surprising that a block exemption regulation for consortia was adopted in 1995 enabling a number of agreements to be exempted from

⁸⁵ *Ibid*, para.158.

⁸⁶ *Ibid*, para.162.

⁸⁷ Case T-86/95, *Compagnie Generale Maritime and others v Commission* [2002] ECR II-1011.

⁸⁸ *Ibid*, para.130.

⁸⁹ The Commission has always been keen to define the relevant market very narrowly, e.g: Case 27/76, *United Brands v Commission* [1978] ECR 207; Case 22/78, *Hugin v Commission* [1979] ECR 1869; Case C-53/92P, *Hilti AG v Commission* [1994] ECR I-667.

⁹⁰ See note 87 above, para.241.

the prohibition of Article 101(1) TFEU.⁹¹ Thus, in the second half of the 1990s, the Commission was once again able to focus on the practices of shipping companies and liner conferences in respect of the maritime leg of their operations.

The maritime transport services market is rather limited as to the number of active players operating in the market and, therefore, it is not surprising that the same shipping companies or liner conferences are investigated more than once. The next Commission decisions to be examined are a good example. In *Far East Trade Tariff Charges and Surcharges Agreement (FETTCSA)*⁹² the parties were all members of the FEFC and the shipping companies involved in the FETTCSA were the same as the ones in the EATA Decision⁹³ which is discussed below. In FETTCSA, the Commission had to consider an agreement relating to charges additional to the basic ocean freight. The members of the FEFC, being a liner conference, were allowed to agree on the level of surcharges and charges; however, this Decision relates to the charges of the non-conference lines of the FEFC.

In the *FETTCSA*, the parties negotiated ways in which they could align their commercial behaviour in relation to the charges and surcharges. These negotiations led to an agreement not to provide discounts from published tariffs for charges and surcharges. The Commission found that it resulted in difficulties for other shipping lines to compete effectively with regard to final price charged to shippers.⁹⁴ This was considered to be severe restrictions of price competition which is a violation of Article 101(1) TFEU.

The undertakings argued that the FETTCSA was a 'technical agreement' for the purposes of Article 2 of the Regulation 4056/86 which contained a list of agreements that were excluded from Article 101(1) if

⁹¹ In 1996 alone the Commission allowed five consortium agreements to be exempted under the consortia block exemption Regulation after the deletion of some anti-competitive clauses which were not indispensable to the effectiveness of the agreements.

⁹² OJ [2000] L268/1.

⁹³ OJ [1999] L193/23.

⁹⁴ See note 92 above, para.134.

their ‘sole object or effect is to achieve technical improvements or cooperation’. The Commission, however, interpreted Article 2(1) of the Regulation 4056/86 narrowly as meaning that even in cases when the parties can prove that their agreement is a ‘technical agreement,’ such agreements will not fall within the scope of Article 2(1) if they restrict competition. This is so because the exemption must be regarded as ‘merely declaratory: it lists a number of different kinds of agreement which do not fall within the scope of Article [101(1) TFEU] when their sole object and effect is to achieve technical improvements or technical cooperation.’⁹⁵ The Commission concluded that the FETTCSA was not a technical agreement⁹⁶ and, therefore, did not have to apply the interpretation it had given to Article 2(1).

The Commission also rejected the argument that the FETTCSA was a liner conference for the purposes of the Regulation 4056/86; thereby, rejecting the possibility of an automatic exemption.⁹⁷ Finally, the Commission stated that the FETTCSA did not meet the conditions for an individual exemption under Article 101(3) to be granted.⁹⁸

In this case, the Commission had to deal with a simple agreement which was aimed at restricting competition. In fact, it has been stated that ‘the FETTCSA case shows that the Commission will act firmly when conference and non-conference shipping lines conspire together as a cartel’.⁹⁹

The parties to the *FETTCSA* sought judicial review from the General Court asking for an annulment of the Commission Decision.¹⁰⁰ The General Court confirmed the Commission’s findings of infringement of Article 101 TFEU. However, the General Court annulled the fines in their entirety on the grounds that the Commission imposed fines after

⁹⁵ *Ibid*, para.146.

⁹⁶ *Ibid*, para.151.

⁹⁷ *Ibid*, para.162.

⁹⁸ *Ibid*, paras.170-174.

⁹⁹ *FETTCSA: Commission fines shipping lines for an illegal price agreement on the Europe/Far East Trade*. IP/00/486.

¹⁰⁰ *Case T-213/00, CMA CGM and others v Commission* [2003] ECR II-913.

the five-year limitation period set out in Regulation 2988/77¹⁰¹ had expired. It should be noted, however, that the General Court did not overrule the Commission's interpretation of Article 2(1) of the Regulation 4056/86; thereby, suggesting the Court agreed with the 'declaratory' nature of the provision.

The next Commission Decision, the *Trans-Atlantic Conference Agreement* (TACA)¹⁰², took several years to reach a conclusion. The members of the TACA were all former members of the TAA, the conference agreement which was subjected to the Commission's investigation and proceedings.¹⁰³

In 1994, the TACA was notified to the Commission under Regulation 4056/86. The Commission informed the parties that it would also apply the inland transport competition regulation, as some parts of the activities related to inland transport services. The Commission, after investigating the agreement, issued a decision removing the immunity from fines for TACA's inland price fixing activities. The parties then applied to the General Court for judicial review which was dismissed as the inland transport competition regulation did not provide for immunity from fines; therefore, the appeal was held to be inadmissible.¹⁰⁴ Prior to this decision, the Commission had issued several Statements of Objections during a period of two years. The Commission opposed, *inter alia*, the collective price-fixing of tariffs for the inland leg of multimodal transport operation. The Commission was faced with two main issues when dealing with the TACA: first, the interpretation of the scope of Regulation 4056/86; and, secondly, the conference's attempts 'to restrict the availability to shippers of individual and confidential service contracts.'¹⁰⁵

¹⁰¹ OJ [1977] L319/1.

¹⁰² OJ [1999] L95/1.

¹⁰³ See note 68 above. After the General Court refused to annul the Commission Decision in the TAA case (See note 80 above), the TAA parties and the Commission engaged in the negotiations leading to the replacement of the TAA by the TACA.

¹⁰⁴ Case T-18/97, *Atlantic Container Line and others v Commission* [2002] ECR II-1125.

¹⁰⁵ See, 'Competition in the maritime transport sector: a new era' Jean-Francois Pons and Eric Fitzgerald, Competition Policy Newsletter 2002/1 at p.10.

The members of the TACA argued that they qualified for an automatic exemption under Regulation 4056/86, or, alternatively, for an individual exemption under Article 101(3) TFEU. The Commission found that the TACA infringed Article 101(1) because the TACA contained a price agreement in both maritime and inland transport services sectors as a part of multimodal transport operations for the carriage of containerised cargo.¹⁰⁶ In addition, there was a further restriction since members of the TACA had agreed terms and conditions under which they would enter into service contracts with shippers.¹⁰⁷

The Commission focused on the service contracts between the conference and shippers and concluded that individual service contracts to which only one carrier is a party, and where the negotiation of the contract terms and conditions is permitted without intervention from the members of the conference, do not violate Article 101(1) TFEU.¹⁰⁸ However, if the members of the conference entered into joint service contracts and agreed individually not to enter into a service contract with that shipper, then these agreements were likely to be caught by the prohibition of Article 101(1) TFEU.¹⁰⁹ The Commission concluded that the TACA was an example of the latter kind of joint service contract and; therefore, concluded that the agreement was contrary to Article 101(1) TFEU.

It was further argued that joint service contracts of this kind are traditional conference practices; therefore, they should be implicitly exempted by Regulation 4056/86.¹¹⁰ The Commission rejected that argument stating that service contract prices are not tariff rates under the conventional liner conference's practices; therefore, they are not covered by the block exemption.¹¹¹ The reason being that the service contracts include the price which is agreed upon by two or more members of a

¹⁰⁶ See note 102 above, para.399.

¹⁰⁷ *Ibid*, para.379.

¹⁰⁸ *Ibid*, para.443.

¹⁰⁹ *Ibid*.

¹¹⁰ *Ibid*, para.451.

¹¹¹ *Ibid*, para 453.

conference; while, the uniform tariff is a conference price which is uniform for both the members of the conference and all the shippers of the same commodity.¹¹²

The Commission also subjected the TACA to Article 102 TFEU scrutiny. The Commission concluded that the members of TACA had collective dominant position due to economic links between the TACA members, *e.g.* tariffs and extensive enforcement provisions.¹¹³ The abuse of the dominant position took place when the parties to the TACA agreed to impose restrictions on the contents of the service contracts; thereby, preventing price competition (the first abuse).¹¹⁴

The Commission also found that elimination of potential competition was also an abuse of dominant position.¹¹⁵ This proposition was supported by Regulation 4056/86 itself where the existence of competing non-conference services, and the possibility for future potential competitors entering the market, were among the justifications for granting the block exemption.¹¹⁶ However, in relation to TACA's conduct, the Commission found that its very aim was to ensure that 'if a potential competitor wished to enter the market it would only do after it had become a party of the TACA' (the second abuse).¹¹⁷ This could lead to the changes to the competitive structure of the market and to strengthening the collective dominant position of the TACA members.

The Commission, eventually, decided not to impose fines for the violation of Article 101(1) but it imposed a large fine for breach of Article 102 TFEU. The TACA members applied to the General Court for judicial review of the Commission Decision.¹¹⁸ In terms of violation of Article 101, the General Court confirmed that contract service agreements were not agreements for the purposes of Article 3 of Regulation 4056/86

¹¹² *Ibid*, para.456.

¹¹³ *Ibid*, paras.525-531.

¹¹⁴ *Ibid*, para.551.

¹¹⁵ *Ibid*, para.560 citing Case 6/72, *Europemballage Corporation and Continental Can Company Inc v Commission* [1973] ECR 215.

¹¹⁶ *Ibid*, para.561.

¹¹⁷ *Ibid*, para.562.

¹¹⁸ Cases T-191/98, *Atlantic Container Line v Commission* [2003] ECR II-3275.

which required ‘uniform and common freight rates’ for the exemption to be triggered¹¹⁹ since the rates which were fixed in service contracts were not the same for all shippers.

The General Court also upheld the Commission’s findings in relation to the violation of Article 102, albeit, in terms of the first abuse only. The General Court confirmed the Commission’s finding of collective dominant position based on the facts that, *inter alia*, the parties had high market shares, were able to discriminate on prices, and the absence of effective external competition.¹²⁰

However, the Commission’s findings in relation to the second abuse were annulled by the General Court which led to the removal of fines. The argument of the second abuse was evolving around two members of the TACA¹²¹ who, as argued by the Commission, were induced to join the conference. The General Court held that the Commission failed to demonstrate to the requisite legal standard that the TACA members did in fact induce the companies to join the conference.¹²²

In dealing with the fines, the General Court held that the fines imposed for the first abuse should be annulled as they were covered by Article 19(4) of the Regulation 4056/86.¹²³ In other words, the General Court interpreted this legal provision as granting immunity from fines for violation of both Articles 101 and 102 TFEU.¹²⁴ Therefore, the General Court ordered the Commission to remove the fines imposed on the first abuse as the activities of the first abuse were notified by the TACA to the Commission.

The General Court also ordered the Commission to annul fines in relation to practices falling under the inland competition regulation,

¹¹⁹ *Ibid*, para.1382.

¹²⁰ *Ibid*, paras.1085, 1128-1159. The General Court however annulled the Commission’s findings in relation to the exchange of information in individual service contracts as the information exchanged was already published in the United States,

¹²¹ Hanjin and Hyundai who joined the conference from 1994-1995.

¹²² See note 118 above, para.1368.

¹²³ It provides that the fines imposed by this legal provision should not apply to activities that are taking place after the notification to the Commission and before the Commission issued a Decision in relation to Article 101(3).

¹²⁴ See note 118, para.1443.

i.e. the inland price-fixing. The General Court held that the TACA members deserved the annulment of fines due to the mitigating circumstances, *e.g.* at the time of the investigation and the subsequent procedure the TACA parties were thinking that by notifying the agreement to the Commission, they would be protected from the fines.¹²⁵

It has been argued that the Commission's first Decision in the TACA and the General Court's ruling had significantly affected the relationship between maritime law and competition law as it is today. In 1999, the remaining members of the TACA notified the Commission of the amended version of the agreement. It was argued that this event took place because the shipping conferences decided to abandon their normal practice and took the Commission's main concerns into account.¹²⁶

The notified agreement related to both inland and maritime practices. In August 1999, the Commission cleared the inland part of the agreement; while, the maritime activities raised concerns. The Commission stated that the Revised TACA¹²⁷ removed one of the Commission's main concerns, among other things, in relation to the individual service contracts between the members of the conference and the outside shippers. The Revised TACA removed that restriction from the agreement allowing the conference members to enter into individual service contracts with shippers.

Furthermore, the parties to the Revised TACA undertook various commitments, *e.g.* to restrict the information exchange especially in relation to the commercially sensitive information in service contracts. This led the Commission to conclude that the Revised TACA relating to individual service contracts would not lead to an appreciable restriction of competition.¹²⁸ In addition, the Commission interpreted Article 3 of the Regulation 4056/86 by concluding that the fact that the Revised

¹²⁵ See note 118 above, para.1624.

¹²⁶ Maria Jaspers 'The TACA judgment: lessons learnt and the way forward', Competition Policy Newsletter 2004/1, at p.37.

¹²⁷ Case COMP/37.396/D2—Revised TACA, OJ [2003] L26/53, para. 64.

¹²⁸ *Ibid*, para.72.

TACA members are also permitted to enter into service contracts does not preclude Article 3 to exempt the tariff of a liner conference.¹²⁹

The maritime industry and EU competition lawyers waited for a long time for this Decision. It was argued that the Revised TACA should be seen as ‘the concrete outcome of discussions between the Commission and carriers on the application of existing application’.¹³⁰ This happened due to the fact that after a series of the Commission’s investigations and subsequent procedures, the Commission decided to reach a consensus on the future relationship between maritime industry and competition law. It has been argued that the Commission’s main concern was to allow the members of the conference to enter into confidential individual contracts with shippers,¹³¹ an issue the Commission accurately discussed in the Revised TACA Decision.

The next Commission decision concerned the *Europe Asia Trade Agreement* (EATA)¹³² where the Commission concluded that an agreement not to use capacity and to exchange information violated Article 101(1) TFEU.¹³³ Also, it was found that the agreement did not satisfy the conditions set out in Article 101(3) TFEU. The Commission established that Article 101(1) was violated by ‘artificially limiting the liner shipping capacity’.¹³⁴ In applying the principles of exemption, the Commission pointed out that the EATA does not fall within the conventional definition of liner conferences; therefore, the benefits of the Regulation 4056/86 were not applicable.

In applying Article 101(3), the Commission held that the members of the EATA did not satisfy the first condition¹³⁵ because they failed to justify in what way the information exchange contributed to technical

¹²⁹ *Ibid*, para.80.

¹³⁰ Jean-Francois Pons & Eric Fitzgerald ‘Competition in the maritime sector: a new era’, Competition Policy Newsletter 2002/1, at p.12.

¹³¹ *Ibid*, p.11.

¹³² See note 93 above.

¹³³ *Ibid*, para.176.

¹³⁴ See note 93 above, para. 150.

¹³⁵ ‘Improvement of production or distribution or promotion of technical or economic progress’.

or economic progress of maritime transport services.¹³⁶ The Commission also concluded that the EATA did not meet the second condition¹³⁷ given that the capacity non-utilisation agreement and information exchange¹³⁸ did not bring any fair share of benefits to the consumers. The third condition¹³⁹ was also not met since the Commission did not accept an argument that an agreement between conference and non-conference shipping lines is less restrictive of competition than a conference agreement. The Commission stressed that a non-conference agreement may lead to a strengthening of market power of conference member; therefore, inducing the non-conference members to join the agreement.

Mainly, the Commission stressed the importance of the consumer choice in such scenarios.¹⁴⁰ According to the Commission, consumer choice has a fundamental role in ensuring that a market operates efficiently. The EATA, on the contrary, led to the prevention of efficient division of market shares between conference and non-conference members; thereby, depriving the consumers of the choice. Lastly, the Commission stated that in relation to the fourth condition,¹⁴¹ the parties failed to satisfy it as its non-utilisation of capacity agreement was aiming at prices by reducing the supply of transport services to the market. For such reasons, the Commission concluded that the members of the conference fell within Article 101(1) and failed to satisfy the conditions for an exemption under Article 101(3).

The above Commission Decisions and Court judgments concerned primarily the activities of members of conferences. During the period under consideration the Commission also investigated on several occasions practices of non-conference shipowners which raised concerns

¹³⁶ See note 93 above, paras.104-142.

¹³⁷ 'Fair share of resulting benefits' to consumers.

¹³⁸ Their purpose was to bring about an increase in freight rates with no corresponding increase in service quality"

¹³⁹ "The restrictions should not be indispensable to the attainment of the objectives pursued by an agreement in question'.

¹⁴⁰ See note 93 above, para.226.

¹⁴¹ 'Elimination of competition for a substantial part of the services'.

as to their compatibility with EU competition rules.¹⁴² By way of example two decisions concerning ferry operators will be considered briefly below.

In *Greek Ferries*,¹⁴³ the Commission fined ferry operators for fixing ferry prices. The Commission found the violation of Article 101(1) for roll-on roll off price cartel in ferry services between Greece and Italy.¹⁴⁴ The undertakings applied to General Court for judicial review of the Commission Decision.¹⁴⁵ The General Court upheld the Commission decision concluding that the application had to be dismissed entirely as the Commission did establish to the requisite standard that the undertaking participated in a price cartel.¹⁴⁶

In *P&O Stena Line*,¹⁴⁷ the parties formed a joint venture to provide cross channel ferry services. The Commission held that the formation of a joint venture between actual competitors was in breach of Article 101(1).¹⁴⁸ However, the agreement fell within the individual exemption under Article 101(3) as the Commission found that it satisfied all the conditions set out therein. The Commission had difficulty in assessing whether the fourth condition of the individual exemption was satisfied. Although, it was then concluded that characteristics of the market would lead the companies to compete rather than act in parallel to raise prices.¹⁴⁹ Therefore, the exemption was granted for 3 years from the date of implementation of agreement.¹⁵⁰

In both cases neither the *Greek Ferries* nor the *P&O Stena Lines* were

¹⁴² For a recent example: the Commission opened formal investigations in relation to the 'Baltic Max Feeder' scheme for European feeder vessel owners (IP/10/21), 15 January 2010.

¹⁴³ OJ [1999] L109/24

¹⁴⁴ *Ibid*, paras.140-144.

¹⁴⁵ Cases T-56/99, *Marlines v Commission* [2003] ECR II-5225.

¹⁴⁶ *Ibid*, paras.63-65. Further upheld by the ECJ based on the appeal against the General Court's judgement in Case C-112/04 P *Marlines v Commission*, 15 September 2005 (unpublished).

¹⁴⁷ OJ [1999] L163/61.

¹⁴⁸ *Ibid*, para.39.

¹⁴⁹ *Ibid*, para.127.

¹⁵⁰ *Ibid*, para.130.

operating within a liner conference agreement but nevertheless their conduct was subject to scrutiny of the EU competition rules. In the *Greek Ferries* the Commission concluded that this was a price fixing cartel whilst in the *P&O Stena Line* the Commission found the arrangement to be a beneficial joint venture.

The final decision to note in this survey is the Decision¹⁵¹ that the Commission took in respect of the practices of ship classification societies.¹⁵² This decision makes legally binding commitments¹⁵³ offered by the International Association of Classification Societies (IACS). The commitments address the Commission's concerns that IACS may have infringed Article 101(1) TFEU by pursuing anticompetitive business practices. These practices concerned rules preventing non-members of IACS from joining IACS, from participating in IACS's technical working groups and from having access to background documentation which was necessary in order to apply IACS technical resolutions. The comprehensive commitments offered by IACS, and accepted by the Commission, remedied this situation by establishing an objective and transparent qualitative criteria for membership, by providing for the possibility for non-IACS classification societies to participate in the working groups, and by granting full access to IACS technical resolutions and related background documents.

This was the first competition decision affecting the ship classification market and important activity concerning the maritime transport

¹⁵¹ n 36 above. See press release IP/09/1513, 14.10.2009.

¹⁵² Classification societies are organisations that develop and apply technical standards to the design, construction and assessment of ships (and other marine facilities) and which carry out survey work on ships. Flag states can authorise classification societies for the inspection and statutory certification of their ships.

¹⁵³ Commitments are available under article 9(1) of Regulation 1/2003. These are binding promises which if broken enable the Commission to impose a fine up to 10% of IACS' total turnover without having to prove any violation of Article 101(1) TFEU.

market. It was a significant step in the opening up of this market¹⁵⁴ with the objective of lowering prices, increasing innovation and customer choice as well as improving the quality of the service. These are all core objectives of the EU competition regime.

5 Concluding observations

Although EU competition rules were applied to the maritime transport services sector rather late in the development of EU competition law and policy, the Commission decisions and judgments from the European courts have contributed to the understanding and scope of EU competition rules and, significantly, to the development of the concept of collective dominance in Article 102 TFEU.

As far as secondary legislation is concerned, the various investigations of the practices of the members of liner conferences illustrate the narrowness of the liner conference block exemption Regulation. These decisions and judgments reinforced the fact that block exemption regulations are a sort of legislative derogation from the prohibition of Article 101(1) TFEU and must be interpreted narrowly. Any evidence of conduct not expressly exempted was considered outside the block exemption Regulation and had to be tested in accordance with the general rules of Article 101 TFEU.

These decisions and rulings also demonstrate that neither the Commission nor the courts were ready to follow blindly the principle that maritime deserves a ‘special treatment’; thereby, allowing the shipping companies to violate EU competition law. As was highlighted above, both the Commission and the courts were trying to uphold a balance

¹⁵⁴ In 2009 the EU also adopted secondary legislation to regulate this market. In April 2009 Regulation 391/2009, OJ [2009] L131/11 on common rules and standards for ship inspections and survey organisations and Directive 2009/15, OJ [2009] L131/47 on common rules and standards for ship inspections and survey organisations and for the relevant activities of maritime administrations were adopted. These legislative measures recasted Directive 94/57, OJ [1994] L319/20.

between the permitted conduct and conduct which amounted to hard-core violations of competition rules. However, it has been demonstrated that there was a thin line between permitted conduct and breach of competition law and policy in the maritime sector. The decisions and cases discussed above show that in majority of cases, some shipping companies were crossing that line; thereby, being subjected to heavy fines and prohibition orders. This could lead to two possible conclusions that either the shipping companies were not aware of the scope of the block exemption Regulation, or that the liner conference block exemption Regulation was simply not fulfilling its intended purpose. The former can be illustrated by the repeated conclusion that a multimodal agreement was not to be considered solely under the maritime competition Regulation. Thus such operators needed to fulfil the conditions of two separate, though similar, competition law regimes: one for inland transport, the other for maritime transport.

As for the Regulation not fulfilling its intended purpose, it is true that this legislative measure was criticised from its adoption as not reflecting the maritime transport market at the time when multimodal carriage agreements were already becoming more popular. Nevertheless, the adoption of the 1986 maritime transport package was an achievement in itself, given the resistance that had existed to any EU law intervention in the maritime transport services industry. It was the internal market project as a whole and the enthusiasm for opening up all markets to competition which made it inevitable that the maritime sector would have to be treated like any other economic activity.

The decisions reviewed above also indicate that the Commission was concerned to ensure all aspects of the maritime transport services market remained competitive. The Commission has investigated not only the practices of liner conferences but also those of ferry operators and classification societies.

Now, 50 years later, the maturity of the EU competition law regime has been achieved to a great extent. The rules are implemented not just by the European Commission as a centralised competition authority but also by the national competition authorities. Under these circum-

tances, it would have been difficult to defend a separate EU competition law regime for the maritime transport services market. It has been demonstrated in the Commission decisions, discussed above, that the rules are applied consistently and there is recourse to judicial review by the European Courts. It will be a matter of time, no doubt, for all block exemption regulations to be a matter of history. Thus, even consortia agreements, may not have their privileged position for much longer.

Access to resources on the Norwegian continental shelf

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I Jurisdiction

This article deals primarily with the production licence, which is the main instrument for providing access to the petroleum resources on the Norwegian continental shelf (NCS). But before discussing this licence, and the licensing system in general, we will provide a preliminary overview of jurisdiction on the NCS. First, we will explain the basis in international law for Norway's jurisdiction over its natural resources on the NCS. This jurisdiction is regulated by the Law of the Sea Convention. Second, we will consider the implications of Norway's membership of the EEA Agreement, which is also significant from a resource management perspective. Several provisions in national legislation concerning access to resources represent the implementation of the EEA Agreement.

1 International law – the Law of the Sea Convention

Pursuant to Article 77 (1) of the Law of the Sea Convention (UNCLOS), the coastal State exercises over the continental shelf sovereign rights for the purpose of exploring it and exploiting its natural resources.¹ This is the basis in international law for Norway's jurisdiction over the petroleum resources on the NCS. Unlike the general jurisdiction exercised over Norway's land territory, jurisdiction over the NCS is limited. The limitation is functional in nature, *cf.* “for the purpose of...”. In other words, the jurisdiction is limited to certain activities in connection with petroleum resources.

¹ Pursuant to Article 56 (1) of UNCLOS, Norway exercises similar rights in the Exclusive Economic Zone (EEZ), which consists basically of the water column above the continental shelf. Most importantly, these sovereign rights relate to living natural resources, such as fish. They also encompass wind energy production, which has significant potential on the NCS.

A coastal State's jurisdiction over its continental shelf relates to natural resources. Mainly these are the mineral and non-living resources of the seabed and subsoil, *cf.* Article 77 (4). One question here is whether reservoirs on the continental shelf used for the storage of carbon dioxide (CO₂) injected into the seabed can be regarded as a natural resource. The Norwegian government is in the process of proposing new legislation on this issue pursuant to the Continental Shelf Act.² This implies that subsea reservoirs on the continental shelf used for the permanent storage of CO₂ are considered to be a natural resource over which Norway exercises sovereign rights. Thus CO₂ stored in subsea reservoirs on the NCS does not pose jurisdictional problems. The same position has been adopted in other jurisdictions.

Sovereign rights over the continental shelf are exclusive in the sense that if the coastal State does not explore the continental shelf or exploit its natural resources, no one else may undertake these activities without the express consent of the coastal State, *cf.* Article 77 (2).

The term continental shelf is defined in UNCLOS Article 76 as the seabed extending beyond the territorial sea to the outer edge of the continental margin or in any case extending 200 nautical miles from the baseline from which the territorial sea is measured. The continental margin is further defined in Article 76, with the result that a State's continental shelf may be curtailed due to the proximity of opposite or adjacent coastal States. Such States must enter into delimitation agreements regarding the extent of their respective continental shelves. Norway has entered into delimitation agreements with Denmark and the UK, Iceland, Denmark/Greenland and Russia based on the median line principle. The delimitation agreement with Russia was signed on 15 September 2010 and is awaiting ratification in the respective Parliaments.³

² Act no. 12 of 21 June 1963 relating to exploration for and exploitation of other subsea natural resources than petroleum.

³ The Storting and the Duma.

2 EEA law – the EEA Agreement

Norway is a member of the EEA Agreement and accordingly forms part of the EU internal market, which aims to achieve a free flow of goods, services, persons and capital. The agreement has been entered into between the EFTA Member States (except Switzerland) and the EU Member States,⁴ which together constitute the European Economic Area. In addition to its jurisdictional significance, the agreement is also important from a resource management perspective. In paragraph 10 of the preamble, the parties emphasise their commitment to the prudent management of natural resources. Furthermore, in paragraph 11 they state their intention to base their future legislation on their commitment to achieve high levels of protection of health, safety and the environment and safety.

The agreement operates on two levels. The primary legislation consists of the EEA Agreement itself, which has been transposed into Norwegian legislation by the EEA Act.⁵ The secondary legislation consists of directives and regulations incorporated into the EEA Agreement by decision of the EEA Joint Committee.⁶ These have been implemented through many Norwegian acts and regulations pursuant to Article 7 of the EEA Agreement. As far as the petroleum sector is concerned, the so-called Hydrocarbons Licensing Directive and Gas Market Directives I and II have been incorporated into the EEA agreement and implemented in Norway through the Petroleum Activities Act (PAA) and the Petroleum Activities Regulation (PAR).⁷ We will return to the relevant

⁴ The EEA Agreement was signed on 2 May 1992 and entered into force on 1 January 1994.

⁵ Act no. 109 of 27 November 1992.

⁶ The EEA Joint Committee consists of representatives of the parties to the agreement. Decisions are made by consensus, *cf.* Article 93 (2) of the EEA agreement.

⁷ Directive 94/22/EC on the conditions for granting and using authorizations for the prospection, exploration and production of hydrocarbons, Directive 2003/55/EC concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC. These directives are incorporated into Appendix 4 to the EEA Agreement.

provisions below. The Gas Market Directive III is in the process of incorporation into the EEA Agreement.

According to Article 126 of the EEA Agreement, the agreement applies to the territories of the parties. This wording excludes the NCS, which is not part of the “territory” of Norway. All the same, the Licensing Directive and the Gas Market Directives have been incorporated into the EEA Agreement and implemented through the PAA and the PAR. Although these directives – for Norway – will mainly affect petroleum activities on the NCS which is outside the territory of Norway, the EEA parties considered it useful to incorporate the directives into the EEA agreement.

Another debated provision is Article 125, which states that the agreement shall not affect the parties’ rules on property rights. The prevailing view is that while this article does not prohibit the complete public ownership of resources, which Norway has recently introduced as regards waterfalls, this ownership has to be exercised in accordance with the principles of the EEA Agreement. So far, no similar disputes have arisen under the agreement regarding the ownership of Norwegian petroleum deposits on the NCS, as such ownership stems from Norway’s exclusive right under international law to declare its property rights over its natural resources. Such a declaration was made by Norway on 31 May 1963.

3 National law - the Petroleum Activities Act

Here we will deal primarily with the PAA⁸, although it should be noted that several national acts are relevant to petroleum activities. In addition, the act has been supplemented by several regulations containing more detailed provisions (adopted pursuant to the PAA section 10-18 first paragraph).

⁸ Act no. 72 of 29 November 1996 relating to petroleum activities.

Pursuant to the PAA section 1-1, the property rights to the petroleum resources on the NCS are vested in the Norwegian State. This implies, as a starting point, that the Norwegian State is free to conduct all petroleum activities itself, or through a State-owned company. This is the situation in several petroleum provinces around the world.⁹ Instead, however, the Norwegian State has established a licensing system whereby private and State-owned companies participate as licensees together with the State. The reason for adopting this system was to attract technologically competent and financially strong companies to perform petroleum activities on the NCS. We will revert to the licensing system shortly.¹⁰ Meanwhile, it is clear from the above that commercial companies do not own the petroleum while it is still underground. As licensees, however, they become the owners of their proportionate share of the petroleum produced.

Furthermore, the State has an exclusive right to resource management, *cf.* PAA section 1-1. This provision basically represents a national codification of the principle contained in UNCLOS Article 77 (2). We will revert to the term “resource management” below.

The scope of the PAA requires some initial clarification. As a starting point, the act regulates petroleum activities in connection with subsea petroleum deposits under Norwegian jurisdiction, *cf.* PAA section 1-4 first paragraph. This gives rise to a few issues that need to be highlighted. First, the deposits have to be located on the NCS. A separate act deals with deposits under Norwegian land territory and parts of the seabed subject to private property rights, although so far there are no indications of petroleum deposits in such areas.¹¹ Second, the act regulates petroleum activities in connection with deposits on the NCS. The term petroleum activity is defined in the PAA section 1-6 c. The term is defined broadly and covers activities in connection with a petroleum deposit, including exploration, exploration drilling, production, transport, exploitation and decommissioning (abandonment). These

⁹ Jens Evensen, *Oljepolitiske synspunkter*, Oslo 1971.

¹⁰ See Section II below.

¹¹ Act no. 21 of 4 May 1973.

activities are further defined elsewhere in the PAA section 1-6 and do not necessarily have to take place on the NCS. In fact, several take place on land, typically in landing and processing terminals. This illustrates the *functional scope* of the act. However, the PAA does not cover the transmission, distribution and supply of gas on Norwegian territory. These latter activities are regulated under the Act on Common Rules for the Internal Market in Natural Gas.¹² This act will not be dealt with here. Third, the petroleum activities have to be performed on a facility (defined in PAA section 1-6 d). Note that the definition of “facility” does not include either supply or support vessels or ships that transport petroleum in bulk. Such vessels are considered to be conducting normal shipping activities.

II The licensing system

4 Resource management

The PAA section 1-2 first paragraph introduces the person responsible for executing resource management: the King, who is the highest executive body of the Norwegian state hierarchy. In practice, the King has only a formal role. Real executive power rests with the Cabinet, which has to a large extent delegated its powers to the Ministries. And the Ministries have further delegated their authority to subordinate Directorates. This delegation of powers is reflected in the PAA and in the regulations adopted pursuant to it. In practice, the resource management is carried out by the licensing and regulatory authority.

Petroleum is a limited non-renewable natural resource with a large revenue potential. These characteristics are fundamental to the resource

¹² Act no. 61 of 28 June 2002.

management that is the objective of the PAA. According to the PAA section 1-2 second paragraph, petroleum resources shall be managed in a long-term perspective for the benefit of Norwegian society as a whole. The provision lists several broad concerns that the resource management has to take into account. These include the generation of income, welfare and employment. Furthermore, the resource management shall take into account a variety of interests affected by the petroleum activities, including the environment, Norwegian industry, and regional and local policy considerations. However, these broad concerns are all effect-oriented and do not directly emphasise that petroleum is a limited and non-renewable resource. The latter concerns are reflected in the PAA section 4-1, which generally states that the production of petroleum shall take place in such a manner that as much as possible of the petroleum in place is produced. Furthermore, the production shall take place in accordance with prudent technical and sound economic principles and in such a manner that waste of petroleum or reservoir energy is avoided. Formally speaking, the PAA section 4-1 is directed towards the licensees, but it is generally understood that the resource management has to take this provision into account as well when issuing licences, and making decisions and regulations.¹³

The broad aims of the PAA section 1-2, *cf.* PAA section 4-1, are achievable by different means. One is State ownership and management of the petroleum resources. This is common practice in several petroleum provinces around the world, *e.g.*, Saudi Arabia and Mexico. Alternatively the State can enter into contracts with oil companies, either as entrepreneurs or as owners of part of the production (production-sharing contracts).¹⁴ Norway has opted for a system where companies

¹³ Another provision in the same category as section 4-1 is section 10-1, which contains requirements for prudent petroleum activities. According to this provision, the petroleum activities shall take due account of the safety of personnel, the environment and the financial values which the facilities represent. Furthermore, the petroleum activities must not to an unreasonable extent impede shipping, fishing, aviation or other activities.

¹⁴ An overview of the different systems and their implementation in various states is given by Jens Evensen *l. c.*

execute petroleum activities pursuant to a licence that grants them ownership of their proportionate share of the petroleum produced. A similar system has been adopted in the UK. A key characteristic of licensing systems is that they do not inhibit the State's financial and legislative powers. Consequently, the companies have to rely for investment protection on the continued existence of a stable and well-functioning State. But the Norwegian licensing system also includes a significant element of State ownership, to which we will return shortly.¹⁵

5 Characteristic features of the Norwegian licensing system

The Norwegian licensing system consists of three types of licence: the exploration licence; the production licence; and the specific licence to install and operate facilities for the transport and utilisation of petroleum. In addition, the approval of the Ministry of Petroleum and Energy (MPE) of the development plan (the plan for development and operation) and the MPE's decision relating to the disposal of installations on the basis of the decommissioning plan are both regarded as coming within the licensing system.¹⁶ Although these approvals and decisions are not licences and thus not formally part of the licensing system, they constitute important decisions relating to specific stages of the petroleum activities. In this regard they resemble licences, as a company needs a licence or a government approval/decision before it can commence the next stage of the petroleum activities. In connection with these successive licences or approvals/decisions, the Ministry may stipulate conditions when these are naturally linked with the activities to which the individual administrative decision relates, *cf.* PAA section 10-18 second paragraph.

Other characteristic features of the licensing system are the State's

¹⁵ See section 11 below.

¹⁶ The Ministry of Petroleum and Energy.

organisation of the companies within the licence groups into joint ventures and the comprehensive direct State participation in the licence groups. We will discuss these features in more detail in Section IV below.

III The exploration licence (Petroleum Activities Act, Chapter 2)

6 Scope and contents

Following the opening of new areas pursuant to the PAA section 3-1, the Ministry may grant exploration licences.¹⁷ The authority to do so has been delegated to the Norwegian Petroleum Directorate (NPD). The purpose of this licence is to allow companies to prospect for petroleum deposits. The term “exploration” is defined in the PAA section 1-6 (e) and basically refers to seismic surveys of the geology beneath the seabed. It does not cover drilling (except shallow drilling) for petroleum or for the production of petroleum. Only companies need to obtain a licence: the State itself can conduct activities without a licence, *cf.* PAA section 1-3. The application of the latter provision is general, as it applies to the whole chain of petroleum activities. But it is of very practical application during the exploration phase, since the NPD conducts seismic surveys without an exploration licence.¹⁸ When a licence is necessary, the contents of an application are regulated by the PAR section 3.

Exploration licences are granted for a limited area and for a limited period of three years, *cf.* PAA section 2-1 third paragraph. The scope

¹⁷ The PAA section 3-1 is dealt with in section 9 below.

¹⁸

of the licence is decided by the licensing authority, the NPD. The latter may also stipulate terms for the licence, including terms about the sale or exchange of exploration results, *cf.* PR section 4. Normally exploration activities are undertaken by specialist companies that sell their results to the oil companies on commercial terms.

7 Relationship to the production licence

An exploration licence grants no rights to future licences, including production licences. Furthermore, this licence does not grant exclusive rights, meaning that several licensees and/or the NPD may conduct seismic surveys within the same area at the same time.

IV The production licence (Petroleum Activities Act, Chapter 3)

8 Introduction

This is the main licence determining access to the petroleum resources on the NCS. Initially there were no international restraints on the Norwegian government's authority when granting production licences. As a result, national oil companies, and especially the wholly State-owned company Statoil, were put in a privileged position. This practice changed when Norway became a member of the EEA Agreement and the Hydrocarbons Licensing Directive was implemented into Norwegian law. Today all companies have to compete for production licences and no discrimination is permitted on the basis of nationality, *cf.* Article 4 of the EEA Agreement.

In the following, we will focus first on the procedure for awarding a production licence. Thereafter we will examine the licence group (*i.e.*, the group of companies holding a licence), State participation within the group, and the rights and obligations associated with a production licence.

9 The award process

We need to draw an initial distinction between mature areas and frontier areas. Mature areas are those that have been opened previously and where petroleum activities have commenced. Accordingly the geology of these areas is well-known and the fields are located near existing infrastructure.¹⁹ From a government perspective, it is important to develop these areas rapidly while the infrastructure is still in place and so licensing rounds are announced annually in a system known as “Awards in Predefined Areas” (APA). In frontier areas, by contrast, the geology is little known.²⁰ The first step in the procedure for the award of new production licences in these areas is the opening of new areas, *cf.* PAA section 3-1. This involves an initial impact assessment carried out by the MPE, with a particular focus on the impact of future petroleum activities on all relevant areas, such as society, trade, industry, other users of the sea (*e.g.*, fisheries) and the environment. Next the impact assessment is submitted for broad public consultation to local, regional and central authorities, and to organisations that are presumed to have a special interest in the matter.²¹ The final decision on whether to open a new area is taken by the Norwegian Parliament. With regard to the northern Norwegian Sea and the Barents Sea,

¹⁹ The mature areas are located generally in the North Sea and the southern part of the Norwegian Sea. See *Facts 2010* pp. 30-32.

²⁰ The frontier areas are located generally in the northern part of the Norwegian Sea and the Barents Sea. See *Facts 2010* pp. 32-33.

²¹ More detailed rules on impact assessments pursuant to Petroleum Act section 3-1 are contained in the PAR chapter 2A.

Parliament has passed plans for the management of these areas, including opening them for petroleum activities (Comprehensive Management Plans). The management plan for the Barents Sea was passed in 2006.²² A similar plan for the Norwegian Sea was passed by Parliament in 2009. In these plans, special emphasis has been placed on environmental impacts and the relationship between petroleum activities and fisheries interests, shipping and other relevant issues. As a result, certain areas have not been opened for petroleum activities for the time being.²³

Once an area has been opened for petroleum activities, the next step is the announcement of the area with a view to the submission of applications for production licences, *cf.* PA section 3-5. The announcement will contain information on, *inter alia*, the areas for which applications for new production licences may be submitted, the award criteria and licence terms that shall apply, and the terms that are negotiable. The announcement must be published.²⁴ We will revert below to the award criteria and the licence terms.

The normal procedure on the NCS has been to hold licensing rounds during which applications are received from individual companies.²⁵ The MPE then composes licence groups on this basis. The rationale for adopting this procedure has been that it gives the licensing authority the flexibility to compose groups that have an optimal mix of technical competence and financial capacity. The Hydrocarbons Licensing Directive does not prohibit this practice (*cf.* Article 5 (1) of the directive), provided that the composition of the group is determined on the basis of objective and non-discriminatory criteria. Accordingly the MPE has continued this practice, subject to a few exceptions.

²² Facts 2010 p. 33.

²³ This applies to the Lofoten area in particular.

²⁴ In the Norwegian Gazette (*Norsk Lysingsblad*) and the Official Journal of the European Communities.

²⁵ The first licensing round was held in 1965 and in the period up to 2010 there have been 20 licensing rounds on the NCS. In addition, licensing rounds under the system for awards in predefined areas (APA) have been held every year since 2003.

The award criteria are stated in the PAR section 10, which reflects Article 5 (1) of the Hydrocarbons Licensing Directive. These criteria relate to the technical competence and financial capacity of the applicants, as well as their plans for exploration and production in the areas for which production licences are sought. Other objective and non-discriminatory criteria may be taken into account, but only to decide between two or more applications that are considered otherwise to be of equal merit.

Finally, the production licence is awarded by the King in Council, *cf.* PAA section 3-3 first paragraph. This procedure is purely formal and in practice the government will have prepared all aspects of the decision in advance. Normally, production licences are awarded to joint stock companies registered in Norway.²⁶ But licences can also be awarded to natural persons domiciled in an EEA Member State, or to entities registered within the EEA, *cf.* PAA section 3-1 second paragraph.

What can a disgruntled applicant do? The company may have received, for example, a smaller licence interest than it applied for, or no licence interest at all. Since the decision is made by the King in Council, the highest body in the State hierarchy, an administrative complaint is not possible. An administrative alteration is a possibility, but not a very practical one, unless the King's decision is illegal, *cf.* the Public Administration Act section 35. Illegality could result from incorrect application of the legislation, incorrect facts, incorrect procedure, or abuse of discretionary power. A disgruntled applicant may, however, complain to the European Surveillance Authority (ESA) if he believes that the licence award contravenes the EEA Agreement. Such a complaint may end up in the EFTA Court. An applicant may also sue the Norwegian government in the Norwegian courts. If the case involves the EEA Agreement, a preliminary ruling may be sought from the EFTA Court.

²⁶ A foreign company will establish a Norwegian affiliate in order to meet these requirements.

10 The licence group

A licence group is assembled for each individual licence. The relationship between the licensees is governed by the Agreement for Petroleum Activities (the Agreement), which has attached to it, as Appendix A, the Joint Operating Agreement (JOA). The Agreement and the JOA are standard documents drafted by the MPE. The older of the two, the JOA, has been revised several times.²⁷ These agreements, which are entered into by the licensees as a licence term, also contain the licence terms, *cf.* PAA section 3-3 fourth paragraph. Accordingly these agreements can be argued to form part of the licence, which means that they have to be interpreted in the same objective manner (unlike a normal agreement between private parties that under Norwegian law will be interpreted with the aim of finding the intention of the parties).²⁸

What are the characteristics of the joint venture? It is not a legal person pursuant to Norwegian company law. In fact, the Norwegian Companies Act makes a clear exception for joint ventures operating pursuant to the PAA.²⁹ But the principles of the Companies Act may supplement the JOA in certain cases. In other words, the principles of the Companies Act may apply to the extent that they are appropriate. The joint venture – not being a legal person – can be characterised as an expense fellowship. The expense fellowship is based on co-ownership according to licence interests. We should note here that the fellowship does not apply to the produced petroleum, of which each licensee owns its share.³⁰

The parties to the joint venture and their respective licence interests are stated in the Agreement (clause 2), which also contains the voting rules for the joint venture (clause 3). As a general rule votes are determined according to a combination of the number of entities in the joint

²⁷ The latest version dates from spring 2007.

²⁸ This mode of interpretation is similar to that adopted for the interpretation of acts and regulations.

²⁹ Companies Act section 1-1(4).

³⁰ See section 14 below.

venture and the licence interests they represent. The reasoning for this voting rule is to give smaller entities a reasonable influence in the licence groups. There are, however, exceptions. Certain decisions regarding the surrender of a licence or the revocation of part of the licence area require unanimity. And the company that manages the State Direct Financial Interest (SDFI), Petoro, has the right of veto regarding certain decisions in the licence group. We will revert to this shortly.³¹

The structure of the joint venture is dealt with in the JOA. The Management Committee (ManCom) is the governing body of the joint venture, *cf.* Article 1. All licensees are represented on the ManCom, which is chaired by the licensee that has been appointed field operator. The JOA contains detailed substantive and procedural rules on the tasks of the ManCom, which also has a general competence to decide upon any matter that is connected to the activities of the joint venture.

The operator is another important entity within the joint venture and is appointed by the MPE, *cf.* PAA section 3-7. Normally, the operator is one of the licensees. If this is not the case, the operator will be subject to corresponding obligations under the PAA, *cf.* section 3-7 third paragraph. The operator is also identified in the Agreement and the competences of the operator are regulated in the JOA Article 3. The operator is responsible for the day-to-day management of the joint venture. Internally, the operator prepares decisions for consideration by the ManCom. Externally, the operator represents the joint venture towards contract parties and third parties. The operator performs its duties on a “no gain – no loss” basis. This is standard practice in petroleum activities. The reasoning is that the operator recovers any gains in its capacity as a licensee, by virtue of which it owns part of the production. In addition, the operator gains valuable technical expertise which may be beneficial when future licences are awarded.³² Accordingly the role of operator is highly regarded by the oil companies. It is natural that the operator should not incur any losses when performing its duties on behalf of the joint venture, although the operator will be responsible

³¹ See section 11 below.

³² See section 9 above on award criteria.

for losses incurred by the other joint venture parties that are the result of its wilful misconduct or gross negligence.³³

11 State participation

State participation is very typical of the Norwegian licensing system. The State owns the subsea resources and could have opted to conduct all petroleum activities itself. Instead the State opted to organise its participation in petroleum activities through a licensing system under which the State owns certain licence interests. The nature of this ownership has changed over time.

Originally the State participation in the licensing system was carried out through Statoil, which was formed as a wholly State-owned limited company in 1972. Statoil was granted a 50% licence interest in all licence groups from the third licensing round onwards. The JOAs gave several privileges to Statoil, including a carried interest in the exploration phase and an option to increase its participating interest if a petroleum deposit was found. In addition, the JOAs contained voting rules which gave Statoil a dominant position in the decision-making process.

With effect from 1 January 1985, the State's ownership was reorganised. An arrangement was established between Statoil and the State whereby Statoil's licence interests were split into a Statoil economic share and a State economic share, called the State Direct Financial Interest (SDFI). This was an internal arrangement between Statoil and the State under which a share of the costs accrued and a corresponding share of the revenues generated by Statoil in the licence groups were directly channelled to the State. Externally (*i.e.*, towards the other members of the licence groups, contract parties and third parties) Statoil was still the formal licensee – with its previous licence interests

³³ Cf. JOA Article 3.5. According to this provision, the operator shall under no circumstance be liable for any loss suffered by the parties in connection with damages to third parties caused by a spill of petroleum outside the safety zone.

intact. However, Statoil's dominant position in the licence groups was considerably reduced through changes to the voting rules in the JOAs.

In 2001, another major reorganisation took place that drew a basic distinction between the ownership and resource management roles. The latter role was considered to be best executed by the licensing authority and regulator. Consequently, Statoil was no longer regarded as a vehicle of the Norwegian State and was partly privatised and floated on the stock exchange.³⁴ However, the special rules of the Limited Companies Act (LCA) on companies wholly owned by the State do not apply to a partly privatised Statoil. As a result, the State does not have full control as an owner of the company. Against this background, the management of the SDFI has been transferred to a new wholly State-owned company called Petoro, which has as its main purpose the management of the SDFI.

Petoro's management of the SDFI is regulated in the PAA chapter 11. The relationship between Petoro and the State represents an extension of the previous relationship between Statoil and the State. Since Petoro is organised as a wholly State-owned limited company, the State can direct Petoro's activities as an owner through the company's General Assembly pursuant to the special rules (pertaining to wholly State-owned companies) of the LCA. But unlike the situation with Statoil, Petoro's activities as a general rule are limited to activities regulated by the PAA, *cf.* PAA section 11-1 first paragraph. This means that Petoro's activities must come within the functional scope of the PAA, *cf.* PAA section 1-4. Petoro must manage the SDFI according to commercial principles, *cf.* PAA section 11-2 first paragraph. Wider resource management objectives are pursued by the licence authority and the regulator according to the provisions of the PAA.

The State itself does not apply for licenses, instead reserving licence interests for itself (without any competition), *cf.* PAA section 3-6. This is in accordance with the Hydrocarbon Licensing Directive.³⁵ The PAA also specifies that the State owns the licence interests that it reserves for

³⁴ The State is still a majority owner. At present it owns 67% of the shares.

³⁵ Article 6 (3).

itself, *cf.* PAA section 11-1 first paragraph. Petoro is merely the manager of these licence interests and does not have to compete to provide this service.

In relation to the other licensees in a licence group, the 2001 reform implied important changes in a formal sense. Petoro – as manager of the SDFI – represents the State in the licences. Thus, formally speaking, Petoro is a licensee and a party to the JOA that regulates the relationship between the licensees in the joint venture, *cf.* PAA section 11-2 second paragraph. As a party to the JOA, Petoro takes part in decision-making processes within the joint venture. But Petoro is never the operator of the joint venture, which the most attractive position for oil companies. This is because Petoro is not an ordinary oil company, but is the manager of the SDFI. As a result, Petoro is a relatively small company with approximately 60 employees.

Petoro can oppose decisions by the ManCom that do not respect the conditions and requirements specified in the production licence regarding depletion policies and the State's financial interests, *cf.* PAR section 12 third paragraph and the JOA Article 2.3.³⁶ This is called the veto right. In exercising this veto right, Petoro would function as an instrument for State control. In practice, the veto right has never been exercised.

Petoro does not own produced petroleum, which is owned by the State. Statoil is still responsible for selling the State's share of produced petroleum, although it now does so under the supervision of Petoro. This supervision poses an administrative challenge for Petoro, but does not require it to be organised along the lines of an oil company.

Externally, the licensees will incur contractual obligations and liabilities towards third parties, for example, liability for pollution damage pursuant to the PAA chapter 7. Although this also applies to Petoro, the State is directly liable for any contractual or other obligations incurred by Petoro, *cf.* PAA section 11-3. Petoro will merely receive any claims and forward them to the State. It is not possible to initiate bankruptcy

³⁶ These provisions reflect Article 6 (3) sub-para 3 of the Hydrocarbons Licensing Directive.

proceedings against Petoro.

So what kind of entity does Petoro constitute? Formally speaking it almost resembles a hybrid, conducting a mix of commercial functions (PAA section 11-2) and public functions (the veto right) on behalf of the State. In practice, however, Petoro functions as a commercial entity.

12 The scope of the licence

We can distinguish between a licence's functional scope, its geographical scope and its duration. The licence's functional scope consists of the licensed activities. According to the PAA section 3-3, a production licence entails a right to exploration, exploration drilling and production of petroleum. These terms are defined in the PAA section 1-6. It is important to note here that the term "production" does not encompass the transportation or utilisation of petroleum, for which a separate licence pursuant to the PAA section 4-3 is required, unless the activities are covered by the development plan approval. The latter licences and approvals³⁷ will form the topic of a separate article. Decisions in both these areas come within the licensing system.

A production licence may cover one or several blocks or parts of blocks, *cf.* PAA section 3-3 first paragraph.³⁸ This does not mean that all the production activities necessarily take place within this area. Certain activities may take place on land using modern technology. This is in accordance with the functional scope of the act³⁹. But the petroleum deposit itself must be located within the licence area. To this extent, the geographical scope of a production licence is the licence area. The licence area is an important issue prior to the award of a production licence. In the invitation to submit applications, the licence area is

³⁷ Development of Fields and Infrastructure.

³⁸ The continental shelf is divided into blocks defined by specific geographical coordinates, *cf.* Petroleum Act section 3-2.

³⁹ See 3.

singled out as an item for negotiation.

In other words, the licence area can be negotiated by the applicant and the MPE. On the other hand, the licensee (*i.e.*, the licence group) can later – on specific terms – relinquish parts of the area covered by the licence, *cf.* PAA section 3-14. The licensee can also apply for a partitioning of the licence area and for the award of a separate production licence for the new area, *cf.* PAA section 3-10. The new licence can then be transferred to other companies, providing an opportunity for the restructuring of licence groups and facilitating the unitisation of licence activities. We will revert to unitisation below.⁴⁰

The duration of the licence is regulated in the PAA section 3-9. We can distinguish between three licence periods: 1) the initial period of up to 10 years; 2) the extension period (following the initial period), which is normally 30 years, but can be up to 50 years depending on the expected size of the petroleum deposit. The extension period is stipulated in the licence and is a typical item for negotiation. Note that the licensee can require an extension provided it has fulfilled the work commitment and the other terms of the licence.⁴¹ Historically, the licensee could keep 50% of the licence area. This reflected a compromise, as on the one hand, the licensee should have the necessary incentives to explore the licence area during the initial period, while on the other hand, the licensee should not have an incentive to keep unnecessary licence areas in later periods. Now the licensing authority (*i.e.*, technically, the King) decides on this matter when awarding licences as this allows for more flexible solutions; 3) the licensee can apply for a special extension of the licence. This is relevant when the petroleum deposit cannot be produced completely within normal licence periods.⁴² The duration and the terms of such an extension will be stipulated by the MPE. On the other hand, the licensee can on specific terms surrender the licence, *cf.* PAA section 3-15.

It is debatable whether the singling out of specific licence terms as

⁴⁰ See section 14 below.

⁴¹ See section 13 below.

⁴² The Ekofisk and Troll fields are typical examples here.

negotiable has any impact on the status of the licence: *i.e.*, is it a contract between the Norwegian government and the licensee? The answer to this question has a considerable impact on the competence of the Norwegian authorities to change licence terms to the licensees' detriment, and was a key issue for licensees some years ago. Today most changes in licence terms are beneficial for the licensees, as the Norwegian government desires to maintain the competitiveness of the NCS. Consequently, the status of the licence is no longer a major topic of debate and the parties seem to agree that the licence is not a contract.

13 The obligations of the licensee

The PAR section 11 generally states the types of concerns on which conditions in production licences can be based.⁴³ This provision reflects Article 6 (1) and (2) of the Hydrocarbons Licensing Directive. Conditions must be based solely on the need to ensure that petroleum activities are carried out in a proper manner. Furthermore, a variety of non-economic and – to a certain extent – economic concerns can be taken into account. The latter are limited to those relating to systematic resource management (*e.g.*, the production rate or the optimisation of production activities) and the need to ensure fiscal revenues.

The most important obligation of the licensee during the initial licence period is the obligatory work commitment. Here we need to distinguish between frontier and mature areas.⁴⁴ In frontier areas, the licensee has an obligation to drill a certain number of exploration wells.⁴⁵ The decision to do this requires majority support in the licence group. If no such decision can be reached and no licensees wish to drill in any event, the licence must be surrendered. If some licensees

⁴³ Note that several conditions are codified in the PAA and the regulations are passed pursuant to the PAA. In the following, however, we discuss the conditions in the production licence.

⁴⁴ See section 9 above.

⁴⁵ The production licence 19th licensing round item 4.

wish to drill in any event, the remaining licensees must withdraw from the joint venture. In mature areas, licensees already have substantial knowledge of the geology and it is important to develop the fields quickly. This is reflected in the work commitment for these areas. The licensees have to decide whether to prepare a plan for development (in addition to drilling exploration wells). If no such decision is taken, the licence must be surrendered. If the licensees decide to continue operations, they must prepare a plan for development for the MPE's approval within a fixed time limit from the award of the licence. If they fail to do so, the licence must be surrendered.⁴⁶

Another important item is the miscellaneous conditions.⁴⁷ These contain several prohibitions on drilling and production that are intended to protect the environment and fisheries. Among others there is – as a general rule – a zero discharge obligation. This obligation was formulated initially in government reports to Parliament.⁴⁸ As such reports are not binding on the licensees they must be referred to in the licence documents in order for the obligations recommended in them to take effect. The miscellaneous conditions also contain several references to acts and regulations. The latter references are not strictly necessary from a legal perspective, but may have a beneficial informative effect for licensees and authorities.

We should also mention the area fee here, *cf.* item 2. This is regarded as a rent for the licence area, but is only applicable during the extension period in order to give licensees a sufficient incentive to conduct exploration. More detailed provisions on the calculation of the area fee are found in the PAR section 39.

⁴⁶ Awards in predefined areas 2005 item 4.

⁴⁷ Item 5 in licences for both mature and frontier areas.

⁴⁸ See Report to the Storting No. 25 (2002-2003).

14 The rights of the licensee

The basic rights of the licensee are stated in the PAA section 3-3. However, there are important derogations to be derived from the (rest of the) act. First, the licensee becomes the owner of the produced petroleum. However the manager of the SDFI, Petoro (which participates in the licences on behalf of the State), does not own any of the produced petroleum.⁴⁹ Second, the licensee has exclusive rights to exploration, exploration drilling and production within the licence area. If however the petroleum deposit extends beyond the licence area, the licensee has an obligation to conduct joint activities with the licensee of the adjacent area, *cf.* PAA section 4-7.⁵⁰ The international term for such joint activities is “unitisation”. The PAA goes further, as this obligation also applies in cases where several petroleum deposits are located in separate licence areas and joint activities would obviously be most efficient. Other parties also have certain rights to conduct exploration, to locate facilities and to explore for and produce other natural resources than petroleum within the licence area, provided these activities do not unreasonably inconvenience the petroleum activities, *cf.* PAA sections 3-11, 3-12 and 3-13. The rights to locate facilities according to the PAA section 3-12 have been important, as a pipeline infrastructure to transport petroleum has been established across licence areas. In the future, offshore wind parks have significant potential. Although the building and operation of wind turbines offshore are regulated by a separate act,⁵¹ the relationship of these activities to petroleum activities is regulated by the PAA. Third, the licensee acquires a production right according to PAA section 3-3, but the scope of this right depends on future licences and approvals, especially the approval of the development plan pursuant to PAA section 4-2. We will revert to this in a separate article, *Development of Fields and Infrastructure*.

⁴⁹ See section 11 above.

⁵⁰ The international term in this respect is “unitization”.

⁵¹ Act 4 June 2010 no. 21 relating to renewable energy production offshore (offshore energy production act).

Maritime Plus and the European status quo

The current framework of international transport
law, 'maritime plus' and the EU

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1 Multimodal transport and the law

The use of standardised intermodal containers, which enhances the safety of goods in transit and reduces operating costs, has caused multimodal transport to become a global phenomenon since its introduction in the maritime environment during the previous century. Despite its practical success, however, the proliferation of this type of transport has up until now not been matched by suitable uniform legislation. Political discord and the fact that the use of more than one mode of transport under a single contract complicates the legal situation exponentially probably lie at the root of this deficiency.

Although the multimodal contract of carriage contends with some other legal impediments, the most prominent one seems to be that of ambiguity with regard to the applicable law. The reason for the obscurity in this area is that there is no international multimodal transport convention to lay the ground rules on how to approach a multimodal contract.

Current national and international transport law only regulates carriage by a single means of transport. This is reflected by the international carriage conventions such as the CMR for road carriage contracts,¹ the COTIF-CIM for rail carriage,² the Montreal Convention for air carriage,³ the CMNI for inland waterway carriage⁴ and the Hague Rules,⁵ the Hague-Visby Rules⁶ and the Hamburg Rules for the carriage

¹ The Convention on the Contract for the International Carriage of Goods by Road, signed at Geneva 19 May 1956.

² The Convention concerning International Carriage by Rail (COTIF) of 9 May 1980 as amended by the Protocol of Modification of 3 June 1999 (Vilnius) – Appendix B (CIM).

³ The Convention for the Unification of Certain Rules for International Carriage by Air, signed at Montreal on 28 May 1999.

⁴ The Budapest Convention on the Contract for the Carriage of Goods by Inland Waterway of 22 June 2001.

⁵ The Hague Rules; The Brussels Convention for the Unification of Certain Rules of Law relating to Bills of Lading of 25 August 1924.

⁶ The Hague-Visby Rules; the Hague Rules as Amended by the Brussels Protocol of 23 February 1968.

of goods by sea. National carriage regimes generally tend to reflect this 'unimodal' approach, although the occasional domestic regime diverges from this structure. The German *Handelsgesetzbuch*, or Commercial Code, for instance, bundles the rules on all non-maritime carriage into one subsection, whereas sea carriage has its own set of rules.⁷ Some pioneers have even incorporated rules on multimodal contracts.⁸ These latter multimodal approaches are generally no more than network systems however, meaning that they cause a combination of the relevant unimodal transport rules to apply to a multimodal contract. This is a logical result of the hierarchy which exists in contemporary law.

2 The legal pecking order in the EU

The network approach, which may be characterised as 'live and let live', is the result of the fact that national legislators are generally left little room to manoeuvre by the mandatory international regimes. In the case, for instance, of the rules that are to be applied to the international air stages of a multimodal transport, the Montreal Convention specifically determines that it covers such transport in Article 38 MC. The air carriage convention cannot simply be set aside, since it consists largely of mandatory law, as do its road, rail, sea and inland waterway cousins. Because international law is positioned somewhat higher up the legal hierarchy than national law, a national legislator is unlikely to choose to apply other rules to such air transport than those of the Montreal Convention. The adoption of different national rules would be contrary to the obligations the state has taken upon itself by becoming a member of

⁷ Articles 407-450 HGB for non-maritime carriage and Article 656-663b HGB for maritime carriage.

⁸ Examples include Articles 452-452d HGB of the German Commercial Code and Article 8:40-52 BW of the Dutch Civil Code.

the international convention.⁹

Of course, an international treaty generally should not need national rules in order to apply, aside, that is, from any legislation that might be needed to implement the treaty into the national legal sphere. International transport treaties like the Montreal Convention supply their own scope of application, within which they should be applied regardless of what national rules indicate. One could say international law is created to override national law.¹⁰ Thus, if the state where the court addressed is situated is party to a transport convention that is applicable according to its rules on scope of application, the said court is bound to apply this convention whether the applicable national regime concurs or not.

The same applies to the relationship between national legislation and contractual provisions: national law takes precedence over the provisions of the contract. It should be noted, however, that this is only the case where the national rules are mandatory.

But what of the position of the rules made in Brussels? Where does primary and secondary EU law fit into this picture?¹¹ To answer this question, we must start with the basics. The EU in its current form originates from a series of treaties. The first were the three treaties creating the ECSC, the EEC and EURATOM.¹² These three Communities, which attracted more members over the years, were later combined by the

⁹ According to Article 26 of the Vienna Convention on the Law of Treaties (VC) every treaty in force is binding upon the parties to it and must be performed by them in good faith. This is a codification of the globally accepted adage '*pacta sunt servanda*'. Deviation from international treaties by means of national law is incompatible with this principle and therefore to be avoided.

¹⁰ De Witte 1999. Many nations have either legislation or decisions by their supreme courts that establish the supremacy of international law: in the Netherlands, Article 90 Dutch Constitution; in Belgium, Belgische Hof van Cassatie 27 May 1971 (Fromagerie Franco - Suisse Le Ski / 'Smeltkaasarrest'); in France, Article 55 French Constitution and Cour de Cassation 24 May 1975 (Cafés Jacques Vabre); and in Greece, Article 28 Greek Constitution.

¹¹ Strictly speaking, since the Lisbon Treaty of 1 December 2009, one should refer to primary and secondary EU law.

¹² The Treaty of Paris of 1951, which established the European Coal and Steel Community (ECSC) and the Treaties of Rome of 1957 establishing the European Atomic Energy Community (EURATOM) and the European Economic Community (EEC).

Treaty of Maastricht of 1992 into the European Union and merged into a single legal entity by the Lisbon Treaty of 2009. According to the European Court of Justice (ECJ), which is an EU institution, sovereignty is vested in the Treaties.¹³ However, this assertion has only been granted limited acknowledgement by national governments in a Declaration attached to the Treaty of Lisbon.¹⁴ The main question therefore is to what extent the doctrine emanating from this sovereignty concerning the precedence of EU law over national law is accepted by the EU Member States.¹⁵

The supremacy doctrine was formulated clearly for the first time by the ECJ in 1964, in *Flaminio Costa v Enel*.¹⁶ In its decision the ECJ stated:

“By creating a Community of unlimited duration, having its own institutions, its own personality, its own legal capacity and capacity of representation on the international plane and, more particularly, real powers stemming from a limitation of sovereignty or a transfer of powers from the States to the Community, the Member States have limited their sovereign rights, albeit within limited fields, and have thus created a body of law which binds both their nationals and themselves.

¹³ ECJ 5 February 1963, case 26/62 (*Van Gend & Loos v Netherlands Inland Revenue Administration*), [1963] ECR 1 and ECJ 15 July 1964, case 6/64 (*Flaminio Costa v Enel*), [1964] ECR 585. This concept is not generally accepted however. Chalmers, Davies & Monti 2010, p. 187; Lepsius 2006, p. 29; Sorrentino 2006, p. 123-124.

¹⁴ “17. Declaration concerning primacy - The Conference recalls that, in accordance with well settled case law of the Court of Justice of the European Union, the Treaties and the law adopted by the Union on the basis of the Treaties have primacy over the law of Member States, under the conditions laid down by the said case law.”

¹⁵ Chalmers, Davies & Monti 2010, pp. 184-185. This is only one of four doctrines emanating from the sovereignty concept. The others are that EU law alone should determine the quality of the legal authority of different norms; that EU law can determine the extent of its authority; and the fidelity principle of Article 4(3) TEU.

¹⁶ ECJ 15 July 1964, case 6/64 (*Flaminio Costa v Enel*), [1964] ECR 585. In ECJ 5 February 1963, case 26/62 (*Van Gend & Loos v Netherlands Inland Revenue Administration*), [1963] ECR 1 the ECJ touched upon the issue, but the primary focus of that decision was on direct effect. Craig & De Búrca 2008, p. 345. In 1970 the ECJ underlined the primacy of EU law again in Case 11/70 *Internationale Handelsgesellschaft v Einfuhr- und Vorratstelle für Getreide und Futtermittel* [1970] ECR 1125.

...

The obligations undertaken under the Treaty establishing the Community would not be unconditional, but merely contingent, if they could be called in question by subsequent legislative acts of the signatories.

...

The precedence of Community law is confirmed by Article 189, whereby a regulation 'shall be binding' and 'directly applicable in all Member States'. This provision, which is subject to no reservation, would be quite meaningless if a State could unilaterally nullify its effects by means of a legislative measure which could prevail over Community law.

It follows from all these observations that the law stemming from the Treaty, an independent source of law, could not, because of its special and original nature, be overridden by domestic legal provisions, however framed, without being deprived of its character as Community law and without the legal basis of the Community itself being called into question."

Thus the ECJ has made its point of view quite clear. But is this radical opinion accepted by the EU Member States? In truth, there have been only a few instances in which a national constitutional court has given a national measure priority over an EU measure. In two cases national courts have decided against surrendering individuals wanted in another state within 45 days. These decisions were based on the thinking that, since the measures concerned were in the third pillar, they did not have to take priority over national law at that time.¹⁷ In essence, there is

¹⁷ The surrender of the individuals was prescribed by a European arrest warrant issued based on the Council Framework Decision 2002/584/JHA of 13 June 2002 on the European arrest warrant and the surrender procedures between Member States *Attorney General of the Republic of Cyprus v Konstantinou* [2007] 3 CMLR 42 and *Re Enforcement of a European Arrest Warrant* [2006] 1 CMLR 36. Chalmers, Davies & Monti 2010, p. 204.

tension between the ECJ's view of the status of EU law and that in certain Member States. In *Gauweiler* for instance, the German *Bundesverfassungsgericht* (BverfG), the German constitutional court, clarified that it did not deem it contradictory to the realisation of a united Europe to declare EU law inapplicable in Germany by exception.¹⁸ Generally speaking, however, there seems to be a trade-off between the acceptance of the supremacy of EU law in most cases and the fact that only a small proportion of EU law is invoked before domestic courts. Member States tend to accept the supremacy of EU law when they consider it to be acting within its proper sphere of competence. In most Member States the conceptual basis for this acceptance is not the ECJ's reasoning in *Costa*, but rather provisions found in their own domestic legal orders.¹⁹

The fact that EU law as a general rule is granted supremacy over national law in EU Member States does not, however, tell us anything about its status in relation to international law. For example, is it of a higher order than the international law of the carriage conventions, or should the carriage conventions be considered superior?

In 2004 the ECJ clarified the matter, at least insofar as it concerns secondary EU law and the Montreal Convention.²⁰ In answer to the question whether Regulation No 261/2004 or the Montreal Convention should take precedence, the ECJ determined in *IATA and LFAA v Department for Transport* that:

“Article 300(7) EC21 provides that ‘agreements concluded under the conditions set out in this Article shall be binding on the institutions of the Community and on Member States’. In accordance with the Court’s case-law, those agreements prevail over

¹⁸ BverfG 30 June 2009, www.bverfg.de/entscheidungen/es20090630_2bve000208.html (*Gauweiler v Treaty of Lisbon*).

¹⁹ For instance Article 55 or 88(1) of the French Constitution and Article 11 of the Italian Constitution. Craig & De Búrca 2008, pp. 354, 357 and 365.

²⁰ ECJ 10 January 2006, case C-344/04 (*The Queen ex parte International Air Transport Association, European Low Fares Airline Association v. Department for Transport*), *Jur.* 2005, p. I-00403, see also *NJ* 2006, 372.

²¹ Currently Article 218 TFEU.

provisions of secondary Community legislation.”²²

Although clearly stated, this does not provide any insight into the relationship between EU law and all international treaties, merely those of which the EU is a member. The Montreal Convention may be an integral part of the EU legal order, the other carriage conventions are not.²³ The newest air carriage convention was signed by the Community on the basis of Article 300(2) EC.²⁴ Thus, it follows from Article 218(7) of the Treaty on the Functioning of the European Union (TFEU) that it takes precedence over secondary EU law, as it is an international agreement concluded by the EU.²⁵ Primary EU law, on the other hand, is not set aside. As part of the EU legal order, the air carriage convention does not precede either the TFEU or the TEU.²⁶

Article 218 TFEU does not provide any guidelines concerning treaty law that has not been entered into by the EU. As a result, the relationship between these two layers of law is still unclear.

²² Once a treaty concluded by the EU comes into force its provisions form an integral part of EU law. ECJ case c-181/73, *Haegeman v Belgium* [1974], ECR 449. See also Mendez 2010, under 1. This article can also be found at: <http://ejil.oxfordjournals.org>.

²³ Although the Montreal Convention is a part of the EU legal order it should be noted here that the EC's instrument of approval concerning the air carriage convention contained a declaration in which is stated that the Member States of the European Community have transferred competence to the Community for liability for damage sustained in case of death or injury of passengers and damage caused by delay and in the case of destruction, loss, damage or delay in the carriage of baggage. This made the EC, and currently the EU, competent to adopt rules in this area. It also states that since the competence of the EU is liable to continuous development it reserves the right to amend the declaration accordingly. As a result the status of the part of the Montreal Convention which contains rules concerning the carriage of is somewhat obscure. For the declaration see: www.icao.int/icao/en/leb/mtl99.pdf. Currently the EU is working on acceding to the COTIF. This is possible because *Article 38 COTIF, as modified by the Vilnius Protocol, permits regional economic organisations to accede to the Convention. Whether the EU can and will also accede to the appendices such as the CIV and CIM has not been made known.*

²⁴ Currently Article 218 TFEU. The Montreal Convention was approved by Council decision of 5 April 2001 and entered into force, so far as it concerned the Community, on 28 June 2004.

²⁵ Epiney, Hofstötter & Wyssling 2008, p. 142; Vandamme 2005, p. 190.

²⁶ See Article 218 TFEU. Tietje 2008, p. 57.

In any event, the hierarchy of international and EU law might, at this point in time at least, not seem such a relevant question as regards multimodal transport. After all, there is no EU Directive or Regulation on multimodal contracts, nor is there any such instrument regulating the carriage of goods in general.

As long as there is no international convention on multimodal transport however, there is a chance that Brussels will decide to implement regional, *i.e.*, EU, regulation. In spite of the fact that the industry appears to favour a global approach rather than a regional one, it seems that future EU legislation on this subject is being contemplated. In recent years, prominent legal professionals have been asked for advice, and even to draft potential systems, on several occasions.²⁷

But even if Brussels does not see fit to create a Directive or Regulation on multimodal transport, the question as to the legal status of EU law in relation to the international carriage conventions is still a valid one. The fact is that the Rome I Regulation on the law applicable to contractual obligations of 2008 is likely to add to the confusion over applicable law in the near future. Although the Regulation does not seem to be causing much discomfort at the moment, this may change if one of the Member States of the EU decides to ratify a new carriage convention.²⁸ If this were to happen, which is hardly unlikely given the recent developments in sea carriage law, the consequences of Article 25 Rome I would need to be examined.

Article 25 is meant to regulate the Regulation's relationship with existing international conventions. It does this by determining that: "*the Regulation shall not prejudice the application of international conventions to which one or more Member States are parties at the time when this Regulation is adopted and which lay down conflict-of-law rules relating to contractual obligations.*" The key elements here are the fact that the provision only causes the Regulation to cede to international

²⁷ An example of this is the draft system created by Professors Clarke, Herber, Lorenzon and Ramberg in 2005. Clarke, Herber, Lorenzon & Ramberg 2005.

²⁸ Excepting Denmark, since the Rome Convention was not replaced by the Rome I Regulation in this EU Member State.

conventions (a) to which one or more Member States were party as at 17 June 2008, and (b) that contain conflict-of-law rules relating to contractual obligations. Firstly, these conditions require some explanation. What, for instance, is meant exactly by ‘conflict-of-law rules’? Secondly, they cause the hierarchy of the different layers of law to become important once again. For if the scope-of-application rules of the carriage conventions should not be considered to be ‘conflict-of-law rules’ as, for instance, Wagner suggests, then the status of the international regime will determine whether it applies by means of the national regime appointed by the Rome I Regulation or whether it is considered to be a set of ‘overriding mandatory provisions’, as meant by Article 9 Rome I and thus granted application even in those cases where it is not part of the law appointed by the standard procedure of the Rome I Regulation, and accordingly has precedence *ex proprio vigore*.²⁹ Of course, this latter option is possible only if international conventions that are not part of the EU legal order are deemed to take precedence over secondary EU law.

3 The shape of things to come

When there is a need to determine the law applicable to a multimodal carriage contract, the most efficient starting point still seems to be international law. Since there currently is no international law that regulates the multimodal contract as such, originating either from the EU or elsewhere, the existing transport conventions are the best place to start the investigation. The ‘unimodal’ carriage conventions mentioned in the first paragraph tend either to apply to parts of multimodal transport contracts or to extend their scope of application to certain specific types of multimodal carriage. Therefore the scope of application of these

²⁹ Wagner 2009. W.E. Haak also supported the view that scope-of-application rules are not truly conflict-of-law rules, arguing that since they only demarcate the applicability of a set of rules, they do not refer to the applicable domestic law. Haak (W.E.) 1973, p. 33.

conventions will be analysed in the following, starting with the CMR, the international road carriage convention. There follows a brief discussion of the CMNI and the COTIF-CIM – brief because these conventions largely share the phraseology of the basic scope-of-application provisions of the CMR and there has been much less controversy in legal literature and case law on their scopes of application in multimodal carriage.³⁰ As a result, any ambiguity which is discussed concerning the basic scope of application of the CMR, as established in Article 1 CMR, seems to concern the COTIF-CIM and the CMNI equally.

Unlike the CMR, the scope of the Montreal Convention does not generate many differences in interpretation when it comes to multimodal carriage. Article 38 MC is quite clear on the multimodal aspirations of the Convention. It applies to international air carriage, whether this is part of a multimodal contract or not.³¹ The air carriage convention is therefore mostly interesting as regards multimodal carriage when it comes to the convention's 'extracurricular activities', *i.e.*, the extensions of its scope of application beyond mere air carriage.

The final mode of transport to be reviewed is sea carriage. Although the currently operational sea carriage regimes are worthy of some attention, they are also not scrutinised in detail here. From a multimodal point of view it is not the existing regimes that are of most interest: the attention-grabbing regime is the one that is meant to set aside the current sea carriage conventions. The Rotterdam Rules with their 'maritime plus' approach may not be a fully fledged multimodal transport

³⁰ Basically, Article 1 CMR determines that the *Convention* "shall apply to every contract for the carriage of goods by road in vehicles for reward", Article 1 COTIF-CIM that it "shall apply to every contract of carriage of goods by rail for reward", and the CMNI in Article 2 that it applies to any contract of carriage, whereby a contract of carriage is "any contract, of any kind, whereby a carrier undertakes against payment of freight to carry goods by inland waterway" according to Article 1 CMNI.

³¹ According to Article 38(1) MC, its provisions shall apply only to the carriage by air in the case of combined carriage performed partly by air and partly by any other mode of carriage, provided that the carriage by air is the international carriage of persons, baggage or cargo performed by aircraft for reward, or is the gratuitous carriage by aircraft performed by an air transport undertaking.

regime, but they come close.³² These Rules are intended to regulate all contracts of carriage that include a sea leg. This includes any carriage by other modes of transport that precedes the sea carriage or is subsequent to it. It is therefore the Rotterdam Rules and their fit into the currently existing framework of carriage law that will form the focal point of the analysis of sea carriage law.

In light of the Rotterdam Rules and their potential entry into force in the future, the ensuing paragraphs will again discuss Article 25 of the Rome I Regulation and its possible consequences. With the possibility of individual Member States of the European Union ratifying the Rules in the near future, the question as to the nature of ‘conflict-of-law rules’ becomes sufficiently relevant to merit a review.³³

4 The ‘multimodal’ scope of the CMR

4.1 The ‘contract for the carriage of goods by road’

Article 1 CMR defines both the *ratione materiae*, the material scope of application or the subject-matter covered by the convention, and the *ratione loci*, the geographic scope of application. Of the various paragraphs in Article 1 CMR, it is the first that contains the core scope-of-application provisions.³⁴ It contains the following text:

³² The United Nations Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea, signed at Rotterdam on 23 September 2009.

³³ Since the ceremony in September of 2009, 21 States have revealed their intent to ratify the Rotterdam Rules by signing the new convention. Among these States are the Netherlands, Denmark, France, Greece, Poland and Spain. A complete list of signatories can be found at www.uncitral.org.

³⁴ The second through fourth paragraphs contain more or less marginal demarcation rules, such as definitions and exclusions of specific types of carriage such as funeral consignments. The fifth paragraph can almost be said not to relate to the Convention’s scope of application at all, as it merely entails an agreement by the Member States not to deviate from the Convention in bi- or multilateral agreements among themselves except in relation to a few specifically mentioned areas.

This Convention shall apply to every contract for the carriage of goods by road in vehicles for reward, when the place of taking over of the goods and the place designated for delivery, as specified in the contract, are situated in two different countries, of which at least one is a contracting country, irrespective of the place of residence and the nationality of the parties.

Thus the *ratione materiae* is determined objectively, independent of any rules of private international law.³⁵ But, objective or not, the words ‘contract for the carriage of goods by road’ have been the subject of ample discussion. It is these words that have turned out to be very prone to contrary interpretations by different courts of law.³⁶ The different views on the precise circumstances that will cause the CMR to apply by means of Article 1 CMR can be roughly divided into three categories:

(I) The CMR applies to road carriage provided for in a multimodal contract by means of Article 1 CMR, even if the road stage is merely domestic, as long as the contract as a whole is international.

(II) The CMR applies to road carriage provided for in a multimodal contract by means of Article 1 CMR, but only if the road leg itself fulfils all the conditions set by Article 1, meaning that it must be international.

(III) The CMR does not apply to any part of a multimodal transport by means of Article 1 CMR, because a multimodal contract is not a contract for the carriage of goods by road.

³⁵ De Wit 1995, p. 92. In Italy the *Corte Suprema di Cassazione*, the Supreme Court, maintains the rather exceptional view that the scope of application of Article 1 CMR is restricted by the provision found in Article 6 (1) (k) CMR. Because this last provision determines that the consignment note should contain a statement that the carriage is subject to the rules of the CMR, the *Corte* believes that the application of the CMR is conditional on such a statement, even though Article 4 CMR determines that the absence, irregularity or loss of the consignment note shall not affect the existence or the validity of the contract of carriage which shall remain subject the provisions of the CMR. Berlingieri 2006, p. 40. Not all the lower Italian courts share this view of the CMR’s scope of application. Margetson 2008, p. 130.

³⁶ See Haak & Hoeks 2005, pp. 95-97.

It seems that the only thing that can be said with any degree of certainty is that the text of Article 1 CMR does not support the application of the CMR rules to the non-road carriage legs of a multimodal carriage contract.³⁷

4.2 Article 1 CMR: The ‘pro’ CMR view

The view that the words ‘contract for the carriage of goods by road’ do not literally require the whole voyage to be made by road, merely that the contract includes a road stage, is held by many commentators and courts in Europe.³⁸ Indeed, the article does not state that the carriage has to be exclusively – or even predominantly – by road.³⁹ Therefore, if there is international road transport to or from a Contracting State according to the contract, the CMR applies to the said transport, whether or not the contract is *for* some other type of carriage as well.⁴⁰

It can be argued that interpreting these words differently, so that the CMR does not provide for the possibility of applying by means of Article 1, would lead to unwarranted inconsistencies between similar carriage contracts. Take for instance a contract for international carriage by road, for instance from Warsaw in Poland to Seville in Spain. Such a

³⁷ Ramming 1999, p. 329.

³⁸ Clarke 2003 *International carriage of goods by road*, p. 46 and Clarke 2003 *JIML*; Haak 1986, pp. 98-99; Messent & Glass 2000, p. 45; Van Beelen 1994; Thume 1994, p. 92; Putzeys 1981, pp. 103-104; A/CN.9/WG.III/WP.29, p. 29, par. 115, www.uncitral.org; *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 *Lloyd's Rep.* 25, *ETL* 2004, p. 535; *Datec Electronic Holdings Ltd v UPS Ltd* [2006] 1 *Lloyd's Rep.* 279; Cour de Cassation 25 November 1995, *Bulletin des Arrêts de la Cour de Cassation* 1995, IV, pp. 248-249; Rb Rotterdam 11 April 2007, *S&S* 2009, 55 (*Godafoss*); Rb Rotterdam 28 October 1999, *S&S* 2000, 35; LG Bonn 21 June 2006, 16 O 20/05; OLG Düsseldorf 29 September 2005, I-18 U 165/02. Even the German BGH seemed to support this view in the past, but in a recent judgment the BGH has clarified its views as being quite the opposite. BGH 24 June 1987, *TranspR* 1987, pp. 447-454; BGH 30 September 1993, *TranspR* 1993, pp. 16-18.

³⁹ “There is nothing in the Convention to indicate that, where a contract of carriage is to be performed partly by road and partly by other means of transport, this in itself results in the contract not being one for the carriage of goods by road in terms of Article 1, paragraph 1. In fact, the Convention implies the contrary.” Fitzpatrick 1968, p. 311.

⁴⁰ Clarke 2003 *International carriage of goods by road*, pp. 45 and 29-30; Clarke 2003 *JIML*, p. 32.

contract would, as a rule, be subject to the CMR, as it would concern unimodal international carriage by road. Another contract providing for carriage from Warsaw to Rabat in Morocco would also be subject to the CMR by virtue of Article 2 CMR, as long as the goods remained on their trailer for the short sea passage from Algeciras to Tangier. If the CMR could not apply to the road stages of a multimodal contract by virtue of Article 1, however, the nearly identical third example of a contract entailing carriage by road from Warsaw to Algeciras and by sea from Algeciras to Tangier, with the goods being transferred from the trailer to the ship in this instance, would not be subject to the CMR. This would even be the case for the road stage between Warsaw and Algeciras, which would comprise the largest part of the transport.

It is hard to imagine that either the drafters of the CMR or those involved in the international carriage of goods would regard this latter outcome as sensible. It seems unjustifiable that rights and responsibilities for long international trucking legs in comparable cases should depend on whether a carrier by road does or does not undertake the sea leg, or, if he does undertake it, on whether or not the goods remain on the trailer.⁴¹ All the more so since the Convention was created to generate legal security and a semblance of protection for the shipper. At least application of the CMR to road carriage that is part of a multimodal transport presents courts of law with an internationally known set of rules instead of with a national regime of which they may not have any intimate knowledge.⁴²

4.2.1 An international contract

Among those who are of the opinion that the CMR can be applicable to parts of a multimodal contract by means of Article 1 CMR, there has been some discussion as to whether this is possible when the road stage

⁴¹ Lord Justice Mance in: *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 *Lloyd's Rep.* 25, *ETL* 2004, p. 535 under no. 26.

⁴² The fear of foreign national law should in itself never constitute enough reason to stretch the scope of a convention beyond its intended boundaries however. Van Beelen 1994, p. 49.

itself is domestic. The *Rechtbank* Rotterdam for instance, is known to have expressed the view in the past that the CMR applies to road carriage provided for in international multimodal contracts. The most prominent dispute involved a damaged mobile crane which was carried from Cairo in Egypt to Geleen in the Netherlands.⁴³ Shortly after departure from Cairo the flatbed trailer on which the crane was loaded sank into the softer ground alongside the road due to the driver's negligence. Another crane was brought in to lift trailer and cargo back onto the road, but its cable snapped, toppling both crane and trailer. After the incident, the damaged crane was carried by sea from Alexandria to Antwerp, and transported from there to Geleen by road.

The *Rechtbank* chose to apply the rules of the CMR to the incident in Egypt due to the following disputable '*a contrario*' explanation of Article 2 CMR: since Article 2 CMR means that the CMR merely does not apply to the sea stage of the transport whenever the goods are unloaded from the road vehicle and loaded onto a ship, the CMR does apply to the road stages of such a transport, even if these are domestic. The Court deemed the contract to constitute an international carriage contract, as the place of taking over and the place of delivery were situated in two different countries. Furthermore, because part of this contract entailed road carriage, the Court found that the requirements of Article 1 CMR were met, at least insofar as the road stages were concerned. Therefore, the Court determined that judging the CMR inapplicable to all parts of the transport would needlessly and excessively restrict the CMR's scope of application, and would be contrary to the intentions of the parties to

⁴³ Rb Rotterdam 24 January 1992, *S&S* 1993, 89. In this judgment the Rotterdam Court was said to have followed the teachings of K. F. Haak. Van Beelen 1994, p. 43; Haak 1986, p. 99 and more recently Haak 2010, p. 47.

the convention to create a uniform regime.⁴⁴ However, the Rotterdam Court did deem it necessary for the transport to begin *and* end with road carriage, stating that it would stretch the scope of application of the CMR too far to apply the convention to a domestic road leg if it were the only road leg in the transport. This seems somewhat weak as arguments go, because if consistently employed, the 'extensive pro CMR' perspective⁴⁵ should cause the CMR provisions to apply to all road carriage under an international multimodal contract, and not merely in cases where there are two or more road legs with at least one at the beginning and one at the end of the transport. The convention does not supply any basis on which to support this type of differentiation.

Another weakness in the 'extensive pro CMR' position, as defended by the Rotterdam *Rechtbank* is that it seems to pay insufficient heed to the object and purpose of the CMR Convention. As touched upon earlier, the CMR is an international instrument and as such is meant to standardise the conditions governing contracts for the *international* carriage of goods by road. Indeed, this is stated literally in the preamble of the convention. To apply the CMR to domestic carriage simply because it forms part of an international carriage contract does not do

⁴⁴ Also in 1992, the *Rechtbank* Rotterdam drew a similar conclusion in relation to a series of potato transports from Gameren in the Netherlands to several destinations in Italy. Rb Rotterdam 5 June 1992, S&S 1993, 107. Since this transport started with carriage by road in one country and ended with carriage by road in another country the CMR applied. That the potatoes had been carried by rail between the first and the last domestic road legs did nothing to counter the applicability of the CMR to the road carriage according to the *Rechtbank*. As in the previously mentioned case it was stated that if there had been ro-ro transport, the CMR would have applied to the whole journey based on Article 2 CMR, and that the CMR applied to the road carriage stages by means of Article 1 if the trailer had not accompanied the potatoes during the rail stage of the transport. It was not deemed necessary for the road stage itself to be international in order for the CMR to apply by means of Article 1 CMR. As long as the place of taking over of the goods and the place designated for delivery, as specified in the contract, are situated in two different countries the CMR was to be applied to any road carriage the contract provides for.

⁴⁵ The view discussed in this section has been fittingly dubbed 'pro CMR' by Van Beelen 1994.

justice to this intent.⁴⁶ It seems illogical to apply an international convention to a part of a transport contract that would not have been covered by the said convention if it had been contracted for separately. Since a transport from Amsterdam to Utrecht is not governed by the CMR, nor is so-called ‘horseshoe’ transport from Alphen aan den Rijn in the Netherlands via Como in Italy back to Alphen aan den Rijn; such transport should also not be governed *ex proprio vigore* by the CMR if it forms part of a larger multimodal transport.⁴⁷ Since the *Rechtbank* chose to consider the transport stages of the contract separately by determining that the CMR did not apply to the sea stage unless the cargo remained on the trailer, logic dictates that the various road stages should also be considered separately.

There is a limit to the uniformity of law which treaties can or should achieve.⁴⁸ Van Beelen surmises that it is very probable that no one would even have thought to apply the CMR to domestic road carriage provided for in a multimodal contract if the rules found in Article 2 had not been incorporated into the CMR.⁴⁹

Furthermore, applying the CMR to domestic road carriage would very likely create recourse problems for the multimodal carrier.⁵⁰ And, as a last but certainly not least objection, there is Article 17 CMR. This article determines that the carrier is liable for any loss of the goods and

⁴⁶ Even though the aim of legal uniformity causes the use of treaty law in all situations with an international element to be very alluring, this is a temptation that ought to be resisted in this case as the text of the CMR indicates that it is not intended to apply to domestic carriage. The fear of foreign national law is in itself not enough reason to stretch the scope of a convention beyond its intended boundaries. Van Beelen 1994, p. 49. Cf. Laurijssen 2004, pp. 569-570.

⁴⁷ Hof ’s-Gravenhage 29 September 1998, *S&S* 1999, 33.

⁴⁸ In *Quantum*, Lord Justice Mance determined to this end that: “*Although we do not have to decide the position in relation to such a leg in this case, there would also seem to me no incongruity if it were to be concluded that an initial or final domestic leg falls outside CMR, like any other domestic carriage.*” *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 *Lloyd’s Rep.* 25, *ETL* 2004, p. 535.

⁴⁹ Van Beelen 1994, p. 47.

⁵⁰ The most significant example here is the fact that the kilogram limitation may vary; under the CMR it is 8.33 SDR, while under the domestic law of the Netherlands it is approximately a third of that amount. German national law, on the other hand, makes use of the CMR limitation amounts (Article 414 HGB), as does the U.K.

for damage thereto occurring between the time when he takes over the goods and the time of delivery. If the taking over and delivery mentioned in Article 1 CMR were meant to be understood as being the very first taking over at the start of the multimodal carriage and the final delivery at the very end of the transport, Article 17 would cause the multimodal carrier's liability to be regulated by the CMR during all parts of the journey, even during the non-road stages. The prevailing opinion seems to be, however, that this is not the case.⁵¹

4.2.2 International road stages

A more generally accepted view is that the 'place of taking over' and the 'place of delivery' of the goods as referred to in Article 1(1) CMR are to be understood as referring to the start and end of the contractually provided or permitted road leg.⁵² The German Supreme Court, the Bundesgerichtshof or BGH, adopted this point of view in 1987. In this judgment the BGH explicitly declared the CMR applicable to a road stage performed under a multimodal contract. The contract was for carriage from Neunkirchen in Germany to Portadown in Northern Ireland, but only from Neunkirchen to Rotterdam was it to be carried out by road. Literally the BGH stated that: "*The CMR applies to the land stage of the carriage, as ensues from Article 1 of the Convention*".⁵³ *Vis-à-vis* the Northern Irish road stage of the transport between Belfast and

⁵¹ Ramming 1999, at p. 329 and Ramming 2007, p. 284.

⁵² *Quantum Corporation v Plane Trucking* [2002] 2 *Lloyds Rep* 25; Rb Rotterdam, 28 October 1999, *S&S* 2000, 35 (Resolution Bay); Rb Rotterdam 23 April 1998, *S&S* 2000, 10; OLG Köln 25 May 2004, *TranspR* 2004, p. 359, *VersR* 2005, 574; Rb Maastricht 28 May 2003, *S&S* 2004, 57; Rb Rotterdam 11 April 2007, *S&S* 2009, 55 (*Godafoss*); Rb Rotterdam 3 May 2006, *LJN* AX9359; *Datec Electronic Holdings Ltd v UPS Ltd* [2007] 1 *W.L.R.* 1325; Cour de Cassation 25 November 1995, *Bulletin des Arrêts de la Cour de Cassation* 1995, IV, pp. 248-249; Hof 's-Hertogenbosch 2 November 2004, *S&S* 2006, 117; Rb Antwerpen 23 September 1975, *ETL* 1976, 279; Rb Rotterdam 1 March 2001, *S&S* 2002, 89; Rb Rotterdam 15 May 2008, *LJN* BD4102.

⁵³ "*Für die Landstrecke gilt die CMR, wie sich aus Art. 1 des Abkommens ergibt*"; BGH 24 June 1987, *TranspR* 1987, pp. 447-454 at p. 447. In 2008 the BGH however explained that this judgment applied the CMR indirectly, namely by means of German national law, and not directly based on Article 1 CMR. BGH 17 July 2008, *TranspR* 2008, pp. 365-368.

Portadown, the BGH on the other hand determined that the CMR did not apply, as this road stage did not cross any borders.⁵⁴

Academic commentators, such as Hill and Loewe, had voiced their preference for this interpretation long before the 1980s and, over the years, support for this opinion has steadily grown.⁵⁵ Since carriage to and from the United Kingdom always involves sea, rail, or air carriage, due to its geographic situation, the English have concerned themselves with the scope of application of the CMR regarding multimodal carriage from the very beginning. Indeed, the very existence of the expansion of the CMR's scope in relation to roll-on/roll-off (ro-ro) carriage, which is found in Article 2 CMR, can be ascribed to the English delegation.⁵⁶ Against this backdrop Hill has remarked that, when there are no ro-ro operations, the CMR is to be applied only to the segments of the transit of a cross-Channel shipment if the segment concerns the crossing of an international frontier on a road vehicle.⁵⁷

Quantum

A more contemporary English example of the view that the CMR applies to the international road stages of multimodal transports can be

⁵⁴ Cf. BGH 17 May 1989, *TranspR* 1990, pp. 19-20, *NJW* 1990, pp. 639-640, *ETL* 1990, pp. 76-80; OGH Wien 19 January 1994, *TranspR* 1994, pp. 437-439; Rb Haarlem 16 March 2005, *S&S* 2006, 137; Rb Rotterdam 30 November 1990, *S&S* 1991, 56; Hof Den Haag 25 May 2004, *S&S* 2004, 126; *Princes Buitoni Ltd. v Hapag-Lloyd Aktiengesellschaft and Another*, [1991] 2 *Lloyd's Rep.* 383.

⁵⁵ Loewe 1975; Hill 1975, pp. 604-605. Some examples of the more contemporary sources are: Wilson 2004, p. 246; Mankabady 1983, p. 136 and perhaps Clarke 2003 *International carriage of goods by road*, p. 29.

⁵⁶ At the instigation of the English delegation the drafters expressed the wish to extend the application of the Convention by adding this article, since without it the Convention would be of little use to them: it would never apply to road transport in England. Haak 1986, p. 94.

⁵⁷ Hill 1975, pp. 604-605.

found in *Quantum v Plane Trucking*.⁵⁸ The case involved the loss of a consignment of hard disks owned by Quantum, which were to be transported by Air France from Singapore to Dublin under an air waybill. The disks were flown from Singapore to Paris by Air France without incident. At Charles De Gaulle airport the three pallets were unloaded from the aircraft. The second segment of the transit was to be a ro-ro movement from Paris across the Channel via England, Wales and the Irish Sea in order to reach Dublin. While being carried by road towards the Welsh port of Holyhead, the goods were stolen by the driver and a supervisor in the employ of Air France's subcontractor for the second stage, Plane Trucking. At the time of the theft the disks were on board the same trailer vehicle onto which they had been loaded in Paris. When Quantum sought compensation for the loss of the goods from Plane Trucking, Plane Trucking contended that by reason of a "Himalaya" clause on the reverse side of the air waybill issued by Air France, it was entitled to invoke the same limits of liability as were available to Air France.⁵⁹ Although Air France accepted liability, a dispute ensued concerning the grounds.

During the proceedings all parties agreed that the Warsaw Convention on carriage by air, which applied between Singapore and Paris, did not apply to the movement between Paris and Dublin. But, while Air France argued that its contract terms applied to this stage, the claimants advocated application of the CMR. Under the contractual provisions Air France would be able to invoke a limit of liability, whereas under the

⁵⁸ *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2001] 2 *Lloyd's Rep.* 133 and *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 *Lloyd's Rep.* 25, *ETL* 2004, p. 535. An interesting detail is that the question as to whether the CMR applied in this case actually touched upon both of the scope-of-application articles of the CMR. Although the attention of all parties involved in the proceedings was drawn to Article 1 CMR, Article 2 CMR played a part as well, albeit a minor one. As was mentioned only *en passant* in the judgments, the carriage across the Channel and the Irish Sea concerned ro-ro carriage.

⁵⁹ In general terms, a Himalaya clause is any clause in a bill of lading which seeks to extend to non-carriers any immunity, defence, limitation or other protection afforded to the carrier by law and/or the bill of lading. The clause takes its name from the *S.S. Himalaya* which starred in a decision by the English Court of Appeal; *Adler v Dickson (The Himalaya)* [1954] 2 *Lloyd's Rep.* 267.

CMR Air France could invoke no such thing due to the intentional theft by the driver, which caused any such invocation to be barred by Article 29 CMR.

At first instance, Mr Justice Tomlinson determined that one of the features of the CMR is that, as its full title suggests, and as Article 1(1) provides, it attaches to contracts rather than to carriage. Because of the attachment of the CMR to contracts, the judge insisted on considering the entire movement from Singapore to Dublin as a whole. After some deliberation he found that it was ‘essentially’ and ‘predominantly’ a contract for carriage by air, and that that which was true of the whole was also true of the parts.⁶⁰

Tomlinson’s take on this matter was vividly criticised by Clarke by means of an unusual but accurate metaphor. He commented that if the contract of carriage was characterised based on the distance between Singapore and Paris relative to the rest of the journey, this was like saying that a cocktail such as a Bloody Mary should be classified as non-alcoholic because it contains more fruit juice than vodka.⁶¹

On appeal the judgment was reversed. The Court of Appeal applied the accumulation principle and concluded that the contract in dispute was for carriage by road within the parameters of Article 1(1) CMR in relation to the ro-ro movement from Paris to Dublin, and that Air France’s own conditions were overridden accordingly to the extent that they would limit Air France’s liability.⁶² The Court distinguished two key aspects to the quandary encountered when interpreting the meaning of ‘contract for the carriage of goods by road in vehicles for reward’ in Article 1(1) CMR. The first was the extent to which the application of the CMR depended upon a carrier having obliged himself

⁶⁰ Clarke 2002 *JBL*. Assessing a contract in this manner was named ‘*Gesamtbetrachtung*’ by the Germans and was rejected by the German judiciary as unsuited for the appraisal of multimodal carriage contracts. BGH 24 June 1987, *TranspR* 1987, pp. 447-454.

⁶¹ Clarke 2005, p. 184.

⁶² “Viewed overall, contracts can by their nature or terms have two separate aspects, and the present, despite the length of the air leg, was in my view just such a contract.” *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 *Lloyd’s Rep.* 25, *ETL* 2004, p. 535, per Lord Justice Mance.

contractually actually to carry the goods by road, and whether options in the contract to carry the goods by another means were of influence in this matter. The answer to this question hung upon the force, in context, of the word ‘for’ in the reference in Article 1 CMR to a ‘contract *for* the carriage of goods by road’. The second was the extent to which a contract could be both for the carriage of goods by road, within the scope of Article 1, and for some other means of carriage to which the CMR did not apply.

With regard to the first aspect, the Court concluded that limiting the application of the CMR to situations where the carrier promised unconditionally to carry the goods by road and on a trailer would be contrary to the convention’s purpose of standardising the conditions under which this kind of carriage is undertaken.⁶³ It would exclude too many of the contemporary contracts of carriage, as these tend to contain options for alternative modes of performance, either in general or in relation to specific emergencies. When a carrier promises road carriage, but reserves the right to opt for some other means of carriage for all or part of the way, or leaves the means of transport open, or undertakes to carry the goods by some other means, but reserves the right to opt for carriage by road instead, the mere inclusion of extra options should not bar the application of the CMR when the carriage is performed by road. The permission contained in the contract provided the carrier with the power to determine the applicable legal regime. Such a contract should be considered a contract ‘for’ – in the sense of ‘providing for’ or ‘permitting’ – the carriage of goods by road which actually occurred under its terms.

Concerning the second aspect – whether or not a contract can be both for the carriage of goods by road and for some other means of carriage – it was submitted that the CMR would have been much clearer if it had contained a solution like that of Article 31 of the Warsaw Con-

⁶³ See also Rb Rotterdam, 24 January 1992, *S&S* 1993, 89.

vention on carriage by air.⁶⁴ The Court seemed to be of the opinion that it would have contained such a solution had it not been for the extension of the scope of application found in Article 2 CMR, which made this impossible.

The Resolution Bay

In 1999 the Dutch *Rechtbank* in Rotterdam decided a case involving a container of lamb meat that had been transported from New Zealand to Rotterdam by means of the ocean-going vessel *The Resolution Bay* and thence by road to Antwerp, Belgium.⁶⁵ After arrival it was established that the meat had thawed en route and gone bad. The *Rechtbank* Rotterdam decided that the CMR applied to the damage if the claimants could prove that the spoilage had occurred during the road stage between Rotterdam and Antwerp. In light of the question as to whether the Court had jurisdiction in this matter it commented:

“P&O as combined carrier of goods has chosen to perform the part of the transport between Rotterdam and Antwerp by vehicle by means of road, while the contract, as contained in the CT-document, provided it with the permission to do so. As a result the place of taking over of the goods as meant in Article 1(1) CMR is the place where P&O or the auxiliary P&O charged therewith has taken over the goods for carriage by road, which in this case is Rotterdam.”

As in *Quantum*, the Court deemed the CMR applicable to the – international – road stage, even though the contract did not specify, but only permitted, carriage by road for this part of the transit. In contrast to the

⁶⁴ Article 31 WC stems from 1929 and could have been used as a template to resolve the issue of scope if Article 2 CMR had not prohibited this. Like Article 38 MC, Article 31 WC determines that in the case of combined carriage performed partly by air and partly by any other mode of carriage, the provisions of the convention apply only to the carriage by air, and that nothing prevents the parties from inserting in the document of air carriage conditions relating to other modes of carriage.

⁶⁵ Rb Rotterdam 28 October 1999, *S&S* 2000, 35 (*The Resolution Bay*).

above-mentioned 1992 judgment,⁶⁶ this time the Court interpreted the place of taking over to mean the place where the goods were taken over for the carriage by road, instead of at the beginning of the transport as a whole.⁶⁷

4.3 Article 1 CMR: ‘contra CMR’

Although the BGH applied the CMR to multimodal road carriage by means of the network approach in the late 1980s and the early 1990s,⁶⁸ contemporary German legal literature defends a different point of view. The currently prevailing opinion among authors is that the scope of application defined in Article 1 CMR does not cover this type of carriage.⁶⁹ Many detailed objections to the application of the CMR to anything other than unimodal road carriage contracts, aside from those covered

⁶⁶ Rb Rotterdam 24 January 1992, *S&S* 1993, 89.

⁶⁷ Cf. Rb Rotterdam 11 April 2007, *S&S* 2009, 55 (*Godafoss*); In contrast: Hof ‘s-Hertogenbosch 2 November 2004, *S&S* 2006, 117; OLG Köln 25 May 2004, *TranspR* 2004, pp. 359-361.

⁶⁸ BGH 24 June 1987, *TranspR* 1987, pp. 447-454; BGH 17 May 1989, *TranspR* 1990, pp. 19-20; BGH 30 September 1993, *TranspR* 1991, p. 16-18.

⁶⁹ Basedow 1994 and Basedow 1999, p. 35. Older – and even some relatively recent – German case law seemingly shows that at least some of the German courts had a different take on the subject. BGH 24 June 1987, *TranspR* 1987, pp. 447-454; LG Bonn, 21 June 2006, 16 O 20/05; BGH 21 February 2008, I ZR 105/05. Even some scholars, such as Puttfarcken, are known to adhere to the opposing point of view. Puttfarcken 1997, p. 175. A recent judgment by the BGH has put an end to the debate, however, by determining that in its view the CMR does not apply to international road carriage which is part of a multimodal transport contract. BGH 17 July 2008, *TranspR* 2008, pp. 365-368.

through Article 2 CMR, have been raised, mainly in the last decade.⁷⁰ Until recently it was unclear where the German courts stood on this issue, although there were some cautious examples of courts that did apply the CMR to road carriage performed based on a multimodal contract, most likely in the wake of the 1987 and 1989 BGH judgments.⁷¹ However, the uncertainty has come to an end since July 2008, when the BGH ruled that the part of a multimodal contract of carriage that involves international road transport is not covered by the rules of the CMR if the road vehicle does not accompany the goods onto the other means of transport used.

4.3.1 BGH 17 July 2008

In May 2000, a Japanese manufacturer of copying machines contracted with a Japanese freight forwarder, who acted as carrier, for the carriage of 24 containers stowed with copiers from Tokyo to Mönchengladbach, Germany.⁷² The waybill that was issued for the carriage contained a clause granting the Tokyo District Court sole jurisdiction over any claims arising from the contract of carriage and a clause choosing Japa-

⁷⁰ There may be a connection between the emergence of the majority of the objections and the entry into force on 25 June 1998 of the TRG, the *Transportreformgesetz*. The TRG incorporated specific rules in Articles 452 through 452d HGB on the ‘*Frachtvertrag über eine Beförderung mit verschiedenartigen Beförderungsmitteln*’, the contract of carriage involving carriage by different means of transport. The German rules do not cover all multimodal carriage contracts but are restricted to those contracts of which the various stages would be covered by different rules of law had they been contracted for separately. (“...und wären, wenn über jeden Teil der Beförderung mit jeweils einem Beförderungsmittel (Teilstrecke) zwischen den Vertragsparteien ein gesonderter Vertrag abgeschlossen worden wäre, mindestens zwei dieser Verträge verschiedenen Rechtsvorschriften unterworfen,...” this requirement is found in Article 452 HGB.) It should be noted however that some writers, such as Koller, defended the restricted view of the CMR’s scope long before the TRG came into being. Koller 1989, pp. 769-775.

⁷¹ BGH 24 June 1987, *TranspR* 1987, pp. 447-454; BGH 17 May 1989, *TranspR* 1990, pp. 19-20; OLG Düsseldorf 29 September 2005, I-18 U 165/02; LG Bonn 21 June 2006, 16 O 20/05. In OLG Köln 25 May 2004 (*TranspR* 2004, pp. 359-361) the CMR was applied to an international road stage of multimodal transport, but the OLG did so only because English law applied to the claim.

⁷² BGH 17 July 2008, *TranspR* 2008, pp. 365-368.

nese law as the law applicable to the contract. The containers were carried by sea from Tokyo to Rotterdam. In the port of Rotterdam the containers were transferred onto the trailers on which they were to be transported by road to Mönchengladbach. For this road transport a CMR consignment note was issued. One of the containers, however, failed to reach its destination unscathed. After it was taken over for carriage by road, but before it had even left the port area, the container was perforated by a large steel pole, damaging many of the 50 copiers inside.

After the LG Mönchengladbach had rejected the claim for compensation by the cargo interests' insurance company, as it could not sufficiently prove that it was authorised to claim, the OLG Düsseldorf judged the *Speditiionsunternehmen* liable for the damage based on the CMR.⁷³ The OLG established that the CMR applied to the claim because the accident had occurred after the international road carriage from Rotterdam to Mönchengladbach had started and it deemed the CMR applicable to any international road carriage performed based on a contract for carriage, even if the said carriage contract also involved carriage by other modes such as, in this case, carriage by sea.

The BGH reversed the judgment of the OLG and rejected the claim as inadmissible, since it was of the opinion that German courts lacked jurisdiction regarding this claim. Unlike the OLG, the BGH did not deem the CMR directly applicable to the road carriage leg of the multi-modal transport contract, following the opinion generally supported by the German legal literature.⁷⁴ Nor did it find that the CMR applied indirectly by means of Articles 452 or 452a HGB, as the parties had chosen Japanese law as the governing law for the contract and this prevented these articles of German national law from exerting influence on the matter.

⁷³ OLG Düsseldorf 29 September 2005, I-18 U 165/02.

⁷⁴ The BGH referred to: Koller 2004 *Transportrecht*, Article 452 HGB comment 19, Article 1 CMR comment 5 and 6; Koller 2004 *TranspR*; Herber 2006; Ramming 1999; Basedow 1997, Article 2 CMR comment 1; Fremuth 1994, comment 51; Drews 2003; Erbe & Schlienger 2005; Rogert 2005, pp. 15, 117; Mast 2002, pp. 185, 193; Herber/Piper 1996, Article 1 comment 45, Article 2 comment 6.

Hence, since the CMR did not apply, Article 31 CMR could not confer jurisdiction on the German courts. Therefore the Brussels I Regulation on jurisdiction applied, which granted exclusive jurisdiction to the Tokyo District Court, since there was a choice-of-forum clause thereto in the waybill.⁷⁵

The BGH gave several reasons for its decision, but admitted that the wording of the scope-of-application articles did not compel such an interpretation. Its first reason was the phrase ‘contract for the carriage of goods by road’ found in Article 1 CMR. This description indicated, according to the BGH, a contract for carriage solely by road. Secondly, the BGH pointed out that the CMR contains a provision specifically dealing with multimodal transport, namely Article 2 CMR. The existence of this Article was cause for the BGH to reason that the CMR applies to multimodal carriage contracts insofar as they are covered by Article 2 CMR, but no farther. The third reason brought to bear by the BGH was found in the Protocol of Signature of the CMR, which states that the drafters of the CMR intended to create a separate treaty to regulate multimodal carriage.⁷⁶ For that reason the BGH deemed the intent of the designers of the CMR to have been to refrain from regulating any or all parts of a multimodal contract. The purpose of the CMR, which is to harmonise the rules for the international carriage of goods by road, did not hamper this point of view, as this purpose relates to unimodal road carriage and mode-on-mode carriage involving road vehicles only.

It appears that the German legislator also adheres to this view of the scope of the CMR, since the German legislation refers to the hypothetical ‘*Teilstreckenrecht*’, which is the law that *would have* applied to carriage by the leg of the transport in question *if it had been* unimodal,

⁷⁵ In addition, neither of the litigants was domiciled in a Member State of the European Union. See Articles 1, 4 and 23(3) Brussels I Regulation.

⁷⁶ Haak 1986, p. 95 footnote 31.

in Article 452a HGB.⁷⁷

4.3.2 Godafoss

In the Netherlands the Godafoss case was, until recently, an advertisement for the less extensive ‘pro CMR’ point of view. At first instance the *Rechtbank* Rotterdam confirmed once again the views concerning the CMR presented in *The Resolution Bay*.⁷⁸ A shipment of salted fish had been stolen during road transport from Rotterdam to Naples, Italy. Since the road stage was international the CMR was applied, even though the road carriage was part of a larger transport from Reykjavik in Iceland to Naples, which also included sea carriage. That the means of transport to be used between Rotterdam and Naples had not been specifically agreed was no obstacle to the application of the CMR according to the *Rechtbank*. Based on the contract the carrier was permitted to carry the shipment by road, which caused the road stage to fulfil the conditions set by Article 1(1) CMR. The Hof Den Haag decided otherwise on appeal however.⁷⁹ Referring to the BGH’s 2008 judgment, the Hof deemed the CMR inapplicable for the following reasons. Firstly, the CMR might not explicitly exclude multimodal transport in Article 1(1), but neither did it explicitly include it. Secondly, Article 2 CMR expressly presents a specific type of multimodal transport as coming

⁷⁷ Furthermore, the BGH felt the need to explain that, although the English Court of Appeal had listed the BGH’s previous judgments stemming from 1987 and 1989 as supporting its expansive view of the scope of the CMR in *Quantum*, in fact these judgments did not support the views expressed in *Quantum* at all. In both judgments German national law applied to the multimodal contracts of carriage as they were concluded by German parties, although this was not expressly mentioned in the judgments. The CMR was as a consequence applied indirectly, in that the CMR’s liability rules were applied since they were part of the German legal sphere. There was no question of an autonomous application of the CMR, however. Koller had already implied as much in 2004 in a reaction to a judgment by the OLG Köln: “*Der BGH hat zwar die Teilstrecke eines internationalen Kfz-Transportes der CMR unterworfen. Er hat dies jedoch auf der Grundlage des deutschen Rechts getan, weil der multimodale Beförderungsvertrag aus der Sicht des deutschen Rechts einen gemischten Vertrag darstellt.*” Koller 2004 *Transpr*, p. 361.

⁷⁸ Rb Rotterdam 11 April 2007, *S&S* 2009, 55 (*Godafoss*).

⁷⁹ Hof Den Haag 22 June 2010, *S&S* 2010, 104 (*Godafoss*).

within the extended scope of the convention's application. Thirdly, the Protocol of Signature also argues against autonomous application of the CMR, as the drafters clearly had not seen the CMR as a regime that was sufficiently balanced to regulate multimodal transport in general. Fourthly, the Hof determined that the English *Quantum* decision should not be followed as it was founded on references to case law that did not unambiguously indicate that the CMR was applicable. There were therefore no pressing reasons to deviate from the BGH's point of view and, moreover, uniform interpretation of the convention was in the best interest of international trade. Furthermore, the Hof argued that the rules on jurisdiction found in the CMR present a practical obstacle to its application in multimodal transport, as they confer jurisdiction on the 'place of taking over' and the 'place of delivery'. If attached to the road carriage, these places might not always coincide with the beginning or end of the entire transport, which would create jurisdictional havoc and uncertainty. Therefore, an exclusive choice of forum, such as was made in the carrier's terms and conditions in this case, should be possible in multimodal transport.⁸⁰ In connection with this the Hof mentioned the Rotterdam Rules with their 'limited network system', which it alleged support such an exclusive choice.

However, there are two problems with this reference to the Rotterdam Rules. Firstly, these Rules have not yet entered into force. Secondly, even if they had entered into force, the Rotterdam Rules would only have allowed such an exclusive choice of forum in the case of volume contracts (*i.e.*, contracts of carriage that provide for the carriage of a specified quantity of goods in a series of shipments during an agreed period of time).

The reasoning concerning Article 2 CMR is also not entirely convincing. It is obvious that Article 2 CMR extends the scope of application of the CMR. The article is, after all, meant to expand the application of the convention beyond mere international road carriage: based on this article the CMR equally applies to the sea or rail stage of a ro-ro trans-

⁸⁰ Especially considering the possibilities for damage to be caused during more than one transport stage and unlocalised loss.

port and to any domestic road stages the transport may entail. This does not mean that the application of the CMR to international road carriage which is part of a multimodal contract by means of Article 1(1) CMR is an expansion of the convention's scope, as the convention is meant to regulate international road carriage. The statement in the Protocol of Signature is also not a reason to curtail the application of the CMR on the same grounds. The CMR was never meant to regulate entire multimodal transports, it was merely meant to uniformly regulate international road carriage, whether part of a larger contract or not.

The fourth reason given by the Hof, the need for uniform interpretation is not as easily countered. The need for uniform interpretation indeed requires courts of law to look at how the other Member States of a convention interpret its provisions. The difficulty here, however, is that the other Member States provide a rather divergent spectrum of decisions. The one reason to choose the BGH's views over those of the English Court of Appeal is that the BGH is a supreme court, whereas the Court of Appeal is not.

4.4 Article 2 CMR: the ro-ro expansion

Article 2 CMR expands the CMR's scope of application beyond mere road carriage. The article determines that where the vehicle containing the goods is carried over part of the journey by sea, rail, inland waterway or air, and the goods are not unloaded from the vehicle, the CMR shall nevertheless apply to the entire transport. When however it is proved that any loss, damage or delay in delivery of the goods which occurs during the carriage by the other means of transport was not caused by act or omission of the carrier by road, but by some event which could only have occurred in the course of, and by reason of, the carriage by that other means of transport, the liability of the carrier by road shall not be determined by the CMR. Under such circumstances the liability of the carrier is governed by the 'conditions prescribed by law' for the hypothetical contract of carriage for the non-road stage alone. If there are no such conditions however, the CMR is to be applied.

4.4.1 The Gabriele Wehr

The main pitfall of Article 2 CMR seems to be the interpretation of the words ‘conditions prescribed by law’. In *The Gabriele Wehr*, the *Hoge Raad*, the Dutch Supreme Court, was asked to clarify the Dutch point of view.⁸¹ Four trailers stuffed with Volvo parts were stowed on the deck of the vessel *The Gabriele Wehr*, which carried them from Göteborg, Sweden to Rotterdam under a non-negotiable waybill. During this sea stage, which was part of a larger transport, as the trailers came from various places in Sweden and were to be delivered in Born in the Netherlands, the vessel encountered a storm and the vehicle parts were damaged. The cargo underwriters promptly sued the road carrier for compensation under the CMR, whilst the latter invoked the ‘perils of the sea’ defence under the Hague-Visby Rules. In response the *Hoge Raad* approached the interpretation of the terms ‘conditions prescribed by law’ objectively.⁸² Because there was no international consensus in either legal literature or case law concerning the questions posed, and since the *travaux préparatoires* were not available to serve as reference, the *Hoge Raad* deemed the purpose and import of Article 2(1) CMR to be decisive.⁸³ As a result the *Hoge Raad* determined that ‘conditions prescribed by law’ were systems of objective transport law. These ‘objective’ transport regimes sometimes left room for contractual deviation, however, especially the Hague-Visby Rules. The lack of a bill of lading, for instance, or an agreement to carry on deck would normally cause them to be inapplicable to the sea carriage.⁸⁴ The objectifying approach of the *Hoge Raad* countered this unwarranted effect. In order to protect the shipper, who had no part in the contract of carriage concluded between the road and the mode-on-mode carrier, an abstract form of the actual mode-on-mode carriage contract had to be considered. The

⁸¹ HR 29 June 1990, *S&S* 1990, 110 (*The Gabriele Wehr*).

⁸² Such an approach is also advocated by Czapski: Czapski 1990, pp. 176-177.

⁸³ Articles 31, 32 and 33(4) of the Vienna Convention on the law of treaties support this. Haak (W.E.) 1990, pp. 328-329.

⁸⁴ Ro-ro operators generally issue non-negotiable receipts, not bills of lading. Haak (W.E.) 1990, p. 328.

relevant proviso of Article 2 CMR deemed the hypothetical contract to be “*a contract for the carriage of the goods alone ... made by the sender with the carrier by the other means of transport*”, which made it obvious that the hypothetical contract was not the existing contract between the carriers, and that the content and the specifics of this existing contract should not determine the hypothetical contract.⁸⁵

By objectifying the exception in Article 2(1) CMR, which is a special manifestation of the network system, special requirements set by the other unimodal carriage regimes, such as the issuance of a bill of lading, do not have to be met. Thus the *Hoge Raad* prevented the CMR rules from applying to the entire transport in all instances involving ro-ro carriage, which would have rendered the exception nearly useless. The CMR’s aim of unifying the liability of the road carrier was thereby achieved to a certain degree, the recourse option was – partially – preserved⁸⁶ and the shipper was prevented from having to cope with conditions and exceptions stemming from contracts he was not party to.⁸⁷

In Germany there seems to be less clarity concerning the meaning of the terms ‘conditions prescribed by law’. Koller for one refers to more than four different opinions, one of which is the Dutch approach in *The Gabriele Wehr*.⁸⁸ Basedow and Loewe concur with the Dutch *Hoge Raad*

⁸⁵ See also: Herber 1994, p. 381.

⁸⁶ Glass 2000, p. 579; Bombeeck, Hamer & Verhaegen 1990, p. 143; Haak 2005, p. 308.

⁸⁷ A few years after *The Gabriele Wehr*, the *Rechtbank* Rotterdam showed in its judgment in *The Duke of Yare* that the objective approach propagated by the *Hoge Raad* had taken hold. Although the general approach of the *Hoge Raad* was followed by the *Rechtbank*, *The Duke of Yare* also showed that the details of the mode of operation set out in *The Gabriele Wehr* were still in need of some clarification. As a starting point the *Rechtbank* followed the *Hoge Raad* by not projecting the mode-on-mode carriage contract onto the hypothetical contract. The *Rechtbank*’s second step, however, was to request the parties to furnish evidence concerning the contract of carriage that the shipper and the mode-on-mode carrier would have entered into had they contracted for the carriage of the goods alone. Thus the *Rechtbank* inserted a subjective element into the mix, which seems questionable in light of the *Hoge Raad*’s intent to objectify the issue. Rb Rotterdam 1 July 1994, S&S 1995, 99 (*The Duke of Yare*). See also Van Beelen 1997.

⁸⁸ Koller 2007, pp. 1162-1163, Article 2 CMR comment 8. Helm also adheres to the approach in *The Gabriele Wehr* of the Dutch *Hoge Raad*. Helm 1979, p. 440 comment 5.

and reject the use of the mode-on-mode contract as the template for the hypothetical contract. They argue that the specifics of the mode-on-mode contract should be disregarded because this would enable the road carrier to invoke exceptions to his liability which stem from the contract between him and the mode-on-mode carrier to which the shipper is not party, and which he therefore is unable to influence.⁸⁹

Mankowski on the other hand is of the opinion that consistently applying the objective approach takes matters too far. Although, as in *The Gabriele Wehr*, he deems it sufficient for the ‘conditions prescribed by law’ to be binding for only one of the parties, he also thinks that applying the Hague-Visby Rules when no bill of lading has been issued, or would have been likely to have been issued if the sender had contracted for the carriage of the goods alone with the mode-on-mode carrier, is contrary to the scope-of-application rules of the uniform instrument itself and thus unacceptable. Thus, as the relatively least harmful option, he encourages the road carrier to request a bill of lading from the mode-on-mode carrier, as in his view such a bill is a prerequisite for the application of regimes such as the Hague-Visby Rules.⁹⁰ In practice, however, such a request seems less than feasible.⁹¹

A precursor of the objective approach taken in *The Gabriele Wehr* was a case decided by the LG Köln in 1985. The LG established that “*auch der tatsächlich zwingende, von der Fährgesellschaft unabänderbar vorgegebene Vertragsinhalt zugunsten des Straßenfrachtführers berücksichtigt werden müsse*”, and that therefore a bill of lading was

⁸⁹ Basedow 1997, p. 913. Loewe 1976, p. 524. This point of view is shared by Czapski. Czapski 1990, p. 176. For comparison: in multimodal transport the multimodal carrier is also not allowed to invoke conditions against the consignor stemming from the contract between him and the actual carrier. OLG Hamburg 10 April 2008, *TranspR* 2008, pp. 213-218.

⁹⁰ Mankowski 2004, p. 1060, Rz. 1409.

⁹¹ Quantum, for instance, would have had to ask the unidentified sea carrier to issue bills of lading for the ro-ro stages of the contracted transport across the Channel and the Irish Sea. It seems unlikely, however, that Quantum either had, or wanted, any contact with the subcontracting carriers. *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2001] 2 *Lloyd's Rep.* 133 and *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 *Lloyd's Rep.* 25, *ETL* 2004, p. 535.

not required.⁹²

Clarke establishes that, as in Germany, the English views on this subject are not exactly homogeneous. To illustrate this he makes mention of three views: the concept that the hypothetical contract should be based on the contract between the carriers; the approach taken in *The Gabriele Wehr*; and a third possibility which proceeds from the perspective that the proviso is the exception whereas the application of the CMR is the rule. As such the exception should be strictly construed, meaning that the CMR rules apply unless a case falls clearly within the proviso. This is a solution that he admits was rejected by the Dutch *Hoge Raad* in *The Gabriele Wehr* and by a French court in 1986.⁹³

In Belgium, the Antwerp *Rechtbank van Koophandel* chose to follow the objective approach in 2000. This meant determination of the content of the hypothetical contract *in abstracto*. Because objective construction is intended to protect the consignor, who was not able to negotiate conditions concerning the carriage by the other mode, the *Rechtbank* determined that the non-road carriage regime needed to be applied without taking into account the specific circumstances of the case.⁹⁴

All in all, the objective approach taken in *The Gabriele Wehr* seems the pre-eminent solution to an issue that causes much dissension. It is analogous to the commonplace model of a reference to foreign law minus the conflicts rules of the said legal system.⁹⁵ Yet it has the disadvantage of not ensuring that the regimes governing the main contract and the sub-contract are aligned. Recourse actions by the CMR carrier against the mode-on-mode carrier may therefore fail to generate sufficient recompense. Nevertheless, it seems better than applying the CMR when no bill of lading has been issued or when carriage on deck has been agreed, as is apparently the practice of the French courts, since this causes the chances of recourse problems to be even greater.⁹⁶

⁹² LG Köln 28 May 1985, *VersR* 1985, p. 985. Herber 1994, p. 379.

⁹³ Clarke 2003 *International carriage of goods by road*, p. 42.

⁹⁴ Rb van Koophandel Antwerpen 25 February 2000, *ETL* 2000, pp. 527-540.

⁹⁵ Clarke 2003 *International carriage of goods by road*, p. 42.

⁹⁶ Cour d'appel de Paris 23 March 1988, *ETL* 1990, pp. 221-226 and Cour de cassation de France 5 July 1988, *ETL* 1990, pp. 227-228 (*Anna Oden*).

4.5 The love/hate relationship between multimodal transport and the CMR

Multimodal carriage and the CMR do not seem able to cope with existing either together or apart. Nevertheless, the only thing that is crystal clear at this point is that there is nothing resembling a general consensus on the scope of application of the CMR concerning multimodal transport. Both Articles 1 and 2 CMR have long been the subject of debate and disagreement. Since there is no international court which has a final say in CMR matters – the ECJ recently clarified that it is not authorised to assess the content of the CMR – this is not likely to improve in the future.⁹⁷

5 The ‘multimodal’ scope of the CMNI and the COTIF-CIM

As their terminology is very similar to that of the CMR, the basic scopes of application of both the CMNI and the COTIF-CIM raise questions akin to those flowing from Article 1(1) CMR. Whether the terms ‘contract to carry goods by inland waterway against payment of freight’ or the words ‘contract of carriage of goods by rail for reward’ can be considered to include inland waterway or rail carriage that is only part of a multimodal contract, is just as uncertain as under the road carriage convention. Due to the strong parallels, a mere referral to the situation outlined above concerning the CMR seems to be sufficient here. Besides the basic scope of application – international inland waterway and rail carriage – both conventions also cover specifically defined types of multimodal transport. The CMNI is less adventurous than its rail carriage cousin however. According to Article 2(2) CMNI, carriage without transshipment, both on inland waterways and also in waters to which maritime regulations apply, is governed by the inland waterway regime.

⁹⁷ ECJ 4 May 2010, case 533/08, (*TNT Express Nederland B.V. v AXA Versicherung AG*)

Provided, that is, that the distance to be travelled in waters to which maritime regulations apply is the smaller and that no maritime bill of lading has been issued in accordance with the applicable maritime law. This last condition is likely to cause conflict between the CMNI and the sea carriage conventions, such as the Hague and Hague-Visby Rules, which only apply if such a document has been issued. The Hamburg Rules do not require a document to be issued in order to apply to sea carriage, however. Here the condition that the sea stage of the transport must be shorter than the inland waterway stage may be of use to avert conflict. Nevertheless, if the sea stage is not insignificant enough to be 'absorbed' by the inland waterway carriage, both the Hamburg Rules and the CMNI will apply to the sea stage of the transport.⁹⁸

An additional, if less obvious, extension of the CMNI's scope of application beyond actual inland waterway carriage can be found by combining Article 16(1) CMNI, which states that the carrier is liable for loss resulting from loss or damage to the goods caused between the time when he took them over for carriage and the time of their delivery, and Article 3(2) CMNI, which determines that the contracting parties can agree that the taking over and/or delivery of the goods shall not take place on board the vessel. Since the CMNI applies to 'any contract of carriage according to which the port of loading or the place of taking over of the goods and the port of discharge or the place of delivery of the goods are located in two different States', and a 'contract of carriage means any contract, of any kind, whereby a carrier undertakes against payment of freight to carry goods by inland waterway', there is some small scope for bringing other modes of transport under the influence of the CMNI. If, for instance, the parties agree that the goods are to be taken over at the premises of the consignor, and delivered after road and inland waterway carriage at the premises of the consignee, the pre- and end-haulage by road could be covered by the CMNI.

⁹⁸ The Hamburg Rules are just as explicit as the Montreal Convention on their stance regarding sea carriage that forms part of a multimodal transport. According to Article 1(6) Hamburg Rules, a contract which involves carriage by sea and also carriage by some other means is deemed to be a contract of carriage by sea for the purposes of the convention only in so far as it relates to the carriage by sea.

It seems prudent, however, to interpret this extension as very limited. To cause it to extend the CMNI beyond those preceding and subsequent non-inland waterway transports that are so supplementary in nature that they can be 'absorbed' by the inland waterway carriage is unwarranted, as this would mean applying the inland waterway convention to non-inland waterway carriage. And even though the CMNI refers to 'the law of the State applicable to the contract of carriage' for the period before loading and the period after discharge, application of these rules by means of the CMNI is an awkward solution. In particular since extending the CMNI's influence to include independent stages of non-inland waterway transport would mean that international transport stages would also be included, and such transport might well already be governed by its own international regime. Such an interpretation would therefore cause potential conflict between the CMNI and other carriage conventions, which its drafters presumably did not intend. It is most likely that the extension to non-inland waterway carriage that is not of a completely subsidiary nature was not intended to go beyond the combination of inland waterway and sea transport referred to in Article 2(2) CMNI.

Like the CMR and the CMNI, the COTIF-CIM also expands its scope of application to carriage by other transport modes. Yet, unlike under the other two conventions, transshipment does not bar the application of COTIF's CIM appendix. As long as a contract for international carriage involves rail transport supplemented by internal transport by road or inland waterway, carriage by sea or transfrontier carriage by inland waterway, Article 1(3) and (4) causes the CIM to apply to both the rail and non-rail transport.

Despite this extended scope of application, a conflict between the CIM and either the sea carriage regimes or the CMNI is unlikely to ensue. This is because the expansion of the application of the CIM rules to sea or international inland waterway carriage is only effectuated when the said carriage is performed on services included on a very limited list.⁹⁹ Conflict between the CMR and the CIM seems more feasi-

⁹⁹ This list of services can be found at www.otif.org.

ble, however. According to the explanatory report on the CIM 1999, the fact that the carriage in question is to 'supplement' the transfrontier carriage by rail means that the principal subject-matter of the contract of carriage must be transfrontier carriage by rail.¹⁰⁰ It has therefore been suggested that, in order to avoid conflict with the CMR, internal road transport that is 'supplemental' to the rail carriage must be considered to be of a completely subsidiary character and as such 'absorbed' by the rail carriage.¹⁰¹ This seems an untenable position, however, as the ordinary meaning of the word 'supplementary' is 'something provided in addition to something else in order to improve or complete it', which suggests a separate entity, not something to be absorbed.¹⁰² As a result conflicts with the CMR may occur on occasion. Article 2 CMR also may cause conflict between the CMR and the CIM in relation to the rail stage of a ro-ro transport; Article 1(3) CIM would have the same effect concerning any internal road stages.

Besides the potential for conflicts, the annexation of domestic transport stages by the CIM has the potential to cause further mayhem. A less warranted side-effect of the pursuit of uniformity by those drafting the CIM is that it causes recourse gaps. If, for instance, damage or loss occurs during supplemental domestic road carriage that fulfils the requirements of Article 1(3) CIM, the multimodal carrier will be liable to the cargo interests up to the amount of 17 SDR per kilogram based on the CIM. The subcarrier, who may actually have performed the road carriage, is on the other hand not bound by the CIM, but rather by the applicable national regime. If this is Dutch law this means that the multimodal carrier will receive no more than EUR 3.40 per kilogram in compensation from the subcarrier, which leaves him to cope with a loss of approximately EUR 15.30 per lost or damaged kilogram.¹⁰³

¹⁰⁰ Explanatory report COTIF-CIM, www.otif.org, p. 12.

¹⁰¹ Koller 2007, p. 1746.

¹⁰² Oxford Advanced Learners Dictionary, www.oxfordadvancedlearnersdictionary.com.

¹⁰³ For the SDR EUR exchange rate see www.imf.org.

6 The ‘multimodal’ scope of the Montreal Convention

The Montreal Convention’s initial attempt to demarcate its scope of application can be found in Article 1 MC. The scope of the instrument is not solely restricted to the transport of goods: the regime governs passenger transport as well, as can be derived from Article 1(1) MC, which determines that its regulations apply to all international carriage of persons, baggage or cargo performed by aircraft for reward. If gratuitous carriage by aircraft is performed by an air transport undertaking, however, the reward condition is waived.

In Article 1(2) MC the explanation of what is meant by ‘international carriage’ shows that, although this is not explicitly mentioned in Article 1(1) MC, the convention presupposes the existence of an agreement, a contract of sorts, on which the carriage is based.¹⁰⁴ As Mance LJ commented in *Western Digital v British Airways*: “While it is clear that in certain respects the Convention scheme provides general rules rather than merely statutory contractual terms, it is also clear that the draughtsmen had very much in mind as a premise to its application the existence of a relevant contract of carriage”.¹⁰⁵

Thus, the most prominent conditions for the application of the air carriage convention in Article 1 of the convention are: (a) the existence of an agreement; which concerns (b) international carriage; of (c) cargo (or persons or baggage); and which (d) is to be performed by aircraft.

¹⁰⁴ Koning 2007, p. 60; Giemulla & Schmid *Warschauer Abkommen*, Article 1 WC, No. 27.

¹⁰⁵ Comment by Mance LJ in *Western Digital Corporation v British Airways plc*, [2000] 2 Lloyd’s Rep. 142, par. 42. Mance made a similar comment in the *Quantum* appeal (*Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 Lloyd’s Rep. 25, ETL 2004, pp. 535-560): “...it is worth noting that the Warsaw Convention also contemplates an agreement: see in particular art. 1(2) (whereby ‘the expression international carriage means any carriage in which, according to the agreement between the parties...’) and art. 5(2) (whereby the absence, etc. of an air waybill ‘does not affect the existence or validity of the contract of carriage which shall (...) be none the less governed by the rules of this Convention’)...”

Besides the basic scope-of-application provision in Article 1 MC there are two more provisions that influence the multimodal scope of application of the Montreal Treaty. The first is Article 38 MC, which prescribes the use of the network system, at least for the international air stages in carriage contracts. The article states that in the case of combined carriage performed partly by air and partly by any other mode of carriage, the provisions of the convention shall apply only to the carriage by air, provided that the carriage by air falls within the terms of Article 1 MC. As the provision itself also states that it is subject to Article 18(4) MC, the exact period of the carriage by air is demarcated by that provision. It is this last provision that is the second factor worthy of mention in relation to the Montreal Convention's multimodal footprint. The result is that the rules of the air carriage convention do not apply to any stage of a combined carriage contract that does not fulfil the conditions of Article 1 MC.¹⁰⁶ In principle, it excludes carriage by all means of transportation other than aircraft and all carriage not by air.

6.1 The period of the carriage by air

Based on Article 18(4) MC, however, 'carriage by air' under the convention extends beyond actual carriage by air – and sometimes even beyond carriage by aircraft.

The first sentence of the provision starts off somewhat conservatively by stating that the period of the carriage by air – which demarcates the boundaries of the Montreal regime according to Article 38 MC – does not extend to any carriage by land, sea or inland waterway performed outside an airport. Procedures and activities incidental to movement, such as the period of waiting within the confines of the airport before an aircraft can take off, are generally accepted as carriage by air, and probably would have been even without the words of Article 18(4) MC.

¹⁰⁷ The second and third sentences of Article 18 (4) MC contain certain

¹⁰⁶ Ramming 1999, p. 328.

¹⁰⁷ Carriage by air thus includes slightly more than the actual flight: it also includes activities that are closely linked to the flight, such as taxiing *etc.*

exceptions to this rule and extend the period of carriage by air even beyond the airport's boundaries in special circumstances. It is these exceptions, and the fact that the first sentence only excludes non-air carriage outside an airport, that cause the 'period of the carriage by air' to extend beyond actual air carriage by aircraft. Thus Article 18(4) MC extends the scope of application of the Montreal Convention.¹⁰⁸

6.1.1 Unlocalised loss: loading, delivery and transhipment

The first alleged expansion results from the second sentence of Article 18(4) MC,¹⁰⁹ which reads: "If, however, such carriage takes place in the performance of a contract for carriage by air, for the purpose of loading, delivery or transhipment, any damage is presumed, subject to proof to the contrary, to have been the result of an event which took place during the carriage by air."

This presumption is meant to relieve the party that suffered damage or loss from the onerous task of having to prove that the damage was caused by an event which occurred during the carriage by air and not by an event which occurred before or after the air carriage.¹¹⁰ The text

¹⁰⁸ If the condition that the carriage is to be performed by aircraft in Article 1 MC could not be mitigated, the texts of Articles 1, 38 and 18 would be inconsistent and Article 18(4) MC would serve no purpose other than to confuse. It is therefore reasonable to assume that, in the situations mentioned by Article 18(4) MC, the use of aircraft is not a necessity. This is supported by Article 18(2) of the original Warsaw Convention, and Article 18(4) WC HP MP4, which both determine that carriage by air is not necessarily always by aircraft, as it comprises the period during which the luggage or goods are in the charge of the carrier, 'whether in an aerodrome or on board an aircraft'. This paragraph literally states that the Warsaw rules should apply in an aerodrome or on board an aircraft. In other words, these circumstances do not have to coincide for the Convention to apply. In addition the jurisprudence clearly indicates that the purpose of the last two paragraphs of Article 18 WC and MC is to expand the period during which the carrier is liable for damage sustained to the goods beyond the period of actual flight. *Clarke v Royal Aviation* (1997) 34 *Ord.* (3d) 481, as cited in Clarke & Yates 2004, p. 320; OLG Frankfurt 21 April 1998, *TranspR* 1999, pp. 24-27; BGH 21 September 2000, *TranspR* 2001, pp. 29-34.

¹⁰⁹ In reality it is quite impossible to establish whether the Convention's scope is actually expanded by this provision or not, since it pertains to unlocalised loss. Because it is unknown where the loss or damage occurred, it could just as easily have been during the air carriage.

¹¹⁰ Giumulla & Schmid *Montreal Convention*, Article 18 MC, No. 92.

shows that effectuation of the presumption extending the scope of application of the convention's rules is subject to three conditions: (a) the carriage must take place during the performance of a contract for carriage by air; (b) the carriage must involve loading, delivery or transhipment outside an airport; and (c) there must be no proof that the damage occurred elsewhere. Since Article 38(2) MC states that the parties may insert conditions relating to other modes of carriage into the document of 'air carriage', the document relating to the entire transport remains an air carriage document even if the transport as a whole is multimodal. This indicates that the reference to a contract for 'air carriage' as meant in Article 18(4) MC includes multimodal contracts which provide for an international air stage.

Whether the carriage supplementing the actual air carriage can be categorised as loading, delivery or transhipment is sometimes difficult to determine. The terms themselves indicate that certain restrictions apply; the carriage involved can be no more than accessory.

Transhipment seems to be the easiest to demarcate. Only those transports that cause the goods to be carried between flights, from one airport to another are covered. Transhipment is generally thought to be limited to surface transport between two airports, and two air stages which are part of a single movement of goods, where the link cannot be made by air.¹¹¹

Loading and delivery, on the other hand, are more difficult to distinguish. In Germany these terms are deemed to cover only the pre- and end-haulage to and from the nearest airport suitable for the carriage of

¹¹¹ Clarke 2002 *Contracts of carriage by air*, p. 119; OLG Hamburg 11 January 1996, *TranspR* 1997, pp. 267-270 at p. 269. It seems somewhat arbitrary that the presumption applies to a transhipment between two airports if there is no scheduled air service between these airports, but does not apply to exactly the same carriage if there is a scheduled service. Perhaps a reason for this can be found in the existence of choice: in the first situation there is no choice but to carry by some other mode of carriage, but in the second situation the carrier could have decided to carry by air and deliberately decided not to do so.

the goods in question.¹¹² English and Dutch opinion can at least be said to recognise that such carriage as was performed by road in *Quantum* was too extensive to count as either loading or delivery.¹¹³

6.1.2 Unsanctioned substitution

The final extension of the period of carriage by air is found in the third sentence of Article 18(4) MC. If a carrier, without the consent of the consignor, substitutes carriage by another mode of transport for the whole or part of a carriage intended by the agreement between the parties to be carriage by air, such carriage by another mode of transport is deemed to be within the period of carriage by air. Like the unlocalised loss provision, however, this might not in reality be an actual extension of the Montreal regime. Based on the adage '*pacta sunt servanda*', the Montreal regime should in any case be applied to carriage that is substituted for the agreed air carriage without the consent of the consignor or consignee.¹¹⁴ Since a contract of carriage is a consensual contract, the content of the contract has generally been deemed decisive when it comes to the determination of the applicable legal rules.¹¹⁵

¹¹² OLG Karlsruhe 21 February 2006, *TranspR* 2007, pp. 203-209; Kirchhof 2007, p. 134; Giemulla & Schmid *Montreal Convention*, Article 18 MC, No. 88. OLG Düsseldorf 12 March 2008, I-18 U 160/07, www.justiz.nrw.de. The coverage of the Montreal Convention was not extended to the unlocalised loss of a shipment of metal bucket-like containers through Article 18(4) MC. The OLG applied German national law instead of the Montreal Convention based on its belief that the road carriage stages – the goods were carried first from groupage facilities in Germany to a 'HUB' airport by road, were then carried by air to a 'HUB' airport in America, from which they were carried to the consignees – did not concern either loading, delivery or transshipment.

¹¹³ Hof Amsterdam 6 May 1993, *S&S* 1994, 110; *Quantum Corporation Inc. and others v Plane Trucking Ltd. and Another*, [2002] 2 *Lloyd's Rep.* 25, *ETL* 2004, p. 535. Nevertheless, since the loss was localised in *Quantum*, the judgment does not provide as much insight into the English views as one might hope.

¹¹⁴ Van Beelen 1996, p. 74; Müller-Rostin 1996, pp. 967-978.

¹¹⁵ Koning 2007, p. 122; Haak 2007. For a different view see BGH 17 May 1989, *TranspR* 1990, pp. 19-20, *NJW* 1990, pp. 639-640, *ETL* 1990, pp. 76-80. Under the Warsaw regime the BGH decided that the '*Meistbegünstigungsprinzip*' should be applied: the air carrier was held liable for the damage based on the regime of one of the modes used in the carriage, namely the regime that was most beneficial to the claimant.

On the positive side, the clearly stated consequences of unsanctioned substitution promote legal certainty: there can be no misunderstanding as to the applicable legal regime. It seems correct for the carrier to be held accountable on the basis of the contracted-for regime, as this is the regime the shipper expected and on which he based his preparations, such as taking out insurance.¹¹⁶ There are situations, however, in which a carrier would profit from a breach of contract. The substituted carriage might, for instance, be cheaper, but also riskier for the cargo. In such a situation the cargo interests would in fact be worse off than if the carrier had adhered to the contract.¹¹⁷

7 The consequences of the Rotterdam Rules

The most prominent current sea carriage conventions, the Hague and Hague-Visby Rules, do not refer to multimodal transport in any way. Whether they apply to the maritime parts of a multimodal contract if a bill of lading is issued therefore remains unclear. The third sea carriage convention currently in effect, the Hamburg Rules, specifies that its rules apply strictly to the international sea carriage stage of a contract that also provides for non-maritime carriage. Although the Hamburg Rules have never equalled the success of the two Hague and Hague-Visby Rules, the regimes do exist alongside each other. The result is uncertainty as to the applicable law for sea carriage contracts. To remedy this situation UNCITRAL's Working Group III on transport law created the Convention on Contracts for the International Carriage of Goods

¹¹⁶ Kirchhof 2007, p. 138.

¹¹⁷ Added to this is the fact that the unbreakable Montreal liability limit may be reason to abuse this rule. If a carrier is, for instance, aware of the untrustworthiness of some of his employees, or perhaps suspects that the subcontractors he intends to employ are not completely reliable, he may decide to contract for air carriage with a shipper even if he in fact intends to carry by road or rail. If it then happens that one of his employees or his subcontractors steals the cargo, the carrier will be protected by the Montreal regime's unbreakable limit of 17 SDR per kilogram, instead of being forced to compensate the shipper for the entire loss as per the CMR.

Wholly or Partly by Sea, also known as the Rotterdam Rules. These Rules are intended to supplant the existing maritime regimes and aim to create a modern and uniform law concerning international carriage of goods that includes an international sea leg, but which is not limited to port-to-port carriage. The new rules are a ‘maritime plus’ instrument with a decidedly maritime liability regime.¹¹⁸ Although modern times seem to demand such a door-to-door regime, it also represents a risky endeavour. None of the past attempts either to extend the application of a sea carriage regime beyond the antiquated scope of ‘tackle-to-tackle’ or to implement a multimodal transport regime has been very successful thus far.¹¹⁹

Originally, the purpose of the new convention was to regulate, besides the international sea carriage leg, all parts of a multimodal transport that were not subject to an international mandatory regime of their own.¹²⁰ This latter objective was not wholly achieved, however. As it stands now, the convention also regulates parts of ‘wet’ multimodal transports that are already subject to mandatory regimes of uniform law.¹²¹ As a result, some of the drafters feared that its scope might conflict with existing unimodal regimes, particularly with the CMR and the COTIF/CIM.¹²² Therefore certain exceptions from the instrument’s overall uniform regime were considered necessary.

These exceptions are incorporated into the new regime by an arrangement that is described as a ‘minimal (or limited) network system’. This network arrangement is described as minimal with good reason, since it is limited to the subjects of the carrier’s liability, limitation of liability and time for suit. In all other areas covered by the Rules their provisions apply irrespective of any differing provisions in other potentially applicable conventions, barring some exceptions.¹²³

¹¹⁸ Faghfoury 2006, p. 107.

¹¹⁹ Diamond 2008, p. 135.

¹²⁰ A/CN.9/WG.III/WP.21, Article 4.2.1 and A/CN.9/510, p. 9, www.uncitral.org.

¹²¹ Haak & Hoeks 2004, p. 433.

¹²² M. F. Sturley, ‘Scope of coverage under the UNCITRAL Draft Instrument’, *JIML*, 2004-2, p. 146.

¹²³ A/CN.9/WG.III/WP.29, p. 21, par 72, www.uncitral.org.

In the early stages of drafting, the network provision caused the new Rules to give way to ‘provisions of an international convention’, ‘which according to their terms apply’.¹²⁴ This would have allowed the differing interpretations mentioned above concerning the scope of the CMR to continue to work their mischief. Since it would thus not have been the Rotterdam Rules that would have determined whether the relevant unimodal convention would have applied to a certain non-maritime part of the carriage, but the scope-of-application rules of the unimodal convention in question, the diversity of opinion as regards the law applicable to the road stages would have endured.¹²⁵ As a remedy, the part of the article which read ‘according to their terms apply’ was adapted.

7.1 The ‘minimal network’ of Article 26 RR

The current version of the minimal network system can be found in Article 26 RR, which states:

Article 26. Carriage preceding or subsequent to sea carriage

When loss of or damage to goods, or an event or circumstances causing a delay in their delivery, occurs during the carrier’s period of responsibility but solely before their loading onto the ship or solely after their discharge from the ship, the provisions of this Convention do not prevail over those provisions of another international instrument that, at the time of such loss, damage or event or circumstance causing delay:

(a) Pursuant to the provisions of such international instrument would have applied to all or any of the carrier’s activities if the shipper had made a separate and direct contract with the carrier in respect of the particular stage of carriage where the loss of, or damage to goods, or an event or circumstance causing delay in their delivery occurred;

¹²⁴ A/CN.9/WG.III/WP.56, www.uncitral.org. Circa 2005.

¹²⁵ Hoeks 2008, p. 269.

- (b) Specifically provide for the carrier's liability, limitation of liability, or time for suit; and
- (c) Cannot be departed from by contract either at all or to the detriment of the shipper under that instrument.

The text of subparagraph (a) now contains a fiction that ensures that the operation of the new Rules takes place independently of the scope-of-application provisions of other transport conventions.¹²⁶ The revision of the network provision is a step in the right direction compared to the previous versions, albeit a small one. Because of the fiction contained in the article, a small amount of uniformity has been created where before there was none. Under the final version of the new regime, the rules on carrier liability, limitation of liability and time for suit of the existing transport conventions are to supersede the rules of the 'maritime plus' instrument regardless of how their scope-of-application rules are interpreted in relation to multimodal carriage.

Unfortunately, the problem endures regarding the conflict between the provisions of the unimodal conventions that do not deal with the carrier's liability, limitation of liability, or time for suit and those of the new Rules. Whenever the loss can be localised and there is another mandatory international regime applicable to the transport stage that is the subject of dispute, the provisions dealing with liability, limitation of liability and time for suit of this international regime will apply to the claim for compensation, together with the remaining provisions of the Rotterdam Rules. In relation to the CMR, this means that if the court addressed deems the CMR applicable *ex proprio vigore* to road carriage

¹²⁶ There is a striking resemblance between the fiction in Article 26(a) RR and parts of Article 452 HGB, which is part of the German legislation on multimodal carriage. Article 452 HGB determines that if carriage of goods is performed by various modes of transport on the basis of a single contract of carriage, and if at least two of the (hypothetical) contracts would have been subject to different legal rules if "separate contracts had been concluded between the parties for each part of the carriage which involved one mode of transport", then the provisions of the German national law on affreightment in general will apply to the contract, unless the special provisions following after Article 452 or applicable international conventions provide otherwise.

under a multimodal transport contract, there is still room for conflict between the Rules and the CMR, as the CMR regulates a greater number of issues on a mandatory basis than the liability of the carrier, the limitation of liability, or time for suit alone, as do the Rotterdam Rules.¹²⁷

As a result an obscure patchwork of regimes that were not designed to complement each other, and which may very well conflict at times, will apply to the claim. This creates much room for confusion and it seems rather likely that the courts in different states, or even courts within the same state, will differ in opinion as to its operation. The results of Article 26 RR would therefore seem rather unpredictable.¹²⁸

An additional 'flaw' in the network approach of Article 26 RR is the clause that restricts its operation to damage to or loss of or delay of the goods that has occurred '*solely before their loading onto the ship or solely after their discharge from the ship*'. These words have the effect that damage that occurs during more than one stage of the transport is governed entirely by the Rotterdam Rules. Although this dilutes the 'purity' of the network approach even further, it is debatable whether this 'flaw' should be considered detrimental. Under the current legal framework, situations involving damage that occurs or was caused during multiple stages of a transport may cause the application of more than one carriage regime, at least if the damage cannot be divided up, or the different aspects of it cannot all be allocated to one specific transport segment. If the Rotterdam Rules can establish some uniformity and legal security in these often complicated situations by taking precedence, this solution may have some merit. Still, granting precedence to the new regime does not prevent one, or very likely more than one, of the existing carriage regimes from applying equally under these circumstances. Thus conflicts between the conventions are even more likely to occur when the damage or loss has occurred during more than one transport stage. Under these circumstances the limited network

¹²⁷ For one, both the CMR and the Draft contain rules on jurisdiction. For other examples see A/CN.9/WG.III/WP.29, www.uncitral.org, paras. 72-105.

¹²⁸ UNCTAD/SDTE/TLB/4, 13 March 2002, UNCTAD commentary on the Draft Instrument on Transport Law, www.unctad.org, p. 19.

approach does not grant precedence to even the rules on carrier liability, limitation of liability or time for suit of the other applicable conventions, which causes all of the mandatory rules of the other conventions to become sources of potential conflict.

An added uncertainty is that if the damage occurs during more than one stage of the transport, but the stages to which the damage can be ascribed are all non-maritime stages, the limited network approach will most likely cause the rules relating to these types of transport to take precedence over the Rotterdam Rules. This can be said to be ‘most likely’, but is by no means a certainty, as the text of the provision potentially granting precedence seems to be focused on only one set of rules. This is because sub-paragraph (a) of the article refers to ‘*such international instrument*’ in the singular. As a result, Article 26 RR either fails to operate at all or merely adds to the confusion under these circumstances.

7.2 An attempt to prevent a conflict of conventions: Article 82 RR

Because there was acknowledgement during the drafting process of the Rotterdam Rules that all of the existing non-maritime carriage conventions expand their scope to include specific types of multimodal carriage, and therefore potentially conflict with the new Rules in these areas, Article 82 RR was drafted. Article 82 RR is intended to accommodate the continued application of the ‘normally applicable inland conventions for the carriage of goods’, and to avoid conflicts such as those that the drafters of the Rules thought possible.¹²⁹ The article grants priority to any convention that according to its provisions applies to any part of the contract of carriage involving the named types of transport. To this purpose the article contains the following text:

Article 82. International conventions governing the carriage of

¹²⁹ A/CN.9/526, p. 68; A/CN.9/WG.III/WP.78, pp. 5-6; A/CN.9/510, p. 11, www.uncitral.org.

goods by other modes of transport

Nothing in this Convention affects the application of any of the following international conventions in force at the time this Convention enters into force, including any future amendment to such conventions, that regulate the liability of the carrier for loss of or damage to the goods:

(a) Any convention governing the carriage of goods by air to the extent that such convention according to its provisions applies to any part of the contract of carriage;

(b) Any convention governing the carriage of goods by road to the extent that such convention according to its provisions applies to the carriage of goods that remain loaded on a road cargo vehicle carried on board a ship;

(c) Any convention governing the carriage of goods by rail to the extent that such convention according to its provisions applies to carriage of goods by sea as a supplement to the carriage by rail; or

(d) Any convention governing the carriage of goods by inland waterways to the extent that such convention according to its provisions applies to a carriage of goods without trans-shipment both by inland waterways and sea.

Thus, Article 82 confers precedence instead of claiming it for itself, which is a rather elegant solution.¹³⁰ In this it follows the line set out by Article 26 RR.

¹³⁰ An example of a provision which confers precedence on the instrument it is part of is Article 103 of the UN Charter which stipulates that: "*In the event of a conflict between the obligations of the Members of the United Nations under the present Charter and their obligations under any other international agreement, their obligations under the present Charter shall prevail.*" Yusuf 2004. Compared to clauses claiming priority, the effects of conflict clauses conferring priority on other treaties are admitted with less difficulty, since these target the treaty containing the clause. Only the effect of conflict clauses of this type is confirmed in Article 30(2) VC which provides that "*When a treaty specifies that it is subject to, or that it is not to be considered as incompatible with, an earlier or later treaty, the provisions of that other treaty prevail.*"

Regrettably, the article is in danger of failing to fulfil its full potential due to its somewhat less than precise wording. An example can be found in the second part of the article, in sub-paragraph (b), which pertains to ferry transport to which the CMR applies by means of Article 2 CMR. It may be that the provision is intended to refer to the whole of a ro-ro carriage of goods that is subject to the CMR. As Diamond establishes, however, the words of the provision do not refer to the whole of any carriage but only to “*the carriage of goods that remain loaded on a road cargo vehicle carried on board a ship*”.¹³¹ The result is that its scope is restricted to ro-ro carriage in the strict sense only. If interpreted thus, the provision causes the Rotterdam Rules to take a back seat to the CMR only for the period while the vehicle onto which the goods are loaded is actually being carried by a ship. This means that any claims for compensation resulting from, for instance, the misdelivery of a consignment of shoes trucked from Alicante in Spain to London in the United Kingdom are governed by the Rotterdam Rules, but also by the CMR.¹³² The damage would after all not have occurred during the period of time when the ‘maritime plus’ convention grants all the rules of the CMR precedence. Of course the rules on the carrier’s liability, limitation of liability or time for suit of the CMR may prevail on the basis of Article 26 CMR if the road stage in question is international in nature. Yet the rules relating to other subjects found in both systems, such as rules on jurisdiction, would still lead to conflict. This seems an unwarranted consequence, as it aggravates an already complex situation instead of alleviating it.

Therefore, although Article 82 prevents some of the considerable list of conflicts that may ensue from the application of the Rotterdam Rules, it is not even close to providing an adequate remedy. It does not solve the potential conflicts that Article 26 RR fails to prevent, and, more importantly, also does not prevent the potential conflicts that the drafters of the new Rules intended to avoid by creating the provision, such

¹³¹ Diamond 2008, p.142-143.

¹³² *Laceys Footwear (Wholesale) Ltd. v Bowler International Freight Ltd. and Another* [1997] 2 *Lloyd’s Rep.* 369.

as the potential conflict regarding ferry transport.

Despite all their flaws, however, the Rotterdam Rules may still be our best bet. The tide is running so high that even an imperfect solution is better than none at all. Therefore, even though the rules of the new ‘maritime plus’ regime may lead to conflicts between the conventions, or to differing interpretations, and perhaps even confusion, it seems that the Rules are still the best possible – if incomplete – solution to the quandary in relation to the law applicable to multimodal transport contracts at this point in time. The reality is that no other new international regime on multimodal transport will be drafted in the near future, so the choice is either to seek to effectuate the Rotterdam Rules or to remain in the current impasse.

8 The influence of secondary EU law: Article 25 Rome I Regulation

If the Rotterdam Rules were to enter into force, however, the quandary mentioned in the introduction to this article concerning their status in relation the Rome I Regulation would come to the surface. The difficulty here is that Article 25 Rome I does not grant priority to all international conventions. Concerning the regulation’s relationship to existing treaties, Article 25(1) Rome I states:

“This Regulation shall not prejudice the application of international conventions to which one or more Member States are parties at the time when this Regulation is adopted and which lay down conflict-of-law rules relating to contractual obligations.”

Scenes reminiscent of the impossible constructions depicted by the Dutch artist Escher would unfold if the Rome I Regulation were to take precedence over the new Rotterdam Rules on the basis of this article, while simultaneously – and on the basis of the same article – granting

precedence to the provisions of the CMR.¹³³ One might even need to practise some Orwellian ‘doublethink’ in order fully to grasp the consequences of such a situation.¹³⁴

In short, conferring precedence on the Rome I Regulation would create the following situation: in a transport from New York in the USA to Antwerp in Belgium by sea and thence to Venlo in the Netherlands by road, the Rotterdam Rules would apply to the road stage, but would, based on Article 26 RR, confer precedence to the rules of the CMR on carrier liability, limitation of liability and time for suit. According to the Rotterdam Rules, the other provisions of the CMR should not be applied, at least not insofar as they are contrary to the provisions of the ‘maritime plus’ regime. This would mean, for instance, that the applicable provisions on the right of control would be those of the Rotterdam Rules.

If the Rome I Regulation were to take precedence, however, although the Rotterdam Rules might have been ratified by the EU Member State where the court addressed was situated, the court in question would not be allowed to apply them, even though it was obliged to do so by international law. The reason for this is that Article 25 Rome I would not grant the newer Rotterdam Rules priority, but would cede to the CMR, because this convention is older than the Regulation. As a result, the above-mentioned right of control would be governed by CMR provisions, even though the State involved was also party to the newer Rotter-

¹³³ M.C. Escher, graphic artist, 1898-1972.

¹³⁴ ‘Doublethink’ was to be practised by government functionaries in Orwell’s 1984. It was the act of *simultaneously accepting as correct two mutually contradictory beliefs. According to Orwell it is: “To know and not to know, to be conscious of complete truthfulness while telling carefully constructed lies, to hold simultaneously two opinions which cancelled out, knowing them to be contradictory and believing in both of them, to use logic against logic, to repudiate morality while laying claim to it, to believe that democracy was impossible and that the Party was the guardian of democracy, to forget, whatever it was necessary to forget, then to draw it back into memory again at the moment when it was needed, and then promptly to forget it again, and above all, to apply the same process to the process itself-- that was the ultimate subtlety; consciously to induce unconsciousness, and then, once again, to become unconscious of the act of hypnosis you had just performed. Even to understand the word ‘doublethink’ involved the use of doublethink.”* Orwell 1949, part 1, chapter 3.

dam Rules, to which it most likely ought to grant precedence based on the rule of international public law *lex posterior derogat legi priori* found in Article 30 VC.¹³⁵ Of course, a conflict would only occur in this situation if the court addressed was of the opinion that the CMR applied to international road carriage irrespective of whether the contract involved other modes of transport or not.

If the transport involved ro-ro transport from Felixstowe in England to Rotterdam and road carriage from Rotterdam to Krefeld in Germany, however, any court would have to apply the CMR instead of the Rotterdam Rules if Article 25 Rome I caused the Regulation to have precedence over the Rotterdam Rules.

In the case of an EU Member State ratifying the Rotterdam Rules, this would obviously not be the intended result.¹³⁶

Thus we are faced with two questions. The first is whether the scope-of-application rules of the carriage conventions are indeed 'conflict-of-law rules' within the meaning of Article 25 Rome I. If they are, then the only scenario that would prevent the cat-and-mouse game of the CMR and the Rotterdam Rules outlined above would be one where it was accepted that international conventions that were not part of the body of EU law would take priority at least over secondary EU law, such as the Rome I Regulation. Since the scope-of-application rules of treaties are also referred to as 'unilateral conflict rules', there is a very real chance that these rules should be considered as constituting 'conflict-of-law rules' of the type to which Article 25(1) Rome I refers.¹³⁷ This seems all the more likely since Article 25 Rome I is the successor to Article 21

¹³⁵ The Vienna Convention on the law of treaties, concluded at Vienna on 23 May 1969. Article 30 VC regulates the hierarchy of successive treaties relating to the same subject-matter.

¹³⁶ If the drafters of the Rotterdam Rules had deemed that Article 25 Rome I would have this result, they would probably not have made the effort to draft and include Article 82(b) RR concerning the precedence of another convention in situations involving ro-ro transport. If Article 25 Rome I caused the Regulation to have precedence over the Rotterdam Rules, this paragraph would only extremely rarely be relevant, since almost all of the CMR Member States are also Member States of the EU and bound by the Rome I Regulation.

¹³⁷ Clarke 2003 *International carriage of goods by road*, p. 41; Basedow 1997, p. 913.

Rome Convention, which regulated the convention's relationship with other international conventions.¹³⁸

Then again, if scope-of-application rules are not deemed to constitute 'conflict-of-law rules', the above-mentioned illogical situations concerning the CMR and the Rotterdam Rules will not arise. But even then the problem would endure, albeit in a somewhat different form.

If Article 25(1) Rome I does not relate to scope-of-application rules, then the second question concerning the relationship between Rome I, or secondary EU law, and treaty law which is not EU law still needs to be answered in order to know which one takes precedence. If the answer is secondary EU law, however, the harmonising purpose of international treaty law would be compromised. If treaties could only be applied by means of the national law that was appointed by the Rome I Regulation, or perhaps as 'overriding mandatory provisions' within the meaning of Article 9 Rome I, their international authority would diminish and they would probably be considered more akin to national rules and thus be hampered in achieving their harmonising goals.

All in all, it seems that this second question needs answering, whatever the answer turns out to be to the first. Unfortunately, the literature does not supply an unequivocal answer as regards the status of international treaties, such as the CMR, to which the EU is not a contracting party.¹³⁹

The relationship between such treaties and primary EU law appears to be clear. In *Commission v Finland* the ECJ determined that international treaty law which is not part of the legal order of the EU is subject to enforced conformity to primary EU law on the basis of Article 351

¹³⁸ The Giuliano-Lagarde Report specifically states that Article 21 RC is intended to ensure that the Rome Convention does "not prejudice the application of any other international agreement, present or future, to which a Contracting State is or becomes party, for example, to Conventions relating to carriage." Giuliano-Lagarde Report, Article 21.

¹³⁹ Tietje 2008.

TFEU, the second sentence.¹⁴⁰ This implies the supremacy of primary EU law over international agreements.¹⁴¹ The relationship between treaties that are not part of the ‘*acquis communautaire*’ and secondary EU law, such as regulations and directives, is somewhat more obscure, however. The first sentence of Article 351 TFEU seems to indicate, at least in the case of ‘anterior treaties’ (*i.e.*, treaties concluded by EU Member States before joining the EC), that the older international law should be granted precedence: “The rights and obligations arising from agreements concluded before 1 January 1958 or, for acceding States, before the date of their accession, between one or more Member States on the one hand, and one or more third countries on the other, shall not be affected by the provisions of the Treaties.” Nevertheless, when read in conjunction with the last sentence of the article and taking into account the existing case law, it must be concluded that although the article protects anterior treaties in the abstract, the ECJ often finds reasons not to apply this provision in a case actually before it.¹⁴² Article 351 TFEU is apparently not intended to mean that public international law obligations prevail over EU law. Rather, it is intended to imply the reverse, according to the Commission.

When it comes to ‘posterior’ treaties (*i.e.*, treaties or conventions that have been concluded by EU Member States during their EU membership, The ECJ’s stance in this matter seems crystal clear, however, as is illustrated by the 1971 decision in *ERTA*:

¹⁴⁰ The second sentence of Article 351 TFEU, formerly Article 307(2) EC, states that: “To the extent that such agreements are not compatible with the Treaties, the Member State or States concerned shall take all appropriate steps to eliminate the incompatibilities established.” ECJ 19 November 2009, case C-118/07 (*Commission v Finland*). The object of the proceedings was the *failure to adopt appropriate steps to eliminate incompatibilities between the bilateral agreements concluded with third countries prior to accession of the Member State to the European Union and the EC Treaty*. See also Bungenberg 2010, p. 141.

¹⁴¹ A. Epiny, B. Hofstötter & M. Wyssling, ‘The status of ‘Europeanized’ international law in Austria, Switzerland and Liechtenstein’, in: J. Wouters, A. Nollkaemper & E. de Wet (eds.), *The Europeanisation of international law: the status of international law in the EU and its Member States*, The Hague: T.M.C. Asser Press 2008, pp. 137-159, at p.142.

¹⁴² Klabbers 2009, p. 148.

“In particular, each time the community, with a view to implementing a common policy envisaged by the Treaty, adopts provisions laying down common rules, whatever form they may take, the Member States no longer have the right, acting individually or even collectively, to undertake obligations with third countries which affect those rules or alter their scope.”¹⁴³

Thus, if the term ‘conflict-of-law rules’ in Article 25(1) Rome I also includes the scope-of-application provisions of treaties such as the Rotterdam Rules, any Member State is pre-empted from becoming a member of any new convention that regulates contracts, since such a new convention will always include scope-of-application provisions and the EU has an exclusive external competence concerning the law applicable to contractual obligations, as it has taken internal measures concerning this issue in the form of the Rome I Regulation.¹⁴⁴ Since the European Parliament called on Member States on 5 May 2010 “*speedily to sign, ratify and implement the (...) Rotterdam Rules*”, it would seem unlikely that any of the Rotterdam Rules conflict with EU law, however.¹⁴⁵

Yet, if scope-of-application rules are not ‘conflict-of-law’ rules as per Article 25(1) Rome I, uncertainty still remains concerning the hierarchy of a new carriage convention such as the Rotterdam Rules and the Rome I Regulation.

Of course, if secondary EU law should have priority, there is a silver lining. In that case the difference in views on the scope of the CMR in

¹⁴³ ECJ 31 March 1971, case C-22/70, *ERTA*. The decision was confirmed in *Open Skies* in 2002. ECJ 5 November 2002, case C-469/98, *Commission v Finland*, popularly known as *Open Skies*. In *Open Skies* the ECJ emphasised that, even if the Community’s external competence in the field of air transport might arise by implication from provisions of the Treaty, this case did not involve a situation in which the Community’s internal competence could effectively be exercised only at the same time as its external competence and, therefore, the Community could not validly claim that there was an exclusive external competence to conclude an air transport agreement with the U.S.A.

¹⁴⁴ Klabbers 2009, pp. 187-188.

¹⁴⁵ European Parliament, Brussels 5 May 2010, *Strategic goals and recommendations for the EU’s maritime transport policy until 2018, (2009/2095(INI))*, www.europarl.europa.eu.

Germany on the one hand and in the Netherlands and England on the other may no longer be as consequential. The German BGH and German legal scholars are already of the opinion that the CMR can only apply to a road stage of a multimodal transport contract by means of the applicable national law. Should the Rome I Regulation take precedence over non-EU binding treaty law such as the CMR, and should 'conflict-of-law rules' not encompass scope-of-application rules, then the Netherlands and England would be forced to adopt an approach to the CMR that is rather similar to the German one. This is because if scope-of-application rules in conventions are not considered to constitute 'conflict-of-law rules' as referred to in Article 25 Rome I, and if the Rome I Regulation takes precedence over conventions such as the CMR, courts of law bound by Rome I could no longer apply the CMR *ex proprio vigore* merely because the forum State is party to the CMR. Pursuant to Rome I, such a court would have to grant precedence to the national law applicable to the contract in question and would only then be able to determine whether this domestic law allowed for the application of the CMR to the road carriage provided for in the contract.

The result of this would be that the mandatory rules on carrier liability that are generally found in the international carriage conventions could be circumvented quite easily, for instance by choosing a national regime based on Article 4 Rome I as the law applicable to the contract that does not allow for the indirect application of such a convention. A Dutch carrier and consignor party to a contract for carriage by road from the Netherlands to Germany, for instance, could then choose to have their agreement governed by Canadian law, thus effectively setting aside the CMR (to which both Germany and the Netherlands are party). This seems a less than desirable outcome. Luckily, however, there are a lot of 'ifs' to overcome before this outcome could become a reality.

8.1 A solution?

Although the relationship between conventions that are not part of the law of the EU and secondary EU law remains unclear, it is clear that the

law of international treaties to which the EU is a party supersedes both primary and secondary EU law.¹⁴⁶ This means that the problems mentioned – except the conflicting obligations under public international law stemming from membership of both of these not ‘entirely compatible’ carriage conventions – could be resolved if the EU were to become a party to both the CMR as well as the Rotterdam Rules.

Vis-à-vis the CMR this would promote legal uniformity, because the ECJ would then be authorised to adjudicate on the content of the CMR and, as a result, on its scope of application in relation to multimodal transport.¹⁴⁷ Although not all of the CMR Member States are EU Member States, this would at the very least diminish the current diversity of opinions. The question is whether the EU is willing and, for that matter, able to accede to the CMR.

The Rotterdam Rules meanwhile have done their utmost to attract the patronage of the EU. With Article 93 RR stating that regional economic integration organisations that are constituted by sovereign States and have competence over certain matters governed by the convention may similarly sign, ratify, accept, approve or accede to the Rules, there

¹⁴⁶ Tietje 2008, p. 57. For the primacy of the Montreal Convention as regards secondary EC law see ECJ 10 January 2006, case C-344/04 (*The Queen ex parte International Air Transport Association, European Low Fares Airline Association v. Department for Transport*), *Jur.* 2005, p. I-00403 or *NJ* 2006, 372.

¹⁴⁷ This is currently not possible. “*It is settled case-law that the power, as resulting from that provision, to provide interpretations by way of preliminary rulings extends only to rules which are part of European Union law (see to this effect, inter alia, Case C-130/95 Giloy [1997] ECR I-4291, paragraph 21; Case C-222/04 Cassa di Risparmio di Firenze and Others [2006] ECR I-289, paragraph 63; and Case C-453/04 innoventif [2006] ECR I-4929, paragraph 29). In the case of international agreements, it is settled that such agreements concluded by the European Union form an integral part of its legal order and can therefore be the subject of a request for a preliminary ruling (see to this effect, inter alia, Case 181/73 Haegeman [1974] ECR 449, paragraphs 4 to 6; Case 12/86 Demirel [1987] ECR 3719, paragraph 7; and Case C-431/05 Merck Genéricos – Produtos Farmacêuticos [2006] ECR I-7001, paragraph 31). On the other hand, the Court does not, in principle, have jurisdiction to interpret, in preliminary ruling proceedings, international agreements concluded between Member States and non-member countries (see, to this effect, Case 130/73 Vandeweghe and Others [1973] ECR 1329, paragraph 2; order in Case C-162/98 Hartmann [1998] ECR I-7083, paragraph 9; and Bogiatzi, paragraph 24.)” ECJ 4 May 2010, case C-533/08 (*TNT Express Nederland BV v AXA Versicherung AG*)*

certainly seems no impediment on that account. That there is no impediment in that area does not mean that the EU will ratify, however, as there seems to be some dissension on the desirability of the Rotterdam Rules between the EU Member States. Nevertheless, the European Parliament has recently made its stance clear as was already mentioned above, calling “*on Member States speedily to sign, ratify and implement the UN Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea, known as the “Rotterdam Rules”, establishing the new maritime liability system.*”¹⁴⁸

9 Diagnosis

When confronted with a dispute involving a multimodal transport contract it is rather difficult, to say the least, to determine which law should be applied. This is not a new problem, as the ‘multimodal’ scope of application of the existing carriage conventions has been the subject of international disagreement for decades. This has been copiously illustrated in the first part of this article in respect of the CMR. Recently, however, a few complicating factors have surfaced.

The first is the possible entry into force of the new ‘maritime plus’ convention, the Rotterdam Rules. Because these Rules govern all multimodal contracts that include a sea stage, an extra ingredient has been added to the already obscure ‘multimodal muddle’.¹⁴⁹ In addition to potentially conflicting with the existing carriage conventions, this ingredient also contains a none-too-transparent ‘limited network’ system in Article 26 and a conflict-of-conventions provision in Article 82 of a highly bureaucratic nature: it seems to redirect you at every turn.

The second complicating factor is the influence of EU law. The Rome I Regulation, which replaces the Rome Convention on the law applicable

¹⁴⁸ European Parliament resolution of 5 May 2010 on strategic goals and recommendations for the EU’s maritime transport policy until 2018 (2009/2095(INI)), www.uncitral.org.

¹⁴⁹ The term ‘multimodal muddle’ is borrowed from Glass. *Glass 2006*.

to contractual obligations, seems rather less tolerant regarding conflicting international conventions than was its predecessor. Where the Rome Convention conferred precedence on all conflicting international conventions to which a Contracting State was, or became, a party, the Rome I Regulation only does so concerning conventions that already existed at the time the Regulation was adopted.¹⁵⁰ The Regulation also adds that the convention in question needs to lay down conflict-of-law rules relating to contractual obligations. As a result even more questions have to be answered when determining the law applicable to a multimodal carriage contract than in the past. Due to the Regulation, clarity is now required on what can be considered a ‘conflict-of-law rule’ and whether the convention in question existed before adoption of the Regulation or not. Yet, the most important question to be answered as a result of the extra layer of law that has been added is the one concerning the status of international agreements and EU law. Although the hierarchy is clear regarding such agreements that have become EU law because the EU is party to them, it is far from apparent concerning those international agreements that the EU is not party to.

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¹⁵⁰ Article 21 RC and Article 25 Rome I Regulation.

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The MARPOL Convention
Annex VI on regulations for the
prevention of air pollution
from ships - a fair deal?

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1 Introduction

1.1 The international background

Environmental awareness generally shows continuous signs of increase, although there have been many setbacks. For shipping, the International Maritime Organization (IMO) has for a number of years dealt with issues concerning the protection of the marine environment. Although preventive work is of the utmost importance, the reparative function of environmental liability rules should not be ignored. IMO activities may also have an indirectly positive effect on environmental protection. Thus, while the Safety of Life at Sea Convention (SOLAS) is primarily aimed, as its name suggests, at safeguarding life at sea, such ship safety requirements will also benefit the environment: safer ships, safer seas. This is one example of many.

The IMO is not the only international legislator on environmental issues relating to shipping. The European Union (EU) nowadays plays an important role and there are also other bodies, not least Helcom.¹ Although Helcom's powers are restricted, both geographically and substantively, its political influence should not be overlooked.

A particular issue in environmental terms is air pollution from ships. This is one of the latest international legal debating points in the

¹ Helsinki Commission - Baltic Marine Environment Protection Commission. Helcom is the governing body of the Convention on the Protection of the Marine Environment of the Baltic Sea Area, known as the Helsinki Convention, 1992 (entered into force in 2000) with subsequent amendments. The 1992 Convention was preceded by the 1974 Convention (entered into force in 1980).

area of environmental protection.² An interesting observation is that air pollution from ships does not fit into the existing approach for protecting the marine environment. In this case there is more at stake: air pollution prevention is also important for all land areas, as the polluting matter does not restrict itself to sea or coastal areas. As a result, one can discern a more comprehensive environmental approach than one that merely applies directly to sea areas as such. The common factor, on the other hand, is the ship itself, as the direct or indirect (through its cargo) source of pollution, although the victim of the pollution may be either at sea or on land.

The International Convention for the Prevention of Pollution from Ships, or MARPOL, was adopted in the aftermath of the Torrey Canyon accident in 1967, together with some other international legislation relating to the protection of the marine environment.³ The Convention of 1973 did not achieve substantial support, mainly due to some legal-technical issues. Consequently, a Protocol was added in 1978 that aimed to resolve those problems. MARPOL 1973/1978 today is of considerable

² The IMO initiative on prevention of air pollution has a somewhat more wide-ranging history behind it. On a general level, prevention of air pollution has been discussed for a couple of decades, see, e.g., *Transboundary Air Pollution*, edited by C. Flinterman, B. Kwiatkowska, and J.G. Lammers, Nijhoff, 1986, *passim*. Cf. the IMO solutions with general global measures, Patricia Birnie & Alan Boyle & Catherine Redgwell, *International Law & the Environment*, Oxford University Press 2009, pp. 342 *et seq.* and Agustin Blanco-Bazán, *The Environmental UNCLOS and the Work of IMO in the Field of Prevention of Pollution from Vessels*. Included in *International Marine Environmental Law* edited by Andree Kirchner, Kluwer 2003, pp. 31 - 46, p 31 *et seq.* See also Craig L Carr & Gary L Scott, *Multilateral Treaties and the Environment: A Case Study in the Formation of Customary International Law* (1999) 27 *Denv.J. Int'l & Pol'y* 313, *passim*.

³ However, the Oilpol Convention 1954 had already set criteria for allowed oil discharge.

relevance, but there are variations in view of the six different Annexes.⁴ Originally only two (compulsory) Annexes were associated with MARPOL, relating to prevention of oil pollution and control of pollution by noxious liquid substances respectively. Subsequently four more have been added. Annex VI relating to prevention of air pollution from ships was adopted by the IMO in 1997 (by a specific Protocol that itself had nine articles). This Annex entered into force on May 19, 2005. In 2008, modifications to Annex VI were adopted and these entered into force on July 1, 2010. The renewed Annex VI includes emissions limits that will gradually become stricter.⁵

Annex VI deals with various emissions-related matters, including limits on sulphur emissions, which is the topic dealt with in the following.

The 2008 modifications to Annex VI mean stricter controls on sulphur emissions than before. They also mean that new limits are being introduced both on a general level and also in specifically defined Sulphur Emission Control Areas (SECAs). In general terms, the following original pre-2008 requirements continue to exist:

- the sulphur content of any fuel used on board a ship must not exceed 4.50% m/m
- the sulphur content of any fuel used on board a ship operating

⁴ The Annexes are as follows (with date of entry into force): Annex I - Regulations for the Prevention of Pollution by Oil (2 October, 1983), Annex II - Regulations for the Control of Pollution by Noxious Liquid Substances in Bulk (2 October, 1983), Annex III - Prevention of Pollution by Harmful Substances Carried by Sea in Packaged Form (1 July, 1992), Annex IV Prevention of Pollution by Sewage from Ships (27 September, 2003), Annex V Prevention of Pollution by Garbage from Ships (31 December, 1988) and Annex VI - Prevention of Air Pollution from Ships (19 May, 2005).

⁵ Bin Okamura, *Proposed IMO Regulations for the Prevention of Air Pollution from Ships* (1995) J.Mar.L. & Com. 183 and Sandra Y Snyder, *EPA's Category 3 Marine Emissions Standards: Mimicking MARPOL Annex VI or Mocking the Clean Air Act?* (2005) 75 Brooklyn.L.Eev 1065.

in a SECA must not exceed 1.50% m/m.⁶

The 2008 modifications resulted in the following limits and timetables:

- By 2012 the general limit will be 3.50 % m/m, and from 2020 the figure will be 0.50 % m/m, subject to certain further specifications⁷
- By 2015 the SECA limit will be 0.10 % m/m, subject to certain further specifications (having been 1.00 % m/m since 2010).

Sulphur Emission Control Areas (SECAs) are defined in Annex VI. These areas include the Baltic Sea and the North Sea (and the English Channel). The North American Emission Control Area will enter into force on 1 August, 2011.

The EU is not party to MARPOL, and thus not to Annex VI, but simultaneously applies Directive 32/1999 relating to a reduction in the sulphur content of certain liquid fuels [and amending Directive 12/1993] (the Sulphur Directive). The 1999 Directive has itself been amended by Directive 33/2005.⁸

There are references to MARPOL Annex VI in the preamble of the Sulphur Directive. It should be noted, and this is relevant to the discussion later in this article, that paragraph 21 of the preamble clearly mentions as a line of EU policy that the EU will advocate more effective protection of areas sensitive to sulphur emissions and a reduction in the normal limit value for bunker oil at the continuing and future negotiations concerning MARPOL within the IMO. According to the pream-

⁶ Alternatively, an exhaust gas cleaning system or other approved technology for reducing total SO_x emissions from main and auxiliary engines and boilers to a maximum of 6.0g SO_x /kWh when operating in a SECA may be employed. Controls are also set on effluent discharges from such cleaning systems. Note that the EU Sulphur Directive has slightly different timetables for SECAs, see further references below.

⁷ The alternative date is 2025, pending a review in 2018.

⁸ As this Sulphur Directive covers certain additional sectors, the following amendments have also affected its content: Regulation 1882/2003; Regulation 219/2009; and Directive 30/2009. The Sulphur Directive includes sulphur limits for ships at berth in EU ports and special provisions for passenger ships and ferries sailing on regular schedules. These are not dealt with in this article. See on the background Ludwig Krämer, *EC Environmental Law*, 4th ed., Sweet & Maxwell, 200 p. 216 paras 8-29.

ble, the EU will also continue to seek to have the North Sea/English Channel declared a special low sulphur emission control area. This latter policy is reflected in MARPOL Annex VI. Article 4a of the Sulphur Directive includes provisions dealing with the maximum sulphur content of marine fuels used in SECAs. There are different limits for different EU sea areas. Article 4a introduces more stringent requirements for the Baltic Sea and for the North Sea than for other EU sea areas. Given that the Sulphur Directive follows the MARPOL developments and may also go further, together with the policy statement found in the above-mentioned preamble, an amendment of the Sulphur Directive along the lines of MARPOL Annex VI, 2008 can be expected. The planned timetable at present is to produce a Commission proposal in April 2011.⁹

The MARPOL 2008 amendments and the plans to amend the EU Sulphur Directive accordingly have caused some concern. Many industrial sources and shipowners seem to consider the limit of 0.10 % in a SECA as unreasonable compared with the “general” limit. They maintain that the renewal costs between 0.50 and 0.10 levels are considerable and are causing, for example, pressure on freight rates and prices for both shipping and land-based industry.

So what legal considerations are relevant in this context? The general limits, as opposed to those applicable in SECAs, impose varying requirements on ship operators. Is the resulting non-level economic playing field of any relevance in legal terms? What can an IMO Member State or an EU Member State do if it considers the allegation of a non-level economic playing field to be valid or at least deserving of further investigation? This is the focus of the following analysis.

First, the article discusses the IMO sulphur levels. This includes a look at how Annex VI of MARPOL is applied and also at matters relating to the flag and trading areas of the ship, as well as formal measures that may be taken by any IMO Member State to oppose amendments to

⁹ See European Commission - Environment: http://ec.europa.eu/environment/air/transport/ships_directive.htm; per November 10, 2010. Also, Lloyd’s List October 11, 2010.

Annex VI. Thereafter, EU law is debated in view of the general principles of equality and non-discrimination. In other words, do air emissions limits in different EU sea areas comply with these principles of EU law? These considerations relate to certain general rules and principles of EU law. It is thus necessary to consider not only how an IMO Member State can participate in the IMO decision-making process, but also how such a state in its capacity as an EU Member State is bound by EU law.

The United Nations Convention on the Law of the Sea (UNCLOS), which is also referred to as the Montego Bay Convention, was adopted in 1982 and is considered the Constitution of the Seas. Altogether 160 states have ratified the Convention and generally it can be considered to reflect a truly global view on the international regulation of different sea areas.¹⁰

When UNCLOS was under preparation, one of the major questions was how to divide international jurisdiction between flag States and coastal States. The result was, not unexpectedly, a compromise which is reflected in the provisions dealing with the jurisdiction of coastal States.

UNCLOS needs to be taken into consideration, but within the limited space available in this publication it is not possible to examine the legal problems from that particular perspective. Suffice it to say that UNCLOS regulates flag State and coastal State jurisdiction, but not the internal waters of a coastal State. This means that UNCLOS is of relevance when it comes to exercising State jurisdiction also in relation to air emissions from ships in transit, *cf.* regulation 11 paragraph 6 of MARPOL Annex VI.

As mentioned above, the following is not a comprehensive analysis.

¹⁰ A number of States, for example, the U.S., Turkey, Venezuela and Peru have not ratified UNCLOS. The explanation for the U.S. approach seems to be the deep-seabed mining regime in UNCLOS.

2 The flag

Regulation 1 of MARPOL Annex VI states that the provisions of the Annex shall apply to all ships, except where otherwise stated in Regulations 3, 5, 6, 13, 15, 16 and 18.

Regulation 3 deals with emissions relating to the safety of the ship and emissions connected with trials for reducing ship emissions and research into emissions control technology. The rest of the regulation does not deal with shipping activities. Regulation 5 establishes that the emissions provisions only apply to ships of 400 gross tonnage and above. The flag State itself shall survey the ship or the task may be delegated to a classification society. Regulation 6 specifies various issues concerning certification. Regulation 13 specifies the marine diesel machinery to which the limits on nitrogen oxides emissions either do or do not apply. Regulations 15 and 16 also specify some technical requirements and Regulation 18 deals with fuel oil availability and quality, also to be recorded by means of a bunker delivery note (BDN).

The above-mentioned reference to the application of Annex VI to all ships must be read in the light of Regulation 14 dealing with sulphur emissions. According to paragraph 4 of this regulation, within a SECA on or after January 1, 2015 the sulphur content of fuel oil used on board ships shall not exceed 0.10 % m/m. Less stringent sulphur emission limits apply in non-SECAs, as mentioned above.

Concerning SECAs, the ship in question must, according to Regulation 14 (6), carry a written procedure showing how the fuel oil change-over has been carried out and also comply with further details found in this provision. A proper entry in the ship's log book must be made.

A SECA is defined in Regulation 2 (8) of Annex VI. A SECA is, *inter alia*, stated to be an area where the adoption of certain special mandatory measures is required.

The allowed sulphur emissions are determined by the operational area of the ship. The flag of the ship is not of primary relevance in this respect. In all situations, however, attention must be paid to Regulation

1, according to which Annex VI is applicable to all ships, notwithstanding the above-mentioned exceptions.

The fact that the flag State must arrange the necessary survey according to Regulation 5 does not change the above-mentioned emphasis. And, according to Regulation 7 (4) of Annex VI, no appropriate certificate shall be issued to a ship which is entitled to fly the flag of a state which is not a party.

According to Article 5 (4) of MARPOL 1973, States parties shall apply the requirements of the present convention with respect to ships of non-parties to the convention, as specified (the no-more-favourable-treatment doctrine). This is an important provision.

According to Articles 5 and 6 of MARPOL 1973, the port State is granted particular rights regarding port State control and the issuing of sanctions in line with a specified procedure if there are clear grounds for believing that the condition of the ship does not correspond substantially with the particulars of the respective certificate.

To repeat, it is the ship's operational area that determines the levels of allowed sulphur emissions, not its flag. However, flag has relevance in the sense that a ship whose flag State is a non-party to Annex VI cannot in principle operate in sea areas where a state Party to Annex VI has international jurisdiction in relation to the ship in question. This has been expressed in national legislation in, for example, Finland. According to Chapter 7 Section 1 of the Act on Protecting the Marine Environment (1672/200), contaminating air emissions from ships are prohibited in Finnish territorial waters and in the Finnish exclusive economic zone (EEZ), and also from Finnish ships outside Finnish territorial waters and the Finnish EEZ, as further specified in MARPOL Annex VI, by Helcom, in treaties by which Finland is bound or by EU law. According to Chapter 6 Section 2 of the Government Decree on Protecting the Marine Environment (76/2010), the sulphur content of any fuel used on board Finnish ships operating in a SECA or on board non-Finnish ships operating in Finnish territorial waters or in the Finnish EEZ must not exceed 1.50% m/m (this figure will be changed, provided that the IMO 2008 amendments enter into force in Finland and/or that the EU Sulphur Directive is amended accordingly).

3 The status of an IMO Member State with regard to non-application of the air emissions regulations in MARPOL Annex VI

Of course the IMO itself could make an upwards modification of allowed emission levels, thus making it easier (and cheaper) to operate ships. Politically, however, such a move is not within the realms of possibility.¹¹

Taking a legal approach, Article 16 of MARPOL 1973 includes provisions concerning processes of amendment for both the convention and its annexes. For the annexes, the principle of tacit acceptance is applied. This procedure was also adopted in the SOLAS Convention, 1974. Previous SOLAS Conventions had not included this possibility, with the result that amendment efforts failed. The tacit acceptance procedure has proved an efficient way of changing that pattern. Eventually the same procedure was also adopted in other safety conventions, but the exact wording used in the respective conventions shows some variations of substantive relevance.

Unless a Contracting State provides notification that its express approval is needed or, in applicable cases, communicates an objection, approval is deemed to have taken place, as further specified in Article 16 (2) (f) (ii) and (iii) and (g) (ii) of MARPOL 1973. A sufficient number of, respectively, notifications of requirements for express approvals or objections may cause the amendment not to enter into force. In any case, a State notifying either a requirement for express approval or an objection will not be bound by the amendment until its approval is provided separately. There are certain time limits that must be taken into consideration. If these are not complied with, the State will be bound by the amendment.

¹¹ See, for example, regarding the level of commitment of the IMO, Address of the Secretary-General at the Opening of the 61st Session of the MEPC, MEPC 61/INF. 27, September 27, 2010.

There is a way for a Contracting State to change the status of being bound by either MARPOL, an annex or an amendment thereto. According to Article 18 of MARPOL, a Contracting State may denounce the convention or any optional annex. Here it should be noted that Annexes I and II are non-optional and denouncing them requires the adoption of a standpoint in respect of the Convention as a whole. Denunciation is possible at any time after the expiry of five years from the date on which the convention or an optional annex has entered into force in respect of the denouncing Contracting State. A denunciation takes effect 12 months after receipt of notification by the IMO. If the amended Annex VI is assumed to have entered into force on July 1, 2010, the amended Annex VI can be denounced as of July 1, 2015. It is also necessary, however, to take into consideration the above-mentioned additional 12 months' notification time. As sulphur emissions will be limited to 0.10 % in SECAs from January 1, 2015, a denunciation cannot take effect simultaneously with the entering into force of the amended Annex VI. During the additional notification time, at least in theory, the denouncing State has to take into consideration the new limit. It would thus seem that any State would have to decide its policy on the new limits within the framework of the above-mentioned procedure of reserving express approval, notwithstanding any restrictions based on EU law.

Notification of a requirement for express approval is not necessarily a political statement. Some IMO Member States might need more time to prepare domestic legislation, and such a notification might solve an international dilemma.

In view of the air emissions regulations, the position of any State reacting through an objection/requirement for express approval and/or a denunciation will affect its relationship with the ship involved. From a flag State point of view, one of the above-mentioned reactions will not necessarily be so decisive. From a port State point of view, however, the legal relevance is obvious. Say, with regard to Baltic trade, that Russia would not accept the new emissions limits. This would mean that any trade to or from a Russian port would not be targeted through Russian

port State authorities. Coastal States on the trading route might react in accordance with UNCLOS, but the practicality of exercising coastal State jurisdiction might be questionable.

Further details on state jurisdiction over ships are passed over in this connection, but there are interesting questions concerning coastal State jurisdiction in the territorial sea and the EEZ. Note also that Article 222 UNCLOS includes specific provisions on enforcement with respect to pollution from or through the atmosphere. This provision is not as detailed, however, as the enforcement provisions that deal with pollution of the marine environment.

A fundamentally important additional consideration is EU policy and law, which reduces the flexibility of the EU Member States with regard to policy. This is dealt with in the following.

4 The relationship between the EU and the IMO. EU coordination of Member State activities

In practice, it seems that the EU's relationship with the IMO is settled in the sense that the IMO creates safety standards, while the EU focuses on implementing and enforcing them as efficiently as possible. There are of course a number of additional specifications and exceptions. With regard to any gaps in the IMO's standards, it is particularly interesting to follow what the EU achieves with regard to safety at sea.

The EU is not a member of the IMO, which means that the EU cannot formally and directly take part in IMO decision-making processes. Quite another matter, however, is the way in which the EU - through its Member States - *de facto* influences safety-at-sea work in the IMO. The EU is also not party to the IMO safety conventions, but there is of course nothing to prevent the EU from enacting EU legislation that in

substance includes provisions also found in IMO conventions.¹²

As the EU is not party to MARPOL, the question arises what will happen if or when a Member State, some Member States or all Member States are parties to this convention and there is a conflict between it and EU law. There is, of course, always the same potential for conflict in respect of any convention that one or more Member States are bound by. This is relevant to the discussion here in two ways. Firstly, what can an EU Member State do to abstain - independently of the EU - from implementing Annex VI of MARPOL? Secondly, what can the EU do independently of the fact that Member States are bound by Annex VI of MARPOL?

Article 4 (3) (2) of the Treaty on European Union (TEU)¹³ states that the Member States shall take any appropriate measure, general or particular, to ensure fulfilment of the obligations arising out of the Treaties or resulting from the acts of the institutions of the Union (*cf.* Article 10 EC). According to Article 91 TEU (Article 71 EC), the European Parliament and the Council, as further specified in the provision, lay down common rules applicable to international transport to or from the territory of a Member State or passing across the territory of one or more Member States. This is also the procedure for laying down measures to improve transport safety. According to Article 100 (2) of the Treaty on the Functioning of the European Union, *i.e.*, the FEU Treaty or TFEU (Article 80 (2) EC), the European Parliament and the Council, acting in accordance with the ordinary legislative procedure, may lay down appropriate provisions for sea and air transport. These provisions have a connection with Articles 3 to 6 TFEU, in that these provisions state,

¹² On the other hand, the EU is party to UNCLOS (the Montego Bay Convention) based on Council Decision 392/1998. The EU may interfere in any breach by a Member State of any of the provisions of UNCLOS.

¹³ The Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community (EC Treaty), signed at Lisbon on December 13, 2007 entered into force on December 1, 2009. Article 2 (1) of the Lisbon Treaty changed both the name of the EC Treaty (to the Treaty on the Functioning of the European Union - TFEU) and the numbering of its articles. In the following, the new numbering is used together with references, where necessary, to the respective article of the EC Treaty.

more clearly than did their equivalents in the EC Treaty, the nature of the exclusive competence of the EU and of the shared competence of the EU and the Member States. Articles 2 to 6 TFEU are dealt with below.¹⁴

To the extent that conventions (agreements) concluded by any Member State or States are not compatible with the EU Treaties, the Member State or States concerned shall, according to Article 351 TFEU (Article 307 EC), take all appropriate steps to eliminate the incompatibilities. This priority applies in relation to conventions concluded before the respective State became a member of the Union. The “old” conventions that the respective Member State is bound by are only secondary in respect of the Member State obligations regulated in the EU Treaties. It is of course quite clear that it is not possible for a Member State to act against such obligations. A Member State cannot become bound by a new convention if it conflicts with EU law.

As a further factor limiting independent decision-making by a Member State, the exclusive and shared competence of the EU has to be taken into consideration. This division has to do with the internal competence of the EU, but it affects at least to some extent the external competence that is based on a separate provision in the TFEU. The competence of the EU as a whole is not completely clear and it seems that many borderline matters are evaluated on a case-by-case basis.

The EU, as already stated, is not a member of the IMO. In spite of this, the EU may have competence in relation to the IMO, which means that a Member State does not have full sovereignty to act in matters concerning IMO legislative work. If EU legislation exists covering the same subject-matter as the IMO work, an EU Member State will breach its EU obligations if it acts on its own initiative within the IMO. EU Member States acting within the IMO should first co-ordinate their

¹⁴ As already stated, the EU is party to UNCLOS. According to Article 216 (2) TFEU, agreements concluded by the Union are binding upon the institutions of the Union and on its Member States (Article 300 (7) EC). This means that the Member States cannot act by themselves in order to, for example, seek amendments to UNCLOS. The rights both to take such initiative and to enforce the convention’s provisions fall within the competence of the Union. UNCLOS and other conventions bind the Union in such a way that the conventions form part of the primary law of the Union.

actions within the Union, which has the result that EU Member States act in concert within the IMO.

The demarcations of the EU's internal and external competences are not without problems, but with regard to a Member State's right or possibility to act alone within the IMO, there is a clarifying judgment in the case of *Commission v Hellenic Republic C-45/07* (12.2.2009). Greece had submitted to the IMO a proposal for monitoring the compliance of ships and port facilities with the requirements of Chapter XI-2 of the International Convention for the Safety of Life at Sea, concluded in London on 1 November 1974 ('the SOLAS Convention') and the International Ship and Port Facility Security Code ('the ISPS Code'). Prior to this action by Greece, the EU had enacted Regulation 725/2004 on enhancing ship and port facility security. The aim of this Regulation was to introduce and implement Community measures aimed at enhancing the security of ships used in international trade and domestic shipping and of associated port facilities in the face of threats of intentional unlawful acts. The Regulation also contained details regarding procedures. The Regulation referred to the SOLAS Convention and the ISPS Code. The Commission stated before the Court that Greece had acted in breach of this Regulation in submitting the above-mentioned proposal to the IMO. According to the Commission, the EU had exclusive competence to deal with a matter of this nature. Part of the Commission's arguments reads as follows: "[T]he Community has enjoyed exclusive competence to assume international obligations in the area covered by that regulation. It follows, in its submission, that the Community alone is competent to ensure that the standards on the subject are properly applied at Community level and to discuss with other IMO Contracting States the correct implementation of or subsequent developments in those standards, in accordance with the two measures referred to. The Member States therefore no longer have competence to submit to the IMO national positions on matters falling within the exclusive competence of the Community, unless expressly authorised to do so by the Community."

The Court of Justice of the European Union (the EU Court) stated,

with reference to the articles of the EC Treaty already mentioned above, that the Member States both must take all appropriate measures to ensure fulfilment of the obligations arising out of the EC Treaty or resulting from action taken by the institutions and also must abstain from any measure which might jeopardise the attainment of the objectives of the Treaty. The provisions of Regulation 725/2004 were Community rules promulgated for the attainment of the objectives of the Treaty. The next question was whether Greece, by submitting to the IMO the contested proposal, could be regarded as having assumed obligations which might affect the provisions of Regulation 725/2004. The Court stated in this respect that Greece had submitted a proposal to the IMO which initiated a procedure that could lead to the adoption by the IMO of new rules in respect of the SOLAS Convention and the ISPS Code. Such an adoption would thus have an effect on Regulation 725/2004.

The ECJ clarified that the exclusive competence of the Union did not prevent a Member State from actively participating in the IMO work so long as the views of the Member States in this regard had been coordinated beforehand at Union level. This clarification was very important and in *Commission v Greece* such coordination had not taken place. The Court also stated that the mere fact that the Union was not a member of an international organisation in no way authorised a Member State, acting individually in the context of its participation in an international organisation, to assume obligations likely to affect Union rules promulgated for the attainment of the objectives of the Treaty. The fact that the Union was not a member of an international organisation did not prevent its external competence from in fact being exercised, in particular through Member States acting jointly in the Union's interest. According to the ECJ, Greece, by submitting the contested proposal to the IMO, had failed to fulfil its obligations under Articles 10, 71 and 80 (2) EC.

The *Greece* case is, at least partly, based on a previous ECJ judgment dealing with similar issues, the *AETR* case, *Commission v. the Council* 22/70 (31.3.1971). In other words, the legal framework underlying the

judgment had existed since the time of the European Economic Community.

Looking at the situation before the changes following from the Lisbon Treaty, the *Greece* case shows that once EU legislation has been enacted that is based on IMO rules and/or standards, the possibilities are limited for any Member State independently to take a legislative initiative within the IMO. In such a case only coordinated action by the Member States is possible. Perhaps the *Greece* case also indicates a certain political change within the Union. Coordination has not necessarily always been accurate or precise, but this case establishes the increasingly significant role of the Union in relation to other international legislative units, including the IMO.

The TFEU, to a greater extent than the EC Treaty, includes specific provisions on Union competence, particularly on internal competence. According to Article 2 TFEU, exclusive competence for the Union means that only the Union may act as a legislator and enact legislation that not only binds the Member States, but also prevents them from being active independently within international legislative organisations. A Member State may only act in such a way either if it is so authorised by the Union or if it is implementing Union rules. If the Union has shared competence, both the Union and the Member State may act as legislators. In this situation the Member States may act, but only to the extent that the Union has not exercised its competence. Further details are contained in the above-mentioned article.

The exclusive competence of the Union is defined in Article 3 TFEU. According to Article 3 (2), the Union shall also have exclusive competence for the conclusion of an international agreement when its conclusion is provided for in a legislative act of the Union necessary to enable the Union to exercise its internal competence, or insofar as its conclusion may affect common rules or alter their scope.

According to Article 4 TFEU, the Union shall share competence with the Member States in specified areas, which include both environment and transport. In matters of shared competence, the principle of subsidiarity is applied as specified in Article 5 TEU.

As already stated, the EU is not party to MARPOL and thus also not to Annex VI. Simultaneously, however, the EU is applying Directive 32/1999 relating to a reduction in the sulphur content of certain liquid fuels [and amending Directive 12/1993] (the Sulphur Directive). The 1999 Directive has been amended by Directive 33/2005.

As the EU has exercised its competence through the Sulphur Directive, no Member State can introduce legally binding provisions affecting the same subject-matter that conflict with the Sulphur Directive. It also seems clear that no Member State can act independently within the IMO in an attempt to obtain new amendments to MARPOL Annex VI by, for example, abolishing the SECAs or introducing higher limits in the SECAs than those currently existing on the basis of the 2008 amendments.¹⁵ The *Greece* case provides the framework for actions by any Member State within the IMO. The result is that the possibilities to take such action are either non-existent or extremely limited unless there has been prior coordination within the Union decision-making process. However, it should be remembered that the *Greece* case concerned the exclusive competence of the EU.

Nevertheless, to influence the Union on the basis of mere policy issues containing less restraints on air pollution, particularly in today's world with its heavy emphasis on air pollution prevention, is obviously difficult, and, rather, impossible.

5 EU law and conflicts with international conventions

EU competence in relation to the IMO can also be analysed from another angle. Namely, what is the EU's legislative position where one or more Member States are bound by an IMO convention? In other words, at least in principle might it be possible for the EU, in the case of the IMO's stricter sulphur emission limits, to enact provisions that dif-

¹⁵ In a political context such a development does not seem possible.

ferred from those of the IMO, even if all or at least some of the EU Member States would be bound internationally by the IMO provisions?

Such questions arose in the *Intertanko* case C-308/06 (3.6.2008). Certain international shipping organisations had commenced proceedings before a UK court alleging that Directive 35/2005 on ship-source pollution and on the introduction of penalties for infringements was in conflict with EU law. The national court requested a preliminary ruling from the ECJ, firstly as to whether the Directive was in conflict with certain provisions of MARPOL and UNCLOS, and secondly as to whether certain provisions of the Directive could be considered invalid. The ECJ noted that the EU was not a party to MARPOL. The court further stated that it did not appear that the Community had assumed, under the EC Treaty, the powers previously exercised by the Member States in the field to which MARPOL applied, nor that, consequently, its provisions had the effect of binding the Union. In this regard, MARPOL could be distinguished from GATT 1947 within the framework of which the Union had progressively assumed powers previously exercised by the Member States, with the consequence that it had become bound by the obligations flowing from that agreement. Accordingly the GATT precedent could not be applied in the present case. In the absence of a full transfer of the powers previously exercised by the Member States of the Union, the Union could not simply - because all those states were parties to MARPOL - be bound by the rules set out therein, which the Union had not itself approved. Likewise, the fact that parts of MARPOL had been implemented in Directive 35/2005 was not sufficient for it to be incumbent upon the court to review the Directive's legality in the light of MARPOL. As such, Union competence must be exercised in observance of international law, including provisions of international agreements insofar as they codified customary rules of general international law. No such expression of customary international law could be found in respect of the MARPOL provisions at stake in this particular case.

In the above-mentioned circumstances, it was clear that the validity

of Directive 35/2005 could not be assessed by the ECJ in the light of MARPOL, even though the latter was binding for the Member States individually. The fact that this Convention was binding for the Member States was, however, liable to have consequences for the interpretation of, firstly, UNCLOS and, secondly, the provisions of secondary law which fell within the field of application of MARPOL. In view of the customary principle of good faith, which formed part of general international law, and of Article 10 EC, it was incumbent upon the ECJ to interpret those provisions taking account of MARPOL.

The conclusion in the *Intertanko* case was that the validity of Directive 35/2005 could not be decided in the light of the effect of MARPOL, even though all EU Member States simultaneously were parties to MARPOL. The exceptions to this would have been either the transfer of Member State competence to the Union or a binding effect on the Union based on customary international law. Neither exception was applicable in this particular case.

As this author understands *Intertanko*, the ECJ also provided a statement on whether MARPOL could influence the interpretation of the Directive. Such a “MARPOL effect” on the interpretation of the provisions of the Directive, being secondary law, was possible, provided that those provisions fell within the field of application of MARPOL. Thus, it seems that the ECJ adopted a position both on the issue of the validity of Directive 35/2005 in the light of international law and, to a limited extent, on the interpretation of the Directive.

Certain other legal issues were dealt with in *Intertanko*, but there does not seem to be any need to analyse them here.¹⁶

The *Intertanko* case means that the Union *legally* has an extensive possibility to act independently of international agreements that it is

¹⁶ In reviewing any possible conflict between Directive 35/2005 and UNCLOS, the ECJ found that UNCLOS did not establish rules intended to apply directly and immediately to individuals and to confer upon them rights or freedoms capable of being relied upon against States, irrespective of the attitude of the ship’s flag State. It followed that the nature and the broad logic of UNCLOS prevented the Court from being able to assess the validity of a Union measure in the light of that Convention. This view concerning UNCLOS means that a private legal subject cannot refer to UNCLOS as the basis of the subject’s rights.

either not a party to or otherwise bound by in pursuing legislative work and legislation. This possibility is not hindered even by the fact that all Member States may be bound by a particular international agreement. In cases of conflict, Union law has priority over Member State obligations based on any such agreement. There are some exceptions that have been mentioned above in connection with *Intertanko*. This conclusion regarding the EU's legislative independence of international agreements seems to be relevant in relation to the Sulphur Directive.

What is quite another matter, however, is how the Union decides to act in *political terms* concerning air emission limits.¹⁷

The above-mentioned *Greece* case shows the limited possibilities for Member States to influence IMO legislative work without coordination within the Union. And while the *Intertanko* case shows the extensive competence of the EU, simultaneously it should be remembered that the Member States influence policy issues within the Union, which is not an entity detached from Member State influence. The reality is, however, that the exercise of decision-making power within the Union is particularly difficult for small Member States unless they have the support of one or more of the larger Member States. This observation is, in itself, nothing new.

When applying all these rules, principles and outlines to the present situation of MARPOL Annex VI and the 2008 sulphur emission limits in SECAs, it seems quite clear in legal terms that no particular Member State can independently pursue within the IMO any request to amend this Annex unless any such request has previously been coordinated within the Union. Should coordinating measures have been concluded satisfactorily, any Member State may pursue an amendment along these lines within the IMO.

Internally, it is legally possible for the EU to enlarge the areas of application of the air emissions requirements that have been adopted in MARPOL Annex VI. The Baltic Sea, the North Sea and the English Channel are SECAs, but the EU could level the playing field by legal means by enlarging these areas to cover all EU territorial waters and

¹⁷ Cf. Birnie & Boyle & Redgwell p. 336.

EEZs. The real question, however, is how Member States not so far affected by the special SECA limits might react politically to such an enlargement.

In dealing with issues of this nature, Article 11 TFEU must be considered. This provision states that environmental protection requirements must be integrated into the definition and implementation of the Union's policies and activities, in particular with a view to promoting sustainable development. This provision corresponds with what has been regulated in Article 3 (3) TEU. Also in the above-mentioned respect any air emission requirements going beyond MARPOL would lead to EU law having priority, as stated already, notwithstanding some exceptions.

6 EU law on equality, non-discrimination and proportionality

There is a further important legal aspect to EU law. This has to do with equality, non-discrimination and proportionality. In view of the matters dealt with in this article, it is topical to ask whether a SECA imposed by means of the Sulphur Directive is in accordance with certain fundamental rules and principles of EU law. This question has become more relevant than before in view of industry concerns regarding the compatibility of stricter sulphur emission levels in SECAs following the probable adjustment of the Sulphur Directive.

A legal debate could arise in view of the fact that the Sulphur Directive distinguishes different sea areas in the same manner as Marpol Annex VI.

Since its very beginnings the common market has been established and secured on the basis of the familiar four freedoms: the free movement of goods, of persons, of services and of capital. These freedoms are supplemented by the important rule on the right of establishment of business undertakings as further specified in Article 49 *etc.* TFEU.

These principles are given particular protection, as shown, for example, in the case of *Commission v United Kingdom* C-246/89 (4.10.1991) concerning registration rights for vessels.

According to Article 56 TFEU (Article 49 EC), restrictions on the freedom to provide services within the Union shall be prohibited as further specified in this provision. It is possible to extend this right to nationals of a third country, also as specified. There is a reference in Article 62 TFEU (Article 46 EC) to some restrictions found in Articles 51 to 54. In this connection it is relevant to refer to Article 52 TFEU (Article 46 EC), according to which there is a possibility of restrictions laid down by law, regulation or administrative action providing special treatment for foreign nationals on grounds of public policy, public security or public health. These grounds for restricting free movement of services are at the disposal of the Member States for use in their national law.¹⁸

The TFEU (like its predecessors) provides that maritime transport is dealt with separately from the explicit Treaty provisions. In 1986, a specific maritime package was introduced. One part of this is Regulation 4055/86 applying the principle of freedom to provide services to maritime transport between Member States and between Member States and third countries. As a matter of fact, the starting points stated on a general level in the Treaty are repeated in the Regulation.

The TFEU prohibits discrimination. This includes Article 18, according to which any discrimination on grounds of nationality is prohibited. Air emissions limits are an example of a situation where direct discrimination might take place. Indirect discrimination is also of legal relevance. Specifying this is particularly important, as discriminatory measures are under certain conditions allowed, which means that a Member State may in some circumstances take discriminatory action on a national basis. It is generally considered that in order to be permissible indirect discrimination must be based on measures justified by

¹⁸ Cf. on free movement of goods and services Birnie & Boyle & Redgwell p. 783.

overriding reasons in the general interest.¹⁹ In order to be so justified, the national legislation in question must be suitable for securing the attainment of the objective which it pursues and must not go beyond what is necessary in order to attain it. The latter requirement reflects the application of the principle of proportionality. The joined *Sea-Land Service* cases C-430/99 & C-431/99 can be referred to as examples.

The Member States cannot restrict the freedom to provide maritime transport services except on grounds admitted by EU law. Another matter is how the *EU itself* in its own legislation must take into consideration the freedoms mentioned above. The starting point in this respect is Article 26 TFEU, according to which the internal market comprises an area without internal borders in which the free movement of goods, persons, services and capital is ensured in accordance with the provisions of the Treaties. According to Article 9 TEU, the Union observes in all its activities the principle of equality of its citizens, who shall receive equal attention from the Union institutions, bodies, offices and agencies. All private subjects must thus be treated on an equal basis under Union law. According to Article 5 (4) TEU, the content and form of Union action shall, under the principle of proportionality, not exceed what is necessary to achieve the objectives of the Treaties.

The Lisbon arrangements include a number of protocols. The above-mentioned Article 5 (4) specifically refers to Protocol No. 2 on the application of the principles of subsidiarity and proportionality. For the most part this protocol contains procedural provisions concerning the implementation of the principle of subsidiarity, but Article 5 of the Protocol states that “Draft legislative acts shall take account of the need for any burden, whether *financial* or administrative, falling upon the Union, national governments, regional or local authorities, *economic operators* [author’s italics] and citizens, to be minimised and commensurate with the objective to be achieved”.

¹⁹ See especially Mikaela Björkholm: *Fri rörlighet i Europa ur ett sjöarbetsrättsligt perspektiv. En analys av sjömannens och redarens grundläggande friheter* (Doctoral Thesis), Gyldendal Akademisk 2010. Björkholm Chapter 2.2.3.2 in light of the status of seafarers.

Article 5 (4) TEU, when taken together with Article 5 of Protocol No. 2, creates an obligation for the Union to evaluate also such actual burdens as may fall upon economic operators. The principle of proportionality when applied in this form and the above-mentioned requirement of equal treatment under Union law, added to the specific requirement of non-discrimination on the basis of nationality, mean that the Union must in every case decide whether it is justifiable knowingly and explicitly to put private legal subjects financially and economically in non-equal positions through Union legislation.

When looking at the possibilities for Member States to restrict the above-mentioned freedoms on a national basis due to overriding reasons in the general interest, it seems that financial/economic reasons may not so far have been seen as relevant, or at least this is the impression one gets when considering the *SETTG v Ypourgos Ergasias* (case C-398/95). On the other hand, this particular case involved industrial relations and so it is not necessarily possible to conclude in general terms that all national restrictions based on financial/economic reasons would be prohibited.

It is of course impossible to state with complete certainty where the application of these general principles might lead in respect of each individual legislative act by the Union, but their value as arguments cannot and should not be ignored.

The above-mentioned discussion does not clarify in further detail how the factor of equality/non-discrimination should be taken into account in Union legislation. It is quite clear that there are situations where it is necessary by such legislation to create regional differences within the Union, not least for environmental reasons. It is always relevant to ask where the line between acceptable and non-acceptable Union legislation should be drawn in respect of the four freedoms, the requirement of equality and the requirement of non-discrimination: the line must exist somewhere.

In the case of MARPOL and the Sulphur Directive, the limits on sulphur emissions in any event lead to an “asymmetrical” situation whereby those Member States that are coastal States of SECAs have a

different status than other Member States, including Member States that are the flag States of ships that do not operate in SECAs.

In general terms, it seems that the asymmetrical nature of EU legislation is in many cases accepted. The present Sulphur Directive already imposes special limits on emissions within SECAs. This approach does not seem to deviate from the asymmetrical nature of legislation found elsewhere in Union law.²⁰

A similar situation prevails when the Union has to evaluate whether to become party to a regionally applied/limited treaty and then repeat the respective treaty provisions in Union law. Union involvement in such a treaty puts the Member States in different positions, as some will have regionally based obligations (while others do not). There are several examples: Council Decision 157/1994 on the conclusion, on behalf of the Community, of the Convention on the Protection of the Marine Environment of the Baltic Sea Area (Helsinki Convention as revised in 1992); Council Decision 98/1997 on the conclusion of the Convention for the Protection of the Marine Environment of the North-east Atlantic, including amendments 340/2000; and Council Decision 77/1977 concluding the Convention for the Protection of the Mediterranean Sea against Pollution and the Protocol for the Prevention of the Pollution of the Mediterranean Sea by Dumping from Ships and Aircraft, including amendments 101/1983, 800/1999, 801/1999, 802/1999, 575/2004 and 89/2009.

In the above-mentioned context, the differing status of different EU sea areas caused by the sulphur emissions provisions in MARPOL Annex VI and by the Sulphur Directive are nothing particularly new compared with other previous and current Union legislation.

There are also other examples of sectors in the EU where Member States are dealt with differently. Agricultural subsidies based on Union decisions might be the most striking example. In spite of the basis not being equal as such, this type of activity seems to have been accepted on the whole, at least in legal terms.

²⁰ Cf. MARPOL Annex I covering special areas where there is complete prohibition on operational oil discharges.

Particularly the requirement of non-discrimination has been targeted by the ECJ in cases involving alleged breaches by Member States. This seems to have been especially topical in cases concerning labour relations. For example, in the *Mangold* case C-144/04 discrimination on the basis of age was considered unacceptable, cf. also Directive 78/2000. The same result was established in *Sea Küçükdeveci v Swedex GmbH & Co.* C-555/07 (19.1.2010). There is no obvious black-and-white conclusion, however, that can be drawn from the decided cases.²¹

In the area of the functioning of business undertakings, the case of *Vereeniging voor Energie (VEMW) etc.* C-17/03 (7.6.2005) is especially interesting. This case involved a decision to reserve to a Netherlands company, on a preferential basis, a portion of the capacity of the cross-border system for imports of electricity into the Netherlands. The decision pre-dated the liberalisation of this particular market. Directive 54/2003 concerning common rules for the internal market in electricity prohibited discrimination within the Union electricity market. A Member State had the right to request exemption from this liberalisation, but the Member State in question had not done so. The ECJ did not accept the above-mentioned preference.

In the *VEMW* case the ECJ used a number of arguments in order to reach the above-mentioned conclusion. All those arguments will not be repeated here. One of the main points relevant to the topic of this article was that the Directive in question explicitly required Member States to refrain from all discrimination with regard to the rights and obligations of electricity undertakings. The Directive reflected the general principle of equality.²² According to the ECJ, the prohibition of discrimination required comparable situations not to be treated differently unless the difference in treatment was objectively justified. The plaintiff had referred to a significant economic disadvantage. The ECJ established that

²¹ See further, for example, *Coleman v Attridge etc.* C-303/06 (17.7.2008). See also *Horvath* C-428/07 (16.7.2009) on agricultural subsidies.

²² The Court referred, amongst others, to Case C-280/93 *Germany v Council* [1994] ECR I-4973, paragraph 67, and, in the matter of defence against dumped imports from non-member countries, the judgment of 27 January 2005 in Case C 422/02 *P Chemi-Con (Germany) v Council* [2005] ECR I 0000, paragraph 33..

the situation did involve differential treatment of electricity companies, as access to the market for new operators varied. On the other hand, the Directive allowed access to be refused under certain enumerated conditions. In this case, however, the ECJ found that no such conditions existed.

There were several categories of legal arguments in the *VEMW* case. The judgment shows that the principle of non-discrimination is applied in EU law also in relation to the pursuit of economic activities. It is irrelevant that the judgment concerned a particular Directive. The requirements of equal treatment and non-discrimination as general principles of EU law are clearly established (repeated) in this judgment. For the purposes of this article, it is particularly relevant to refer to paragraph 48 of the judgment, which states that the prohibition of discrimination, which is one of the fundamental principles of Community law, requires comparable situations not to be treated differently unless such difference in treatment is objectively justified. The requirement for different treatment to be objectively justified is absolute.

The *VEMW* case, like much of what has been discussed above, deals with problems on a Member State level. The requirements of equal treatment and non-discrimination included in the Treaty on European Union are, however, on such a supreme level that they do not only bind Member States but also, of course, the Union itself. On the other hand, in reality the preparation of all Union legislation involves internal control mechanisms of such a nature that it seems somewhat improbable that legislation would be passed that contained unacceptable elements of non-equality or discrimination. It is also a fact, as shown above, that EU law permits varying rights and obligations whereby the Member States, or rather economic activities in different Member States, are put in different positions.

With regard to EU law itself, there are examples where the requirements of equality and non-discrimination have been tested. It is interesting to make a comparison here with the above-mentioned situation of conflict between EU law and “national law”. In the case described below, the matter concerned conflict within EU law.

In the case of *Spain v the Council* C-141/05 (8.11.2007), Regulation 27/2005 came under scrutiny because of alleged discrimination. The case concerned fishing quotas in Union waters and activities by Union fishing vessels in other waters. Spain was dissatisfied with the quotas and demanded the annulment of the regulation. Article 20(2) of Regulation 2371/2002, on which Regulation 27/2005 was based, provided that when the Community established new fishing opportunities, the Council was to decide on the allocation of those opportunities, taking into account the interests of each Member State. Spain had applied for quotas that it had not possessed during a transitional period. The Council had rejected Spain's application. Consequently it had become impossible for Spanish vessels to fish in certain zones. Spain introduced three different bases to its claim, of which one was the infringement of the principle of non-discrimination. In its judgment, the ECJ stated that the Council had not infringed the principle of non-discrimination. The arguments applied by the Court were very detailed, dealing simultaneously with fishing quota provisions and the facts connected with the case. Nevertheless, the ECJ provided one statement of particular general relevance as follows:

“40 Compliance with the principle of non-discrimination requires that comparable situations must not be treated differently and that different situations must not be treated in the same way unless such treatment is objectively justified (see, *inter alia*, Case C 44/94 *Fishermen's Organisations and Others* [1995] ECR I 3115, paragraph 46; Joined Cases C 87/03 and C 100/03 *Spain v Council*, paragraph 48; and Case C 134/04 *Spain v Council*, paragraph 28).”

The Union legislature must thus take into consideration the same general principles as must the Member States in view of their respective national laws. Like the *VEMW* case, the *Spain* case also included a reference to objectively justified grounds. In addition, under these circumstances the principle of proportionality also has to be continuously taken into account by the EU legislature.

A case more closely akin to the situation with sulphur emissions

than the fishing quotas case mentioned above was the case of *Société Arcelor et Lorraine etc. v Premier ministre etc.* C-127/07 (16.12.2008). The EU had by Council Decision 69/1994 become a party to the United Nations Framework Convention on Climate Change and, thereafter, by Council Decision 358/2002 had approved, on behalf of the European Community, the Kyoto Protocol to the United Nations Framework Convention on Climate Change.²³ These treaties deal with the prevention of greenhouse gas emissions and with trading in emissions allowances. Due to its treaty obligations, the EU adopted Directive 87/2003 establishing a scheme for greenhouse gas emissions allowance trading within the EU. The Directive included some recitals that were relevant to the case. Two amending proposals were subsequently made in order to include aviation activities and new industrial categories such as the production and processing of non-ferrous metals, the production of aluminium and the chemicals industry. Directive 87/2003 was transposed into French law in 2004. The steel sector in France requested the competent French authorities to repeal the relevant parts of the French legislation as being, *inter alia*, contrary to the principle of equal treatment. This part of the case was referred to the ECJ for a preliminary ruling. The question was whether Directive 87/2003 was valid in the light of the principle of equal treatment, insofar as it made the allowance trading scheme applicable to installations in the steel sector without including in its scope the aluminium and plastics industries. The ECJ repeated the principle that non-equal treatment might be allowed when objectively justified. The Court also established that the steel, chemical and non-ferrous metal sectors were, for the purposes of examining the validity of Directive 87/2003 from the point of view of equal treatment, in a comparable position while being treated differently. It was established as such that the inclusion of an economic activity within the scope of Directive 87/2003 created a disadvantage for the operators concerned in relation to those carrying on activities not so included. Even if being subject to such a scheme did not necessarily and systematically entail unfavourable economic consequences, the existence of a disadvantage

²³ See for further background Birnie & Boyle & Redgwell pp. 340 *et seq.*

could not be denied for that reason alone, since the disadvantage to be taken into account from the point of view of the principle of equal treatment might also be such as to affect the legal situation of the person concerned by a difference in treatment.

The above-mentioned section of the ECJ's judgment would provide a favourable starting point for an industry concerned about - and negatively affected by - particular EU legislation.

The ECJ, however, also looked closely at the question of justification for different treatment, which must, as stated above, be objectively justified. The Court acknowledged that justification could be found if it were based on an objective and reasonable criterion being proportionate to the aim pursued by the treatment. It was established by the Court that the Community would have wide discretion in a situation where political, economic and social choices were involved, and where complex assessments and evaluations were needed. In complicated restructuring, a step-by-step approach was considered acceptable.²⁴ In all situations, however, objective criteria were necessary.²⁵ The Court also referred to the principle of proportionality. In this respect the ECJ stated that "... it must be considered that, even if the importance of the objectives pursued is such as to justify even substantial negative economic consequences for certain operators, the Community legislature's exercise of its discretion must not produce results that are manifestly less appropriate than those that would be produced by other measures that were also suitable for those objectives."²⁶

The conclusion was that the EU would have broad discretion in

²⁴ The Court referred to Case C 344/04 *IATA and ELFAA* [2006] ECR I 403, paragraph 80), Case 37/83 *Rewe-Zentrale* [1984] ECR 1229, paragraph 20; Case C 63/89 *Assurances du crédit v Council and Commission* [1991] ECR I 1799, paragraph 11; and Case C 233/94 *Germany v Parliament and Council* [1997] ECR I 2405, paragraph 43.

²⁵ Case 106/81 *Kind v EEC* [1982] ECR 2885, paragraphs 22 and 23, and *Sermide*, paragraph 28, Case C 284/95 *Safety Hi-Tech* [1998] ECR I 4301, paragraph 51.

²⁶ Reference was made to, concerning measures relating to agriculture, Joined Cases C 96/03 and C 97/03 *Tempelman and van Schaijk* [2005] ECR I 1895, paragraph 48, and Case C 504/04 *Agrarproduktion Staebelow* [2006] ECR I 679, paragraph 37. See also Case C 331/88 *Fedesa and Others* [1990] ECR I 4023, paragraphs 15 to 17, and Case C 86/03 *Greece v Commission* [2005] ECR I 10979, paragraph 96.

finding justification for non-equal treatment. The principle of proportionality had to be applied as specified. The word “manifestly” in this context reiterates what had already been said, *i.e.*, that the legislature has a broad discretion.

Referring to the particular Directive more concretely, the ECJ stated that Directive 2003/87 was a novel and complex scheme that could have been disrupted by the involvement of too many participants. This justified the adoption of a step-by-step approach whereby experience would be gained in the first stage of implementation. Acceptance of such an approach depended, however, on regular reviews of the situation. Including the chemical sector within the scope of the Directive would have made the (para. 65) “management of the allowance trading scheme more difficult and increased the administrative burden, so that the possibility that the functioning of the scheme would have been disturbed at the time of its implementation as a result of that inclusion cannot be excluded”. Exclusion from the scope of the scheme at this particular initial stage had more advantages than disadvantages. The ECJ accepted that the EU legislature had properly made use of objective criteria.

The final conclusion of the ECJ was that the difference in treatment between the chemical sector and the steel sector had been justified. The Court also accepted different treatment of the non-ferrous metal sector, basing its conclusion on the need for the allowance trading scheme to be administratively feasible in its initial stage. Thus, the EU legislature had not infringed the principle of equal treatment by treating comparable situations differently when excluding the chemical and non-ferrous metal sectors from the scope of Directive 2003/87. The validity of this Directive was not affected by the principle of equal treatment.

The *Soci t  Arcelor* case raises further criteria of great importance with regard to all kinds of different treatment by the EU legislature on a sector-by-sector basis. That the steel sector’s case failed had partly to do with the fact that the inclusion of different industrial sectors in the trading system was planned to take place gradually. This meant that the non-equal treatment was only temporary. As the administrative burden of including all sectors would have been too great, the legislature’s step-

by-step approach was considered justified. Such arguments with regard to justification would also not be irrelevant when considering the different geographically based sulphur emission limits within the EU.

Could the criteria applied in the *Soci t  Arcelor* case be applicable in relation to the Sulphur Directive and, if so, could they be used to establish that a SECA violates the principle of equal treatment, the principle of non-discrimination or the principle of proportionality? In some ways it seems that the emphasis in the *Soci t  Arcelor* case on a stage-by-stage approach and on the feasibility of administration were more concrete criteria that could not easily be adapted to the potential problems posed by the Sulphur Directive and SECAs. Such considerations are related, however, to the need to establish further facts concerning the economic and administrative consequences of SECAs and the alternative of maintaining similar limits on sulphur emission in all EU waters. Several feasibility studies are available.²⁷ Once the existence of a non-equal position has been established, it is for the Commission to prove that the non-equal treatment of different commercial actors is objectively justified as, for example, was established in the *Soci t  Arcelor* case.

²⁷ See *Study to review assessments undertaken of the revised MARPOL Annex VI* submitted by the International Chamber of Shipping, MEPC 61/INF.10 13 July 2010. This is one of many. See *European Commission - Environment* per November 10, 2010: http://ec.europa.eu/environment/air/transport/ships_directive.htm. This source includes an enumeration of several studies, among them a more general study that covers different aspects of the revision of the Sulphur Directive. The study will calculate the costs and benefits of the IMO agreement and different ways of EU implementation, as well as of changes to sulphur levels of other fuels covered by the Directive. The European Maritime Safety Agency has also produced a report that contains an overview of the available studies related to the impact of future fuel standards set by the 2008 amendment to MARPOL Annex VI for fuels to be used in particularly sensitive areas.

7 Conclusions

Legal arguments against the SECA system contained in MARPOL Annex VI are difficult to find, but certain formalities might provide some possibilities to avoid coming within the scope of application, such as not accepting the 2008 amendment. Such measures will not necessarily be all that effective, however, given that the operational area of the ship is so significant. Political pressure is another matter.

EU law presents more interesting possibilities, as the SECAs potentially give rise to a debate about the requirements of equal treatment, non-discrimination and proportionality.

In spite of the fact that the EU has accepted varying treatment of the Member States and groups of private legal subjects in its own legislation on different sectors, the legal picture seems to be that such solutions can only exceptionally form the basis for challenging a particular piece of EU legislation. Equal treatment of and non-discrimination between the Member States are fundamental principles, but with the possibility of certain exceptions. The situations in which the fundamental principles or the exceptions shall apply have been tested in the ECJ. Whether such debating points are valid with regard to the IMO-based rules on limits on sulphur emissions from ships that will be implemented through the Sulphur Directive is another matter.

There is no possible way of predicting the correct and acceptable level of proof in terms of EU law.

The *Greece* and *Intertanko* cases dealt with above show that the legislative flexibility of EU law is considerable when the EU is not party to a particular treaty. This flexibility remains unchanged even where all the Member States are party to a treaty. The EU is not party to the IMO maritime safety conventions, and thus not to MARPOL. When considering this flexibility, it should of course be remembered that the EU must not exceed its own competence. It should also not be overlooked that, as already mentioned, the EU is *de facto* linked to general global developments regarding air emissions.

To satisfy strict environmental principles, there is always the possibility of accepting low levels of sulphur emissions from ships throughout the EU's sea area without differentiation. The EU's flexibility means that the EU may, for example, legally lower limits on sulphur emissions to, say, 0.10 % in all EU waters. Whether this would be either practical or politically acceptable is, as already said, more questionable.

In legal terms the real conflict, if any, lies between, on the one hand, the generally accepted benefits of controlling air emissions in general, including emissions from shipping, as a part of a serious effort to promote global environmental protection and, on the other hand, the problems of a particular sector not having a level economic playing field – especially considering that the EU currently is emphasising the principles of equality and non-discrimination.

The impact of the Rotterdam rules on general average

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1 Introduction¹

The title of this study is the impact of the Rotterdam Rules² on general average.³ This may seem slightly odd, as the study covers both the Rotterdam Rules and the York Antwerp Rules. These two sets of rules seem to upset people in all different quarters.

First some words on the scepticism towards general average. Today there are still people who smile sceptically before asking, “Ah, general average! Is that old dog still around?”⁴ Further, not many people know what general average is actually all about. And among those who do, it is quite clear that the institution is widely disliked. Criticisms of general average fall into several main categories, with the concept being described as too old-fashioned, too time-consuming, too complicated as well as unnecessary in a world with modern marine insurance.⁵ It seems easy enough to agree with these criticisms and I am convinced that Hans Jacob Bull, as the master mind behind the Norwegian Marine Insurance Plan, agree on that. Even so, as he so rightly has pointed out, general average has shown an extraordinary ability to survive the most

¹ This article is based on work undertaken by the author in connection with the AMD Forum in Marrakesh, November 2009, in which Hannu Honka, Regina Asariotis and Francesco Berlingeri held talks, together with papers presented at the open meeting of the Canadian Maritime Law Association in Montreal, March 2010 and at the meeting of the Insurance and General Average Committee of the U.S. Maritime Law Association in New York, May 2010.

² United Nations Convention on Contracts for the International Carriage of Goods Wholly or Partly by Sea, adopted by UN General Assembly on December 11, 2008, signed at a signing ceremony held in Rotterdam on September 20, 2009. The new Convention has become known as the Rotterdam Rules.

³ General average is mad up in accordance with the York Antwerp Rules (YAR), normally still in accordance with the YAR 1994, but sometimes in accordance with the newer YAR 2004.

⁴ See Pineus & Sandström “The Hamburg Rules from the Average Adjuster’s point of view” in *Nordisk Försäkringstidskrift* 1978 p. 163 at 165.

⁵ See, e.g., Tetley, *International Maritime and Admiralty Law*, 2002, p. 395 and Lowndes and Rudolf. *The Law of General Average and The York-Antwerp Rules*, 12th ed., by Wilson & Cook, Appendix 5.

hostile attacks.⁶

The Rotterdam Rules have also been the target of a good deal of criticism.⁷ For many years, firstly within the CMI and finally within UNCITRAL, efforts were made to agree new rules for international carriage by sea. The goals were: 1) to provide an effective replacement for the Hague, the Hague-Visby and, where applicable, the Hamburg Rules; and 2) to extend the scope of the earlier regimes by covering many more issues, e.g., multimodality. After many years' work, a new set of Rules finally saw the light of day.

So far the Rules have been signed by over 20 states. They will come into force within one year of the deposition with the UN of the 20th instrument of ratification (or similar instrument). So far,⁸ one State has ratified the Rules.⁹ Friends of the Rules around the world are quite confident that, despite the criticism, the new Rules will become a fact sooner rather than later. Meanwhile, even though the Rules may take some time to enter into force, it is still of some interest to consider their impact on general average.

As a point of departure, there seems to be a general assumption that the Rotterdam Rules will be the death of general average. At the very least, it is thought that shipowners will be more reluctant to declare general average.¹⁰ This article attempts to provide some thoughts about the correctness of that assumption.

⁶ See, e.g., Bull, "Haveri grosse – fortidslevning med fremtid" in *Marius* no. 190, 1992, p. 60.

⁷ See, e.g., *A response to the attempt to clarify certain concerns over the Rotterdam Rules published 5 August 2009*, published by Barry Oland, Kay Pysden, Professor Jan Ramberg, Professor William Tetley, Douglas W. Schmitt and Professor Svante O. Johansson, endorsed by Jose Alcantara, Julio Vidal and Frazer Hunt. This was a response to the Informal document WP.24 No.2 (2009) of the Economic Commission for Europe under the name of *Rotterdam Rules: An attempt to clarify certain concerns that have emerged* signed 5 August 2009, by Francesco Berlingieri, Philippe Delebecque, Tomotaka Fujita, Rafael Illescas, Michael Sturley, Gertjan van der Ziel, Alexander von Zeigler and Stefano Zunarelli.

⁸ February 7, 2011.

⁹ The state is Spain.

¹⁰ Cf. Neame, "What impact will the Rotterdam Rules have on ship Owners?" in the July 2010 issue of *Britannia News*.

2 The Issue at stake

2.1 The concept of fault and general average

General average is established according to the York Antwerp Rules (YAR). YAR Rule A states that contribution in general average can be claimed, if an extraordinary sacrifice or expenditure intentionally and reasonably is made against a peril in order to benefit the common adventure.

However, a claimant, whether ship or cargo, is *not* entitled to obtain contribution in general average simply because his or her sacrifice or expenditure falls within Rule A. An additional element is required. This follows indirectly from the wording of YAR Rule D:

Rights to contribution in general average shall not be affected, though the event which gave rise to the sacrifice or expenditure may have been due to *the fault of* one of the parties to the adventure; but this shall not prejudice any remedies or defences which may be open against or to that party in respect of *such fault* [italics added].

On the one hand, this means that no provision of law, national legislation, or rule in international conventions has any say in respect of the adjustment of general average. On the other hand, the parties are left free to dispute any issues concerning fault and its effect at a later stage.¹¹

Accordingly we have a two-step system for claims for general average contributions. This system has been criticised, as the first step may turn out to have been unnecessary if fault is identified at the second step. The system is nevertheless confirmed in the Rotterdam Rules, which state in Article 84 RR that nothing in the convention affects the adjustment of general average. The article is silent as to other questions and mentions

¹¹ This is also the case under U.S. jurisdiction, at least in those instances where a Jason or New Jason Clause is used, which is the normal procedure.

neither fault¹² nor time bar.¹³

Expenses made in pursuit of common safety will thus continue to be apportioned between the ship, freight and cargo. Forwarding charges from the port of refuge to the port of destination will continue to be allowed – in accordance with the principle of common benefit – as substituted expenses, up to savings obtained to general average. Losses sustained where cargo is either jettisoned or damaged by fire-extinguishing operations will be distributed as general average.

This situation exists because it is *not* the average adjuster's task to pinpoint the question of fault and put the blame on one or other of the parties. In fact, the York Antwerp Rules specifically state that he or she shall not do so.¹⁴

2.2 What fault?

The general rule for the collection of contributions in general average is that the party at fault cannot claim contributions from other parties that are not at fault. But on what grounds should we assess the existence of fault? And what types of faults exclude entitlement to contributions?

Firstly, as a point of departure, the owner of a contributing value in general average is liable to contribute. Normally, however, there is a legal relationship between the party claiming contribution and the defending party. We should note that the courts tend to investigate that relationship in order to determine whether the claimant is at fault. Normally there are contracts of carriage or similar contracts dealing with the liabilities of the different parties. In order to decide whether a claim will be upheld, it is necessary to scrutinise the contractual provisions of each and every contributing interest. If there is an exemption

¹² It should be noted that Article 84 RR does not repeat the wording of Article 24.2 of the Hamburg Rules, which explicitly states that the consignee may refuse contribution. The different wording seems to have no effect in substance.

¹³ Articles 62 and 65 RR, like the Hague-Visby Rules, do not include any provision regarding the time bar of claims for contribution. The provision regarding general average in Article 24.2 Hamburg Rules excludes the general time-bar rule. Note, however, that a time bar provision is included in Rule XXIII YAR 2004.

¹⁴ Pineus & Sandström, *op cit.*, p. 166.

clause that excludes the liability of the claiming party, a contribution can be claimed with success. If the relevant clause does not exclude liability but, *e.g.*, only limits liability, no claim for a contribution will be upheld. It seems to make no difference whether the legal relationship is based on contract or statutes derived from international conventions.¹⁵

Secondly, one problem with the concept of fault in the context of general average is that fault normally causes losses for which the cargo interests might claim damages from the carrier. In general average, however, losses will not necessarily arise. Contributions may be claimed even if no entitlement to damages arises from the general average event. As an example, consider the following scenario.¹⁶

Although the contract of carriage imposes an obligation on the carrier to exercise due diligence to make the ship seaworthy, the ship is unseaworthy at the commencement of the voyage, due to want of due diligence on the part of the owner. During the voyage the ship and cargo encounter danger. The master engages towage assistance to get the ship and cargo out of danger. This is a general average act and the cost of hiring towage should be distributed over the contributing values. The act also prevents damage to the ship and cargo, in respect of which an action for damages would have succeeded. Since the cargo is not damaged, however, no claim for damages will be supported. From this conclusion it might easily be argued that the cargo interests will have no defence if the shipowner claims a contribution in general average for the cost of hire.

If the towage had not been instigated both the ship and cargo might have been severely damaged. Let us suppose that the ship and cargo were salvaged, but in a damaged condition. The shipowner can, at least if the YAR 1994 apply, claim contributions in general average for the salvage award. Under such circumstances the cargo interests would have a valid claim for damages. In addition, it is quite clear that the cargo interests would have a defence against claims for contributions

¹⁵ See Lowndes and Rudolf. *The Law of General Average and The York-Antwerp Rules*, 13th ed., by Cook & Cornah, para. D.04.

¹⁶ The example is inspired by the text in *ibid.* para. D.03.

from the shipowner, who was at fault. In other words, the cargo interests have a defence against claims for contributions where there is so-called actionable fault.

Accordingly the test for an actionable fault is whether, if the general average act had not been performed (with the result that the peril would have taken effect), the person claiming the contribution would have been legally liable to the party against whom contribution is claimed.¹⁷

3 The Rotterdam Rules and carrier's fault

3.1 Scope of the Rules

To draw any conclusions regarding the impact of the Rotterdam Rules on general average, we must consider the scope of the Rules, which is established using a slightly different approach to that taken by the Hague-Visby Rules and the Hamburg Rules. All three sets of rules exclude non-liner trade from their scope. The scope of the Hague-Visby Rules, however, unlike that of the Rotterdam Rules, depends not on the trade but on the document issued, *i.e.*, the bill of lading. As regards third parties, all three sets of rules seem to include these within their scope of application, but the Rotterdam Rules are not restricted to the bill of lading holder only.

Although Article 6 RR states that the Convention does not apply to non-liner trade, this statement is revoked immediately by Article 7 RR, which provides that notwithstanding Article 6, the Convention does apply in non-liner trades as between the carrier and a consignee who is not the original party to the charterparty.¹⁸

For example, where a charterer ships his own cargo, the Convention is not applicable. If, however, the original charterer sells the cargo during the voyage, then the Convention applies as between the new

¹⁷ *Ibid.* D.03.

¹⁸ See, *e.g.*, Baatz *et al.*, *The Rotterdam Rules – a practical annotation*, 2009, p. 19 *et seq.*

cargo owner and the carrier. This is normal practice in many domestic legislative systems regarding sea carriage, e.g., the Nordic Maritime Codes. Accordingly it seems that the Rotterdam Rules will apply to a majority of non-liner shipments.

In the case of volume contracts, however, we should note that under the Rotterdam Rules the parties to the contract of carriage can agree to other terms than those stated in the Rules. This follows from Article 80 RR. A volume contract means a contract that provides for the carriage of a specified quantity of goods in a series of shipments during an agreed period. Such an agreement could provide for the transport of just two containers in the course of three months. Such an agreement would be valid – subject to some additional conditions – in respect of a consignee who is not the original party to the volume contract. Some duties cannot be excluded, most importantly the obligation of the carrier, which follows from Article 14 RR, to exercise due diligence to make and keep the ship seaworthy.

This opt-out concept might be apprehended as a wicked plot on the part of the shipowners. In reality the idea was driven by US cargo interests, who signed away some of their rights in return for low freight rates. It remains to be seen how this opt-out clause will function in practice.

3.2 The carrier’s qualified presumed fault liability

The carrier’s fault-based liability is dealt with in Article 17 RR. This lengthy provision applies to cargo claims under the Rules and expressly stipulates – by means of a rather complicated ping-pong approach – how the burden of proof is allocated as between the cargo interests and the carrier. The approach appears very similar to that taken in the Hague-Visby Rules, but the text is significantly different, both in structure and wording. Supposedly this will also have an effect on the outcome in substance.¹⁹

¹⁹ Asariotis “Loss due to a combination of causes” p. 146 and Thomas “Liability regime of carriers and maritime performing parties” p. 61, both in *A new convention for the Carriage of Goods by Sea – the Rotterdam Rules*, 2009, D.R. Thomas (Ed.) p. 146.

This is not the place for a thorough discussion of different aspects of the Rules.²⁰ In order to understand the impact of the Rules on general average, we can make do with an overview of the liability regime.

As a point of departure, the carrier is personally, as well as vicariously, liable if the cargo claimant proves loss, damage or delay (in the interests of brevity, we refer hereinafter only to loss) during the period of liability. This follows from Articles 17(1) and 18 RR.

If the claimant succeeds in establishing that damage occurred during the relevant period, then the carrier's fault is presumed.

The carrier may be relieved of all or part of the liability on one of two grounds. Firstly, the carrier will be relieved of all or part of its liability if it can prove absence of fault in respect of the cause or one of the causes of the loss. This is clear from Article 17(2) RR. The carrier has to prove either absence of fault or absence of a causative link between the faulty action and the loss.

Secondly, the carrier will be relieved of all or part of its liability if it can prove that the loss was caused or contributed to by an event or circumstance listed in Article 17(3) RR. This list is similar to that found in the Hague-Visby Rules, subject to some deletions and additions. The most important deletion concerns error in management of the ship or navigation. The exception for nautical fault has thus finally been abolished as a defence for the carrier.

Thereafter, Article 17 (4) and (5) RR contains three qualifications regarding the exceptions in 17(3) RR. If the carrier is able to prove a valid defence under the rules in Article 17(3) RR, the burden of proof reverts to the claimant, who may be able to undermine the defence if he is able to prove either

- i) *that* the fault of the carrier, or of a person it is responsible for, caused or contributed to the event or circumstance on which the carrier relies; or
- ii) *that* an event or circumstance not listed in Article 17(3) RR con-

²⁰ See, e.g., Baatz, *et al. ibid.* p. 45 *et seq.*, Asariotis, *ibid.*, and Thomas, *ibid.*, for a more thorough discussion.

tributed to the loss and the carrier cannot prove that this event or circumstance is not attributable to its fault or to the fault of any person it is responsible for.

- iii) *that* the loss was probably caused by or contributed to by unseaworthiness *and* the carrier is unable to prove either that:
 - a) none of the events or circumstances regarding unseaworthiness caused the loss; or
 - b) it complied with its obligation to exercise due diligence in making the ship seaworthy.

Throughout the text in Article 17 RR we find phrases recognising the fact that the loss may have more than one cause. The words “caused or contributed to” are repeated frequently. What does this mean? Article 17(6) RR clearly states the position adopted by the Rules. When the carrier is relieved of part of its liability pursuant to Article 17 RR, the carrier is relieved of part of its liability without having to prove the proportion of loss not due to its own breach.

This should be apprehended as a clarification and a necessary harmonisation for jurisdictions that have applied the Hague-Visby Rules on a “rule-of-exceptions” basis rather than a “rule-of-presumption” basis. Contributory causation is regarded as an accepted concept under the Rotterdam Rules.

However, there seems to be a marked difference to the Hague-Visby Rules, where the carrier could only escape liability to the extent that it could prove that a distinguishable proportion of the loss was due to an excepted peril. This difference could have considerable implications for the practical outcome of cargo claims, where much may depend on the available evidence. Determining what proportion of a loss is attributable to a contributing event seems to be left to the Court’s discretion.²¹ This will inevitably lead to a great deal of uncertainty until case law is settled.

To conclude, there are a couple of major changes in the pattern of liability under the Rotterdam Rules as compared with the Hague-Visby

²¹ Asariotis, *ibid.* p. 148.

Rules. Most strikingly, the carrier's defence of nautical fault is no longer available and a proportional reduction of the carrier's liability is more likely in circumstances where a loss has several contributing causes. The next question concerns the impact of the changes embodied in the Rotterdam Rules.

4 The Rotterdam Rules applied to typical general average cases

4.1 Some statistics regarding causes of general average

In order to shed light on the effects of the Rotterdam Rules, we need some practical scenarios on which to base our discussion. Below we discuss the most common causes for general average, although even these are hard to pinpoint with any degree of accuracy.

The lack of reliable statistical sources is striking. No global statistics exist, forcing one to rely on figures from the various adjusting companies and adjusting associations. There are, however, a couple of reliable estimates regarding the frequency and financial impact of general average.

Causes	Percentage of:	
	Frequency	Financial loss
Engine failure	34.8	8
Collision and contact	23.4	24
Grounding	9.7	29
Weather	7.5	8
Mechanical	7.5	4
Structural	5.6	-
Engine fire	4.5	25
Fire	2.8	
Other	4.2	2
Total	100	100

Some investigations are mainly based on figures from a single region or market.²² In the 1990s a couple of reports attempted to take a wider perspective. Firstly UNCTAD released a report in 1994.²³ Subsequently the IUMI issued a report by M. Marshall to be presented at the meeting held in Oslo in 1996.²⁴ This report has been updated and one such update was prepared for presentation at the IUMI meeting in Singapore in 2004.²⁵ The figures in the table above have been modified to conform to the presentation in that paper.

These figures are not completely reliable. In some markets they vary due to different trading patterns. For example, in the Scandinavian market, with its intense coastal traffic, grounding seems to be the main cause of general average. Nevertheless, the figures give a fairly good picture of the different causes.

Even though it might be possible to obtain figures concerning the causes of general average, these figures would only provide limited information as to the actual causes of the incidents. General average statements do not deal with the question of fault and are not intended to do so. This makes it even harder to say anything about the actual cause of an incident or whether fault was involved.

One way of ascertaining the extent to which fault is a contributory cause of general average is to study reports from various National Maritime Safety Boards. However, such reports do not necessarily have any connection with general average. Even if some general statistical assumptions can be made on the basis of these reports,²⁶ the findings in them are not a reliable way of determining if fault was involved in cases of general average.

Other reports provide some figures, although it is hard to follow

²² Some early reports, with limited scope, can be found in Selmer, *The survival of general average* (1958) and Pineus & Sandström, *ibid.*

²³ *The Place of General Average in Marine Insurance Today* UNCTAD/SDD/LEG/1 (8 March 1994)

²⁴ Marshall, *General Average – A statistical update*, IUMI 1996.

²⁵ Marshall, *General Average – the figures and their relation to the debate on reform*, IUMI, 2004.

²⁶ Cf. Pineus & Sandström, *ibid.*

how these figures have been obtained. The following statement comes from the IUMI report for 1996:

Adding together the casualties which result from the condition of the ship (engine and mechanical failure, those “weather” losses which are more attributable to the ship’s own structural failure than the elements, and fire losses which follow poor engine room maintenance or cargo supervision), we find that this type of loss accounts for over half of all GAs by number. A further 35% result from navigation, mostly involving error. About a third of engine failure losses seem to involve unseaworthiness.²⁷

A later update presents the incidence of negligence in cases of general average. New cases show that fault seems to be acknowledged in about 60 per cent of all cases. In a further 15 per cent, fault seems likely to have been involved. In about 15 per cent the underlying cause of the general average seems to be unseaworthiness. Only in about 10 per cent of the cases is there an absence of fault.²⁸

The following attempts to apply some of these figures to various standard cases of general average in order to discuss the impact of the Rotterdam Rules. The reader is advised to approach the figures referred to with caution, as they represent no more than estimates or qualified guesses as to the actual causes of general average and the incidence of fault.

4.2 Engine failure

Engine failure may be attributed to technical failure, human factors or, sometimes, fire. The exact numbers attributable to each cause are not easy to state. Some reports suggest that about one-third of engine failures are caused by human error, which includes mistakes and misjudgements by those aboard.²⁹ Generally speaking, this represents *error in*

²⁷ Marshall, *General Average – A statistical update*, 1996, p. 4.

²⁸ Marshall, *General Average – the figures and their relation to the debate on reform*, 2004, slides 30 and 31.

²⁹ Pineus & Sandström, *ibid.*, p. 168.

management caused by a human factor. According to the Rotterdam Rules, the carrier will be held liable for nautical fault in such circumstances and the defendant will thus have a valid defence against a claim for contribution.

However, the vast majority of engine failures can be explained by technical factors, for which the carrier normally is free from liability. In such circumstances the shipowner has a good chance of collecting contributions in general average. A couple of points are worth noting here.

As regards engine failure as such, pursuant to Article 14 RR, the shipowner's obligation at the inception of the voyage to ensure the ship is seaworthy is extended throughout the entire voyage. This might affect the shipowner's chances of obtaining contribution in general average. It is not sufficient to service the engine at the loading port; prudent maintenance and checks must also be performed during the voyage.

Cargo interests are currently, and will continue to be, proactive in the event of engine problems. They will request explanations and investigations in order to establish whether the owner exercised due diligence to keep the ship seaworthy. As we saw in section 4.1 above, the IUMI estimates that one-third of engine failures are attributable to unseaworthiness. Under the Rotterdam Rules, the shipowner's claim for contribution will not be valid in such cases. But since this is already the case under the Hague-Visby Rules, the Rotterdam Rules will not have any immediate impact on general average in this regard.

It is also important to note that engine problems generally result from a combination of causes. In cases involving costs in connection with a technical failure of the engine, a claim for contribution in general average may have to be reduced pursuant to Article 17(6) RR if human error contributed to the failure. Even so, it still may be worth making a claim.

In conclusion, claiming a contribution in general average following an engine failure is likely to remain as difficult under the Rotterdam Rules as it is today. This can be explained by the fundamental obligation to keep the ship seaworthy, which is similar in current conventions and the Rotterdam Rules.

4.3 Collision and other contact

Normally a collision or contact with an object other than a ship (sometimes referred to as “allision”) is said to be attributable to nautical fault. Accordingly, under the Rotterdam Rules, the owner will be liable on the basis of fault and will be unable to recover contributions in general average, since the exception for nautical fault has been deleted from the catalogue in Article 17(3) RR.

However, liability in collision cases is, in the vast majority of cases, allocated between the parties according to the degree of fault on each side. Thus the extent of the owner’s liability may turn out to be relatively minor. In such circumstances, pursuant to Article 17.2 RR, the owner will only be held liable for a proportion of the damages, as Article 17.6 RR imposes liability in proportion to the degree of fault. The shipowner will therefore be able to collect contributions to the extent to which fault was attributed to the other ship.

This leads us to the conclusion that, even if the Rotterdam Rules were to apply, general average would be declared in collision cases in very much the same way as today. Situations involving contact might fall away due to the abolition of the nautical fault exemption. Thus we can assume that it will be a little more difficult to claim contributions in general average in collision situations.

4.4 Grounding

As can be seen from the figures in section 4.1 above, the majority of groundings are attributable to human factors, which include mistakes and misjudgements shown by those aboard. Generally speaking, this represents *nautical fault* caused by a human factor. In this case, under the Rotterdam Rules the owner would not be able to rely on any exception for nautical fault. Thus no contribution in general average could be collected from cargo interests.

On closer examination, however, it becomes clear that grounding is often caused by multiple factors. Under the Rotterdam Rules, owners might invoke the provisions of Article 17.6 RR in order to resist claims

for loss or damage or to claim partial contributions in general average. Whether owners will be inclined to invoke these provisions remains to be seen.

In my experience, the owner's chances of success in such an endeavour would be far from good. Would it be worthwhile initiating a general average and collecting security in the knowledge that the amount ultimately to be contributed was very uncertain? Where large amounts were involved, however, the temptation might prove irresistible.

4.5 Structural factors and weather

General average causes categorised as attributable to structural factors or the weather include springing a leak and listing. A vessel that springs a leak on the high seas will normally be considered unseaworthy. The owner will have the burden of proving either that other circumstance intervened, *e.g.*, severe weather conditions, or that due diligence was exercised. This would probably be hard to prove in many cases.

Thus the owner is likely to encounter problems in overturning the presumption of fault with regard to the obligation to ensure the ship is seaworthy both before and during the voyage. Under these circumstances it may be hard to collect contributions in general average. The situation will not, as I understand it, be changed by the application of the Rotterdam Rules. They may even put the shipowner in a better position, as it might be possible to prove that a circumstance or event excluding liability contributed to the leak, in which case Article 17(6) RR would apply. In this case the shipowner would at least be able to collect a partial contribution.

In conclusion, where a general average case is attributable to structural causes, *e.g.*, springing a leak, the Rotterdam Rules will not bring about any negative effects on general average. Much the same is true where a ship starts to list.

4.6 Fire

According to the new convention fire is excluded from the carriers liability. This follows from Article 17(3)(f) RR. Under Article 17(4) RR, however, if the cargo interests were to establish negligence on the part of the owner or its servants, this exclusion would not apply. Any contribution claim would thus fail. The cargo interests' chances of establishing negligence would probably be remote. If so, general average in such situations should continue, as currently, to be distributed over the contributing values.

4.7 A special situation

Many commentators on the Rotterdam Rules have pointed out that the relationship between Articles 17(3)(o), 17(5), 15 and 16 of the Rules is far from clear.³⁰ Articles 15 and 16 RR are referred to in Article 17(3)(o) RR as coming within the excepted list of events. The carrier is relieved of liability for sacrifices of goods in situations covered by Articles 15 and 16 RR, all according to 17(3)(o)RR. If, however, the sacrifice is due to unseaworthiness, pursuant to Article 17.5 RR the carrier is liable, notwithstanding Article 17(3)(o) RR.

In this connection it is important to look at the text of Articles 15 and 16 RR. The effect of the word “notwithstanding” in both Articles 15 and 16 is rather confusing. Article 16 RR seems, on the face of it, to relieve a carrier that would otherwise have been liable of liability for losses due to unseaworthiness. Thus no liability would be imposed on the carrier for cargo loss or damage due to jettison.

If this is right it would be very surprising, as it would mean the abolition of the seaworthiness warranty. However, it does seem unlikely that the carrier could escape any liability for a cargo sacrifice (*e.g.*, jettisoning cargo to lighten the ship) if the ship had initially got into difficulties due to unseaworthiness.

If we were to suppose that the carrier would not be liable for the

³⁰ See especially Asariotis, *ibid.* p. 155 *et seq.* and on the AMD Forum in Marrakech, 2009.

jettisoned goods, even though the ship were unseaworthy, this would indeed have some effect on general average, as the owner would then be unable to collect a contribution from other contributing values, *i.e.*, other values than the sacrificed goods, because of the unseaworthiness. In relation to sacrificed goods, a contribution can be collected if they have any value at the destination (*i.e.*, scrap value or similar). Jettisoned goods will normally not have any value as they will have been lost.

The owner of the sacrificed goods can, of course, claim contributions both from the shipowner and from the other values involved in the common maritime adventure.

5 Concluding remarks

The Rotterdam Rules are based on a system of qualified, presumptive and contributory fault-based liability. Key factors for escaping this fault-based liability, and thus being able to claim contributions in general average, will involve burden of proof, fault or negligence and due diligence in making the ship seaworthy. What impact might this have on general average?

Our examination of the various standard cases described above shows that the Rotterdam Rules would have an impact on the risk apportionment represented by general average. However, even if there are important differences, fundamentally the provisions on carrier liability contained in the Rotterdam Rules correspond to those in the Hague-Visby Rules. One thing is clear: the situations and environment in which general average operates will become more complex. Just a glance at the provisions on carrier liability in the Rotterdam Rules will make that conclusion apparent.

While hull insurers would not be greatly affected (except in the relatively rare cases of ship sacrifice), the P&I Clubs would clearly be paying cargo's proportion of general average much more frequently, as cargo interests would decline to pay on the grounds of a breach of the contract

of affreightment.³¹

There seems to be a common consensus that the Rotterdam Rules would at least give cargo interests an increased likelihood of maintaining a defence against contribution. In this case it would seem unwise for a shipowner automatically to incur the costs of an expensive security collection from multiple cargo interests. Deciding not to collect security is not purely the shipowner's call. Many average adjusters are already encouraging shipowners only to declare general average in major cases. This trend may be boosted if the Rotterdam Rules become a reality. More importantly, the shipowner should not decide not to collect security without consulting its P&I Club, as Club cover is likely to be conditional on the proper collection of security and the occurrence of a demonstrable breach of contract.³²

And so we return to the main question of our present investigation. Will general average disappear as a result of the Rotterdam Rules? The various comments about the Rotterdam Rules being the death of general average are, of course, based on the common misconception that general average principles are only relevant when money actually passes between ship and cargo interests.

As noted above, even if the Rotterdam Rules most likely will impose some degree of fault-based liability on the carrier, considerable incentives will remain for alleging contributory fault on the part of others. This means that some difficult decisions will need to be made – often very quickly – about whether to collect security for general average in such cases.

The Rotterdam Rules will in some cases prevent the distribution of money between ship, cargo, freight and other contributing values that is anticipated in a general average statement. But the principles of general average will still have to be applied to adjust the costs that arise in a casualty situation. Even in the absence of a contribution between ship and cargo, the principles of general average remain important in distin-

³¹ Cornah "Rotterdam Rules – A bluffers guide" at <http://www.rhlg.com/pdfs/RotterdamRules-ABluffer'sGuide.pdf> visited on August 23, 2010, p 8 *et seq.*

³² *Ibid.*, p. 9.

guishing between ordinary and extra-ordinary expenditure, and between property and liability insurers, *viz.*, H&M and P&I insurers.³³

For all these reasons I maintain that general average will survive the entry into force of the Rotterdam Rules.

³³ *Lowndes and Rudolf. The Law of General Average and The York-Antwerp Rules*, 13th ed., by Cook & Cornah, para. 00.30-32.

The obligation to pay upon cash calls

A test of cooperation under Joint Operating
Agreements

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1 Introduction

Offshore oil and gas production requires huge investments. Under the Norwegian petroleum regime, these investments are undertaken by companies granted production licences by the state entitling them to explore for and exploit petroleum under certain conditions. Among these conditions is the obligation to enter into a Joint Operating Agreement (JOA): each group of licensees that has jointly been granted a Production Licence (PL) for a certain geographical area (a “block”) must establish a joint venture for the purpose of exploiting the rights under the licence.

The aim of the following is to discuss some legal aspects of the investment framework created by the JOA.

Firstly a few facts will indicate the relevance of the topic.¹ Investments in offshore petroleum development projects and offshore operations off Norway in 2011 are expected to reach NOK 150 billion,² *i.e.*, close to EUR 20 billion. Most of these investments are made by the groups of licensees granted PLs, *i.e.*, under the system of JOAs, which typically have a duration of 40-50 years.³ One single development project could imply investments in the order of NOK 20-100 billion,⁴ and the total investment so far on the NCS amounts to over 2010-NOK

¹ Hans Jacob Bull presented similar figures in one of his first publications on petroleum law issues, *Petroleumsvirksomheten på norsk sokkel: Rettslig og administrative konsekvenser*, Tfr 1981 p. 6. It can safely be concluded that the levels of investment, income, taxes and the proportion of exports, GDP and employment over the past 30 years have surpassed even the then most optimistic prognosis.

² Statistics Norway at http://www.ssb.no/english/subjects/10/06/20/oljeinv_en/tab-2010-12-02-01-en.html

³ Cf. the Petroleum Act (Act no. 72 of 29 November 1996) section 3-9 first and second paragraphs.

⁴ The most recent major project to come on stream on the NCS, Gjøa (October 2010), entailed investments of approx. NOK 32 billion, ref. *Facts. The Norwegian Petroleum Sector* (Ministry of Petroleum and Energy and Norwegian Petroleum Directorate) 2010 (“Fact Sheet 2010”) p. 264.

3,000 billion.⁵ In 2009, the petroleum industry accounted for around a quarter of all investments in Norway, as well as for around a quarter of the Norwegian state's income and Norwegian GDP, and close to 50% of the value of total exports.⁶ Accordingly it is reasonable to assume that the system for funding petroleum activities has some relevance for Norway.

As we will see (in Section 2 below), although the joint venture created by the JOA is not subject to the Partnerships Act due to a specific exclusion,⁷ it would otherwise be regarded as a general partnership under this act.⁸ Activities of partnerships/companies are generally funded either by loans taken by the entity, capital accumulated in the entity or by contributions from its participants. The way contributions are made depends on the type of entity: in a limited partnership (*kommandittselskap*) the participants are exposed to contribute funds up to an agreed limit, while in a general partnership (*ansvarlig selskap*) the general rule is that there is no obligation to contribute unless this is specifically provided for in the partnership agreement.⁹ In contrast, in a joint stock company the participants, *i.e.*, the shareholders, have no obligation to contribute at all beyond their share capital.

The joint venture under the JOA fits well into this scheme: the JOA imposes an obligation on all the participants to contribute funds to the joint activities in proportion to their participating interests, normally in response to the operator's monthly "cash call". There is no agreed limit on this obligation. It is true that an important constraint on the participant's exposure follows from the fact that the joint activities are limited by the PL, but the exposure is still in principle unlimited – all

⁵ Fact Sheet 2010 p. 15. The gross income generated over the past 40 years of petroleum activities is in the order of 2010-NOK 8,000 billion.

⁶ Statistics Norway at http://www.ssb.no/english/subjects/09/01/regnskap_en/

⁷ Act of no. 83 of 21 June 1983 section 1-1 (4).

⁸ See Kaasen, *Samarbeid i olje – en spesiell selskapsrett* in Knudsen, Normann, Woxholth (eds), *Selskap, kontrakt, konkurs og rettskilder; Festskrift til Mads Henry Andenæs 70 år*, pp. 153-154.

⁹ The Companies Act section 2-6 (1). The participants in a general partnership are of course exposed directly towards third parties, *cf.* the Partnerships Act section 2-4 (1), but that is another matter.

the more so because there is no joint capital available (see Section 2 below). For this reason the instrumental cash call is tied to a formal procedure designed to safeguard the interests of the participants by controlling their economic exposure under the JOA and at the same time providing an economic basis for the joint activities under the JOA.

The purpose of the following is to examine the complex structure of procedures, decisions and authorisations leading up to the cash call and thus the obligation to pay. This brings us to areas of tension both between the operator and the participants and between minority and majority participants. Formal systems are often employed in such areas because of the lack of effective material regulations. A core topic in the following will therefore be the detailed regulations governing the decision-making process within the JOA that leads up to the imposition of payment obligations on the joint venture participants. Meanwhile, sanctions are ever-present in the background.

2 A general presentation of the JOA

Since 1972 all Production Licences have been granted on the condition that the licensees enter into a standard JOA enclosed with the PL.¹⁰ In the early years, the JOAs were strongly influenced by the special rights vested in Statoil as a participant in the joint venture (the JOAs were therefore referred to as State Participation Agreements) and also differed somewhat from one licence round to the next. However, the special rights of Statoil were removed in 1985 by the establishment of the State's

¹⁰ The legal basis for this requirement is now to be found in the Petroleum Act section 10-18 second paragraph on the King's power to stipulate conditions for individual administrative decisions "when they are naturally linked with the measures or the activities to which the individual administrative decision relates".

Direct Financial Interest (SDFI)¹¹ and in 2007 all JOAs entered into since 1972 were amended with the agreement of the participants, as approved by the Ministry. There are now basically two types of JOA on the NCS: the standard form covering all PLs granted since 1972, and the individual JOAs entered into prior to the introduction of the standard JOA as a condition for granting a licence – but even agreements belonging to the latter group have been amended to implement the basic features of the now standard form.

The present standard JOA is thus the state-of-the-art document for all joint ventures established since 1972, and for our purposes to some extent even for the still active earlier JOAs. The following discussion is based on this document.¹² We can safely adopt this approach, as the parties have no authority over the agreement: “Amendments to, exceptions from or supplements to this Agreement shall be submitted to the Ministry for approval.”¹³ The JOA is accompanied by a standardised Accounting Agreement (AA), providing technical details regarding cash management, audits, and charges and credits to the joint account.

The JOA describes the cooperation between the licensees under the agreement as a “joint venture”, and specifically states that it shall not be considered to be a company under the Companies Act 1985.¹⁴ Consequ-

¹¹ See the Petroleum Act section 3-6. The SDFI was originally administered by Statoil, but following the partial privatisation of the company in 2001, the administration of the SDFI portfolio was transferred to the state-owned trust company Petoro. See further Fact Sheet 2010 p. 25. The voting rules of a joint venture are modified if the SDFI holds a share. This is due to the requirements of the EU’s Licensing Directive (94/22) which on this point is implemented in Norwegian law by the Petroleum Regulations (Royal Decree 27 June 1997 No. 653) section 12. This will, however, not be further elaborated on here.

¹² Thus agreements governing most of the investments in transportation infrastructure are excluded – these activities fall outside the scope of the PL. However, these agreements contain systems similar to those discussed. A Norwegian version of the JOA is published at http://www.regjeringen.no/nb/dep/oed/dok/lover_regler/reglement/2007/Konsesjonsverk.html?id=455398

¹³ Special provisions, item 8 of the Agreement Concerning Petroleum Activities (the main agreement, to which the JOA is annexed).

¹⁴ This is for information only, as the exception is made by the act itself, *cf.* Act No. 83/1985 section 1-1 fourth paragraph – some aspects of the exception are discussed in Kaasen, *Samarbeid i olje ...* (footnote 8 above), pp. 152 *et seq.*

ently, the JOA in principle has to function as a self-contained legal basis for the joint activities under the PL. In addition to the provisions dealing with topics specifically related to the petroleum activities (such as rules on field development, sole-risk operations, disposal of petroleum, abandonment plan *etc.*), the JOA contains provisions on the organisation of the joint venture (the Management Committee, the Operator), the joint operations and the general rights and obligations of the participants.

Each participant in the PL, and thus each signatory to the JOA, is generally bound by decisions made by a majority of the participants according to the provisions of the JOA. There are certain specified modifications to this situation,¹⁵ and in general the power of the majority is limited by the scope of the PL and JOA¹⁶ and by the general rules on abuse of power.¹⁷

For our purposes, six aspects of the JOA are significant.

First, the Management Committee (MC) is the “supreme body” of the joint venture. All participants are represented in the MC and make decisions on “all matters concerning joint venture activities” by casting votes based on their participating interests.¹⁸

Second, the operator shall “carry out and administer the day to day management of the joint venture activities” in accordance with the JOA, the decisions of the MC and applicable laws and administrative decisions made by relevant authorities.¹⁹ The operator is in practice

¹⁵ See further in Section 4 below. The most important modification is that no participant can be forced to join in the development of a petroleum deposit.

¹⁶ See further Kaasen: *Scope of Joint Operating Agreements in Norway*, MarLus No. 261 (2000) pp. 127-147.

¹⁷ See further Nesdam, *Interessekonflikter i petroleumsvirksomhet*, MarLus No. 235 (1997) at pp. 62 *et seq.*

¹⁸ JOA art. 1.3 first and fourth paragraphs. The rules on voting differ between the PLs. Normally a decision is reached when supported by a minimum number of participants (often a majority) holding a minimum proportion of total participating interests (often less than a majority). The purpose of the system is, *i.a.*, to avoid minority participants being regularly overruled and thus made passive in the licence operations, so that their expertise fails to contribute to the optimisation of the joint activities. Also, the system implements the restrictions imposed by the EU Licensing Directive on the state’s impact on decisions, see further notes 11 and 48.

¹⁹ JOA art. 3.1.

always itself a licensee and should make neither a profit nor a loss through the execution of its duties – it should make its profit in its capacity of licensee.

Third, the participants in the joint venture are under an obligation to “provide sufficient funds to cover all expenses relating to the activities of the joint venture”, with each party’s contribution to be calculated in accordance with its participating interest.²⁰

Fourth, should any participant fail to contribute its part of the required funds, the defaulted amount is apportioned between the other participants in accordance with their participating interests.²¹ Consequently, the participants are primarily liable to each other on a *pro rata* basis for contributions to joint activities, while having a secondary liability that is joint and several.²² The result is that the joint costs will be covered as long as at least one of the participants is not bankrupt.

Fifth, the produced oil and gas – the result of the joint activities – is taken in kind by the participants in proportion to their participating interests.²³ Consequently, no joint funds are accumulated in the joint venture.

Sixth, the JOA contains extensive regulations²⁴ on how joint activities are decided and budgeted, how the resulting payment obligations are established, and the consequences of any default under these obligations.

For our purposes, the most important general observation to be made on this basis is that no funds are accumulated in the joint venture. This is partly because the joint venture does not have the legal status of

²⁰ JOA art. 8.1.

²¹ JOA art. 9.1 first paragraph.

²² Which is also specifically stated in JOA art. 7.1.

²³ JOA articles 20.1 and 22.1. Until 2002, gas produced on the NCS was marketed jointly (by means of the Gas Contract Committee – GFU, which was phased out due to EEA requirements), but even then the proceeds were channelled to the individual participants, not to the joint venture.

²⁴ The JOA provisions on liabilities and payments, duty of contribution, default, accounts, corporate governance, work programme, budgets, AFE, and procurement add up to approximately a third of the agreement, while the AA adds some 20 pages on accounting.

a company, implying that there is no corporate body capable of financing the joint activities on its own books based on loans. More importantly there is no joint income,²⁵ nor is there any gathering of joint funds in the form of contributions from the participants beyond what is currently needed to run the joint activity.²⁶ The joint venture entails joint expenditure but individual income – the parties cooperate in terms of cash only on the expense side: income takes the form of products in kind. The participants determine the form of the joint activities and make monthly contributions to cover related costs. They then get their hands individually on the proceeds of the activities – the produced petroleum.²⁷

These characteristics naturally affect the provisions of the JOA concerning default.

3 Default under the JOA

3.1 Key points

The participants in the joint venture are subject to various obligations under the JOA. For the reasons stated above, the crucial one is the

²⁵ Admittedly, the JOA presupposes that there might be an “Operating Income” in the form of “Tariff income, processing and any other income”, cf. art. 12.4 item 7. A typical example is fees earned from third-party use of joint assets for transportation or processing of third-party petroleum. Such income is not distributed to the participants, but serves as a buffer when calculating their financial contributions to the joint activities.

²⁶ If the actual monthly need for cash is “significantly less” than the contributed advances, the excess shall be refunded unless the parties agree to transfer the amount to the following period (AA item 1.2.1 sixth paragraph).

²⁷ The JOAs on the UK Continental Shelf have similar characteristics, although they are not standardised beyond what resulted from the common influence of (in the very early days) the American Association of Petroleum Landmen’s Model Form Operating Agreement and (from 1977) British National Oil Company’s (BNO) *pro forma* JOA. See further on this Taylor, Winsor and Tyne, *Joint Operating Agreements* (Longman, 1989) pp. 5-6, 27-32 and 49-58.

obligation to provide funding for the joint activities. In case of default in relation to the payment obligation the JOA prescribes a set of consequences, some of which are applied automatically while others rely on the intervention of the co-venturers.

Issues concerning payment obligations and default used to be mainly of theoretical interest. But this has changed over the last few years as smaller companies, some with limited financial capacity, have become licensees on the NCS. The relevance of these issues is also increasing as production on several oil and gas fields draws towards a close: income declines along with production, implying a possible reduction in both the ability to contribute and the effectiveness of the pressure – represented by the default mechanism – to do so.

The relevance of the default provisions has also become less theoretical due to a development of a different type: a change over the years in the roles of the joint venture partners. In the early years of Norwegian petroleum activities, rather passive participants tended to occupy the back seat of the operator-driven joint vehicle. Over the last 10-20 years, however, the participants have been taking a more active role in preparing the bases for MC decisions and in controlling the operator's conduct of joint activities. This is the result of various factors, *i.a.* the increased interest in “corporate governance” in general²⁸ and the state's emphasis on the “battle of minds” within the joint venture in order to facilitate cost- and resource-effective operations. Some unfortunate experiences with project cost overruns may also have had an impact.

Default under the JOA is defined as failure by a participant to comply with “his obligation to make payments pursuant to Articles 7 or 8”, *i.e.*, the general obligations to provide sufficient funds for the joint activities and to cover the contributions of co-venturers who fail to pay. Details of these obligations will be discussed in Section 7 below. In the following

²⁸ Since 2007 the JOAs have contained a separate article on corporate governance (art. 11). Similar considerations may to some extent be said to have led to the emerge of the Partner Forum (art. 5), which is a body comprising joint ventures having the same operator, with the purpose of dealing with “matters that are common to all the joint ventures” and that are “of common interest within the scope of the provisions of” the JOA and the AA, but having no authority to make decisions (art. 5.1, 5.4 and 5.5).

we look at the JOA clauses on the consequences of not fulfilling these obligations.

One specific payment obligation should however be mentioned at this stage: the definition of default includes a reference to the obligation on each participant “to pay the direct taxes charged to him.”²⁹ Consequently, failure by a participant to pay ordinary taxes levied on its activities under the PL constitutes default under the JOA, entailing all the consequences of such default, *e.g.*, the loss of the right to vote in the MC after five days of default (see Section 3.2 below). However, this can hardly be the intention and there is a contradiction in the JOA regulation on tax liabilities: on the one hand, “None of the other Parties may be held liable pursuant to Article 7.1 for direct taxes which a Party is obliged to pay”³⁰ (*i.e.*, the co-venturers are under no obligation to “pick up” the defaulter’s taxes), while on the other hand, in the case of default (which by virtue of the above reference includes default under a tax obligation), the unpaid amounts “shall be advanced by the non-defaulting Parties in accordance with their Participating interest.”³¹ On this basis it must be assumed that the provision making the payment of taxes an obligation under the JOA is not meant to imply that non-payment of taxes constitutes a default under the JOA.³² The payment of ordinary corporation tax and special petroleum tax is not a matter for the joint venture as such, and there is no reason why non-payment should become a joint matter by means of the default clauses of the JOA. This would seem to be an unintended effect of the JOA provisions underlining individual responsibility for taxes.

²⁹ JOA art. 9.1 first paragraph, *cf.* art. 7.3 *in fine*.

³⁰ JOA art. 7.3 first paragraph.

³¹ JOA art. 7.1.

³² The problem was introduced in the standards that replaced the “State Participation Agreements” in 1985. In earlier versions of Norwegian JOAs, the default provisions are linked solely to the participants’ obligation to provide sufficient funds to cover all expenses related to the joint activities, *cf.* JOA art. 8.1 first paragraph.

3.2 An overview of the default provisions

The immediate consequence of default is that penal interest on the defaulted amount automatically starts to run³³ and that the other parties have to advance the defaulted amount in order to avoid disruption of the joint activities due to lack of funds. Claims for repayment against the defaulting party can be covered by acquiring its share of the petroleum produced, subject to notification to that effect.

This is the only provision that explicitly deprives the defaulting party of the right to lift its proportionate share of the production. It may appear surprising that the defaulting party does not automatically lose this right, given the close link between the obligation to contribute and the production. But for this very reason the default will – even without any specific regulation to that effect in the JOA – presumably give the other participants the right to withhold the defaulter’s part of the production on the basis of the principle of reciprocity between parties’ contractual performance (“*ytelse mot ytelse*”) under general contract law.³⁴

After five working days of default, the defaulter automatically loses its right to vote and its access to data and information for as long as the default persists.³⁵ But it remains a participant in the joint venture, implying that it is irrevocably bound by the decisions and dispositions made by the MC and the operator on behalf of the joint venture. This is a serious situation: the defaulter is irrevocably exposed to all the practical and legal consequences of the joint activities, even though it has no influence on and no information about them.

The final consequence takes effect after three months of default: the other participants may require the defaulting party to assign its participating interest to them against compensation to be agreed, but which shall not exceed the book value of the defaulter’s share.³⁶ This right takes

³³ JOA art. 9.1 second paragraph, *cf.* AA art. 1.2.2.

³⁴ See further Kaasen, *The Co-operation Between Joint Holders of a Production Licence*, in Krohn *et al.*, *Norwegian Petroleum Law* (1978) pp. 3-139 – 3-142.

³⁵ JOA art. 9.2 first paragraph.

³⁶ JOA art. 9.3 first and third paragraph.

priority over the pre-emption rights of the other participants and any agreement assigning the defaulter's interest to another party, including the rights of a mortgagee. For this reason, assignment can only be claimed three months after the mortgagee has been notified of the default, and the mortgagee is entitled to make remedial payments on behalf of the defaulting party. Such payments will have a releasing effect.³⁷

In extreme cases the default may also have consequences under the PL itself: the licence may be revoked if the company holding the licence "is dissolved or enters into debt settlement proceedings or bankruptcy proceedings".³⁸

3.3 Default in the late phases of joint activity

Most of the sanctions for default are effective only where the defaulter can be assumed to want to maintain its full rights as a participant (the exception being the penal interest on defaulted payments). The relevance of this assumption diminishes as production declines and costs increase – and as the abandonment phase draws near, any wish to remain a participant may have totally evaporated. The lack of pressure exerted by the default provisions may in this situation become even more problematic because the likelihood of default in some cases may increase because the activities will be generating less income.

As long as the participants consider themselves to be in the same boat, this type of challenge is handled by means of the JOA provisions on cessation of petroleum activities (art. 30). Where views differ, the potential defaulter may assign its interest or – as a last resort – withdraw from the joint venture (articles 23 and 24). But none of these alternatives

³⁷ In pure economic terms such intervention by the mortgagee will take care of the interests of the non-defaulting parties. But the situation is likely to imply that the mortgagee becomes the real decision-maker in lieu of the defaulter, which could complicate the processes in the MC. However, this could well be the consequence of any mortgaging of participating interests, even prior to any default. The mortgaging of a licence or part of a licence is subject to the Ministry's consent, *cf.* the Petroleum Act section 6-2.

³⁸ The Petroleum Act section 10-13 third paragraph.

offers much help in obtaining financial contributions where the default has already taken place.

It seems, however, difficult to add to the JOA's list of sanctions for default, both in general and to address the specific challenges posed by default during the late phases of activity.

4 System for establishing payment obligations: considerations

We have already seen that there can be no joint activities without running contributions from the participants. This means that it is crucial to ensure that the contributions are made. On the other hand, the system for establishing payment obligations also needs to ensure that joint activities are decided and executed in a cost-effective and controlled manner, allowing the contributors to foresee their future exposure.

These two considerations necessitate a comprehensive set of regulations linking the decision-making system to the technical cash-call system. Dynamic considerations are important: decisions that have a direct impact on the payment obligations cannot be made at an early stage in the process before sufficient knowledge has been gained of all relevant factors. Rather, a step-by-step approach is necessary: planned activities with related budgets have to be decided prior to starting the processes that lead up to firm investment decisions, which in turn form the basis for the technical cash calls that result in actual payment obligations and finally the joint expenditure. A challenge in this process is to maintain cost-effectiveness and control throughout, especially in the process of entering into contracts with third parties. In this respect the competing powers of the MC – representing the non-operating participants – and the operator – which is also a member of the MC – are essential.

In the early standardised JOAs these issues were not regulated in

great detail.³⁹ The agreements simply stated that all participants were under an obligation to make advance payments according to their participating interests to finance the joint activities, based on the operator's expected costs in the coming period. An adjustment of the contributions was to take place following the operator's reports on actual costs.

In the present JOA this rather simplistic approach has been exchanged for a complex system of regulation. But before we look at the details (see Section 5-7 below), the general systems for decision-making should be presented.

Joint activities under the JOA are decided by the MC in accordance with the ordinary decision-making system supplemented by specific rules on work programmes and budgets.

The fundamental element is the ordinary system for making decisions in the joint venture. Each participant has the right and duty to contribute to the management and control of the joint venture activities by casting its vote in the MC.⁴⁰ Though the details vary between the joint ventures, in general a participant may be voted into taking part in an activity that it opposes, while on the other hand it may have to refrain from activities that it would like to pursue on the basis of the PL. There are, however, mechanisms that may modify this position to some extent: rather than being voted into taking part in an activity a participant may assign (part of) its participating interest, and rather than being forced to remain passive it may explore the JOA provisions on sole-risk operations.⁴¹

The most important decision, however, namely whether to develop a petroleum deposit, is excluded from the ordinary voting system: no participant can be voted into doing so, and normally no participant can be barred from developing the deposit. These decisions are taken on an individual basis, linked to the handling of the Field Development Plan.⁴²

³⁹ See, *e.g.*, the JOA for the third licence round (1974-75) art. VI.

⁴⁰ JOA art. 1.3 first paragraph

⁴¹ JOA art. 23 and 18 respectively.

⁴² JOA art. 16.3 on accession to the plan and art. 19 on Sole Risk Field Development. See further Section 5 below.

Within this framework of decisions made by the MC and by the partners individually, the operator “shall carry out and administer the day to day management of the joint venture activities”.⁴³ This necessarily implies that it may make certain decisions itself, without consulting the MC, but always subject to the MC’s right to decide on any issue concerning the joint activities that it demands to be presented to it.⁴⁴

5 Establishing a basis for cash calls: work programme and budget

The work programme and budget for joint activities “shall specify the main activities and economic framework for the coming year” and shall “define clear goals, deliverables and deadlines for significant activities”.⁴⁵ The operator must prepare and propose the programme and related budget according to a process⁴⁶ in which the parties are to be involved, starting with the operator’s preliminary overview by 1 June the year before the programme year and ending with the MC’s modification of the work programme and budget by 1 December. The operator may propose changes to both the programme and the budget in the course of the programme year as necessary.

In addition to the annual planning process, the operator must present programmes and budgets for joint investments and operations for the coming three years and for the whole period of the relevant investment. It must also advise the MC of activities that are not included in the programme (and therefore the budget) that it plans to submit for approval during the budget year. This “optional budget” serves as a means of securing flexibility while still maintaining control over participants’ total exposure and does not require MC approval. However, the

⁴³ JOA art. 3.1 first paragraph.

⁴⁴ JOA art. 1.3 fourth paragraph.

⁴⁵ JOA art. 12.1.

⁴⁶ Described in some detail in JOA art. 12.2-12.4.

MC may accept costs that have not been included in the budget or notified in the optional budget – simply by amending the relevant budget or by approving the expenditure directly. Similarly, the MC may delete items in an approved budget.⁴⁷ The ordinary rules on voting apply to such decisions.⁴⁸

Combined with the detailed requirements regarding the structure and contents of the budget,⁴⁹ this system should provide a solid basis for cost planning and control by the MC.

But it is hardly possible to provide a thoroughly detailed definition of joint activities and related costs by means of this system alone. Further control over the operator's activities on behalf of the joint venture is obtained by means of the specific rules on procurement, which accounts for the major part of joint spending. The operator must prepare for MC approval “an overall procurement and contract strategy” and the budgets must include “an overview showing what significant purchases the operator is planning for the budget year”, including expected contract values.⁵⁰ On this basis the MC must determine which purchases shall be included in the “plan for significant decisions” in the coming year – which may well be helpful but which does not have specific legal consequences. More importantly, the operator must present to the MC for decision “specific purchase strategies, including a bidding list and approval of supplier”, provided the contract value is expected to

⁴⁷ Provided the costs have not already been incurred (but such costs would normally have been incurred on the basis of a separate MC decision in the form of an AFE, see Section 6 below).

⁴⁸ This could admittedly give rise to some complex questions, *e.g.*, due to EEA-inflicted rules (the Licensing Directive art. 6) that entrust the SDFI (see Section 2 above) with a right to veto certain decisions in the MC while at the same time excluding the SDFI from decisions on the choice of suppliers of goods and services for joint activities. This complexity could be worse under the early Norwegian JOAs, see Arnesen, *Samarbeid om petroleumsvirksomhet*, MarLus No. 145 (1987) pp. 53-55.

⁴⁹ The provision on budget structure and content (and therefore also the operator's monthly report and settlements) covers some four pages, which come in addition to the detailed regulations of the AA (art. 2) specifying how charges are to be made to the joint account.

⁵⁰ JOA art. 13.1 first and second paragraph.

exceed a certain level.⁵¹ This implies that the MC has quite detailed control over a major part of the joint costs,⁵² going beyond the control that can be exerted by approving the work programme and budget.

It follows from this that several actions and decisions have to be taken along the way before the operator can enter into a contract on behalf of the joint venture, *e.g.*, for the construction of an offshore production facility. *First*, the decision to develop the deposit – thus incurring investment costs – has to be made according to the specific rules on individual accession to the development plan. *Second*, the related planned investments have to be notified by the operator to the MC three years in advance. *Third*, the investments have to be included in the work programme and budget approved by the MC for the relevant year, based on the operator's proposal.

Each of these three elements is firmly rooted in some basic decisions. For example, should a proven reserve be developed and, if so, at what level and according to what strategy and schedule should production take place? Should extra capacity be installed? How should the produced oil and gas be exported? And so on. Most of these considerations will be covered by the Plan for Development and Operation (PDO),⁵³

⁵¹ NOK 50 million (or NOK 25 million if there is no competitive bidding) *cf.* JOA art. 13.1 fifth paragraph. The amounts may be changed by the unanimous resolution of the MC (*cf.* art. 13.2). The latter provision reflects both the need to adapt to inflation and the principles of corporate governance, as well as the fact that the existence of the JOA is a pre-condition for the PL, and therefore as a starting point cannot be amended by the participants.

⁵² Some details are, however, still left to the parties to sort out along the way. In practice many purchases and contracts extend over more than a year, meaning that the joint venture has to undertake commitments beyond the budget year in order for the operator to enter into the contract. In this case the only guidance to be found in the JOA is that “the Parties shall organize themselves such that the joint venture may commit itself according to the duration of the purchase”, *cf.* art. 13.1 fourth paragraph.

⁵³ The Petroleum Act section 4-2. The PDO includes a budget for the development project, and no major contractual undertakings can be entered into by the joint venture prior to the approval of the PDO, *cf.* section 4-2 fifth paragraph. – The procedure for preparing and acceding to the PDO is regulated in the JOA art. 15. This procedure has been further developed since the early Norwegian JOAs by introducing the Decision on Continuation as a first step, laying the ground for the processes needed to establish the PDO.

which has to be submitted to the Ministry for approval and which thereafter constitutes the general framework for all activities related to the relevant petroleum deposit. No participant in the joint venture can be voted into a PDO by a majority of the participants – this decision is taken on an individual basis and may result in a split in the joint venture, as one or more participants may undertake the development on a “sole-risk” basis, with one or more participants not taking part.⁵⁴ This does not necessarily imply that the latter group is no longer party to joint activities under the PL, as activities unrelated to the relevant deposit may continue. It is beyond the scope of this paper to explore the steps leading up to the PDO and the participants’ accession to it. For our purposes, the important observation is that once a participant has single-handedly decided to join the PDO, it is exposed to the ordinary voting mechanism and the procedures for establishing detailed budgets, and accordingly is liable to cover its part of the related costs.⁵⁵

There is, however, a *fourth* tier in the system for establishing an obligation to contribute to the joint activities. This is the procedure specifically linked to procurement, which obviously constitutes the main element of the joint costs. This procedure is distinguishable from, but closely linked to, the above-mentioned system for establishing the work programme and budget: the budget proposal for the coming year shall include “an overview showing what significant purchases the operator is planning for the budget year” including “the expected contract value”. Further, when considering the budget proposal, the MC shall “decide which purchases are to be included in the plan for significant decisions in the coming year”.⁵⁶

This procedure for purchases implies a step-by-step approach invol-

⁵⁴ Sole-risk field development is regulated by the JOA art. 19, and is subject to Ministry approval. Such situations are extremely rare, presumably because a party that does not participate initially will never be able to join at a later stage, see JOA art. 19.6.

⁵⁵ In this context the only difference resulting from operations being conducted on a “sole-risk” basis is that the participating interests in the venture are adjusted on the basis of who is participating and their interests in the PL, unless otherwise agreed, *cf.* JOA art. 19.3.

⁵⁶ JOA art. 13.1 second and third paragraphs.

ving the operator and the MC, dealing with fundamental issues of project and contract strategy, lists of bidder, choice of contractor, *etc.* and resulting in a final MC “approval of the supplier”.⁵⁷ This approval would of course be based on the commercial terms of the delivery, *i.a.* the price.

For practical reasons the process for obtaining the necessary approvals for procurement is fast-track: the MC’s decision must be made within five working days of the operator’s submission of its proposal.⁵⁸ Due to the previously submitted plans for purchases, the request for approval will normally not come as a surprise to the MC.

Under this system the participants in principle have full control over their cost exposure for joint activities, at least insofar as the costs relate to purchases of a more than minimal nature.

All this said, default under the payment obligations of the JOA is more likely to occur in the final phases of the activities (see Section 3.3 above) or in relation to late-phase minor modifications to the joint assets than in the hectic development phase. However, the tools for controlling the costs are the same – except that the role performed by the PDO procedure in the earlier days of the joint venture may now be performed by the procedure for adopting an “abandonment plan”.⁵⁹

But the JOA contains yet another tool for controlling joint costs incurred by the operator: the AFE.

6 Establishing a basis for cash calls: authorisation for expenditure (AFE)

The JOA art. 12.5 reads:

⁵⁷ JOA art. 13.1 fifth paragraph.

⁵⁸ JOA art. 13.1 fifth paragraph.

⁵⁹ JOA articles 31 and 32 on the adoption and implementation of the abandonment plan, *cf.* the Petroleum Act ch. 5.

“The Operator may only incur expenses and financial obligations on behalf of the joint venture within the limits of the authorizations for expenditure as approved by the management committee pursuant to the exploration, operation and investment budgets, unless otherwise decided by the management committee.”

In other words, an approved AFE is an absolute precondition where the operator is to incur joint expenses (unless otherwise decided by the MC). No valid obligation to contribute to joint costs can be established without an approved AFE, provided the costs can be said to be “incurred” by the operator, as opposed to having a basis in, *e.g.*, rules under tort law, see further Section 7.2 below.

The AFE is proposed by the operator and approved by the MC. In principle the approval presupposes that the expenditure has been planned in the budget, but this is not a real limitation as the MC at any time may amend the budget. The MC is in other words quite free to make a decision on the AFE.

The MC may also decide that no AFE is needed in a specific case. This could be the obvious procedure to adopt where the MC has already approved the commercial terms of a major contract according to the procurement procedures (see Section 5 above).

To prevent too much rigidity in the operation of the AFE system, the operator may exceed an AFE by up to 10% and may incur costs of up to NOK 3 million per year per budget without any basis in an AFE or even in a work programme or budget. The operator may also incur costs without an AFE in an emergency if there is insufficient time to present the matter to the MC.⁶⁰

The AFE system did not exist in the early Norwegian JOAs. It was introduced *i.a.* as a result of the non-operators’ wish to keep tighter control over joint costs following some experiences with major cost overruns. The main effect of the system is that the operator has to pass one final checkpoint before actually incurring costs on behalf of the joint venture – even if the costs and underlying activities have long been

⁶⁰ JOA art. 12.5 second to fourth paragraphs.

planned in the form of work programmes and budgets. It thus serves to facilitate more effective control by the co-venturers of the joint activities within the less stringent framework of plans and budgets.

7 What constitutes a payment obligation?

7.1 The cash call system

The operator's cash call is the normal means for establishing payment obligations under the JOA.

The term "cash call" is not defined in either the JOA or the Accounting Agreement (AA), and it is not used consistently in the AA, which also uses the terms "request for advances" and "cash requirement" (none of these terms are used at all in the JOA). However, the phenomenon has long been referred to in the industry as a "cash call".

The JOA itself does not specify the details of how the co-venturers' payment obligation is established. According to art. 8.1 first paragraph, the co-venturers are "obliged to provide sufficient funds to cover all expenses relating to the activities of the joint venture", while the "[f]urther provisions regarding the Parties' duty of contribution in this respect are specified in Attachment B - Accounting Agreement" (art. 8.2). As we shall see, however, these provisions are not decisive when defining the basis for payment obligations under the JOA.

The gist of the mechanics for securing timely contributions of funds is described in the provisions of the AA art. 1.2.1 first and second paragraphs:

"At least 10 days prior to the beginning of each month, the Operator shall submit to the Non-operators a 3 month forecast, specified by month, of estimated cash requirements.

Upon request, the Non-operators shall advance their share of estimated cash requirements for the following month. The Operator

shall submit a written request for advances at least 15 days prior to the due date. [...]"

The AA contains further technical rules on forecasts, due dates, splits into two payments, additional advances if needed, refunds of excess amounts, handling of different currencies, *etc.*, all of which fall beyond the scope of this paper.

The normal procedure is thus that the participants have an obligation, subject to the operator's request – the "cash call" – to pay their proportionate shares of expected joint expenditure for the following month (although the operator may choose to bill in arrears on the basis of its actual monthly payments rather than requesting advances).⁶¹

This technical payment procedure must be seen in the light of the provisions on plans, budgets and AFEs: in order to be valid, a cash call must be rooted in an AFE,⁶² which again (normally) is rooted in an approved budget. In consequence, the individual participant's exposure to payment obligations is based on the ordinary voting system of the JOA, not on the discretion of the operator.

The cash call need not – and normally will not – correspond either with specific budget items or AFEs. While these will relate to identifiable investments or cost items, the cash call embodies all expected (or accrued) costs during a certain period of time, normally a month, and will consequently normally cover several budget items and AFEs, but not necessarily the whole amount of all of them.

A joint activity may, however, entail costs that have not been planned and budgeted. As such, they fall outside the immediate scope of the AFE system leading up to the ordinary cash call. How are these costs handled in relation to the JOA system for funding joint activities – can they give rise to cash calls?

⁶¹ AA art. 1.2.1 *in fine*. This alternative is likely to be used for just part of the monthly joint expenditure, not the total.

⁶² JOA art. 12.5 first paragraph: "The Operator may only incur expenses and financial obligations on behalf of the joint venture within the limits of the authorizations for expenditure [...]", *cf.* Section 6 above.

7.2 Cash calls without a basis in an AFE?

There are costs that do not fit into the neatly arranged budget system of the JOA. But are they also excluded from the AFE system?

First a basic reminder: some costs linked to the joint activities fall outside the scope of the JOA altogether, such as income taxes levied on the participants in relation to the joint activities.⁶³ No payment obligation towards co-venturers may arise on this basis.⁶⁴ On the other hand, the co-venturers are jointly liable for the area fee. Primarily, each co-venturer is responsible for its share of the area fee attributable to the licence area, but in the absence of payment, the operator must pay on the defaulter's behalf and apportion the amount between the other parties.⁶⁵ There is a distinction between the area fee, which is a condition for holding the actual PL, and income tax, which is generally levied on all income.

Unplanned costs include situations where the joint activity causes damage to third parties. Such third parties may claim compensation under ordinary tort law or, *e.g.*, on the basis of the specific rule in the Petroleum Act making the licensee liable for damage caused by independent contractors in certain circumstances.⁶⁶ In general the addressees of claims for damages can be identified under ordinary tort law. An exception concerns claims relating to pollution damage: these are channelled to the relevant group of li-

⁶³ JOA art. 7.3 states that "None of the other Parties may be held liable pursuant to Article 7.1[the general rule of liability as between the participants] for direct taxes which a Party is obliged to pay. Each Party is obliged to pay the direct taxes charged to him." This is a consequence of the joint venture not being a corporate entity and thus not subject to taxes, *cf.* Taxation Act (No. 14/1999) section 2-2 second paragraph *litra a.*

⁶⁴ But see 3.1 above re. the challenges posed by the link to the JOA provisions on default.

⁶⁵ JOA art. 7.2.

⁶⁶ The Petroleum Act section 10-9 first paragraph: "If liability in respect of a third party is incurred by anyone undertaking tasks for a licensee, the licensee shall be liable for damages to the same extent as, and jointly and severally with, the perpetrator and, if applicable, his employer."

censees according to specific rules.⁶⁷

This implies that claims for compensation for damage caused by joint activities may be directed towards the operator as the representative of the joint venture. Such claims are – to the extent they are valid – “expenses relating to the activities of the joint venture” and must therefore be covered by funds provided by the participants.⁶⁸ This principle would seem to take priority over the technical rules relating to cash calls and AFEs. Thus the decisive factor would be that the participants are under an obligation to pay in advance the costs following from such claims (or to refund payments actually made) in response to the operator’s request.⁶⁹ It is of no relevance that it may be said to be something of a stretch to perceive claims for damages as “expenses and financial obligations” that the operator “incurs” on behalf of the joint venture, and that a cash call in this situation consequently would not necessitate approval of an AFE. This example illustrates that cash calls may impose valid payment obligations even if they are not rooted in the system of plans, budgets and AFEs.

This would also be the case if a governmental body were to cause expenses to the joint venture by some form of intervention, typically an administrative decision.

The same would apply if a third party that had suffered damage due to the joint activities chose to direct its claim at one of the non-operators in the joint venture. Assuming that this non-operator were liable to pay damages,⁷⁰ the operator would be obliged to cover the cost as part of the joint expenses, and the amount would consequently be included in the basis for subsequent cash calls.

⁶⁷ The Petroleum Act section 7-4 second paragraph. For all practical purposes this will mean that no one other than the operator can be held liable on behalf of the joint venturers. For some modifications see the Act section 7-4 third paragraph *cf.* section 7-5.

⁶⁸ JOA art. 8.1 first paragraph.

⁶⁹ AA art. 1.2.1 second paragraph.

⁷⁰ This would be the situation if the ordinary rules of tort law allow claims against the non-operator on the basis of the general rule of joint liability between tortfeasors who may be held separately liable for damage, *cf.* Act on Liability for Torts (Act No. 26 of 13 June 1969) section 5-3 first paragraph.

A similar system applies to claims based on contractual relationships entered into by the operator on behalf of the joint venture (supposedly following the procedure for such commitments).

Consequently, the general observation is that, provided that the costs are “relating to the activities of the joint venture”,⁷¹ they will by means of the operator’s request for funds impose an obligation upon the non-operators to pay according to their participating interests – or even beyond such interests if a co-venturer fails to pay its share, according to the secondary rule of joint and several liability.⁷²

There seems to be just one modification to this direct link between cash calls and costs incurred (actually or expectedly) in relation to joint activities. In certain circumstances the operator may be held personally liable for the costs, and thus be deprived of the right to obtain contributions from the non-operators. This is the case if the joint venture or any of the non-operating participants “sustain losses arising from the Operator’s performance of its functions as an operator” as a “result of wilful misconduct or gross negligence by the management or supervisory personnel of the Operator”.⁷³

7.3 Costs incurred by the operator without authorisation

Leaving aside the unplanned situations discussed in 7.2 above, does an operator that has actively incurred costs on behalf of the joint venture without a valid basis in either MC decisions, emergency rules or in the rules providing the operator with some room for manoeuvre within this framework,⁷⁴ have a right to request contributions from the non-operators to cover such costs?

⁷¹ JOA art. 8.1.

⁷² JOA art. 7.1.

⁷³ JOA art. 3.5 first paragraph. But the operator shall under no circumstances be liable for “losses caused by delay or stop of production”, or losses in connection with pollution damage suffered by third parties.

⁷⁴ See further on the operator’s “prerogatives” in Harstad Eggen, “No gain no loss” - *prinsippet i petrolumsvirksomhetens samarbeidsavtaler*, Marlus No. 359 (2007).

The main example of this situation in practice will be where the operator contracts goods or services allegedly for the benefit of the joint venture, but without having been granted the authority to do so by a decision in the MC.

If the operator has incurred the costs in its own name, there will be no basis for holding the non-operators liable for the costs. The operator's creditor will normally have no legal basis for directing a claim directly against the non-operators, and the operator itself will have no basis in the JOA for requesting contributions.

If the operator has contracted explicitly on behalf of the joint venture, it is likely to have appeared to the third party as having had the authority to do so. In this case, the joint venture may well be legally bound by the operator's representation – based on the general rules of contract law. This might in turn result in the non-operators being held liable directly towards the third party. In this case the paying participant will have to claim a refund from the operator, either on the (unlikely) basis that the costs were regarded as joint costs (and thus should have been dealt with according to the system discussed in 7.2 above) or on the (more likely) basis that the operator should be held personally liable for the costs. However, normally the costs will be paid initially by the operator – in line with joint costs incurred generally. In both cases the operator is likely to aim to redistribute the costs by a cash call.

Should the operator actively incur costs allegedly of a joint nature without proper authorisation, the problem is thus likely to be whether the resulting cash call is valid.

To determine this issue, two sets of rules need to be considered. On the one hand, the costs may be assumed not to have been authorised under the JOA. This would seem to imply that there is no basis for a cash call (see 7.1 above). On the other hand, the “Operator shall in its capacity as such neither have profit nor loss through the execution of its duties”, and “[i]f the joint venture or any of the Parties sustain losses arising from the Operator's performance of its functions as an operator, the Operator shall only be liable for such losses provided it is the result of wilful misconduct or gross negligence by the management or super-

visory personnel of the Operator” (the no-gain-no-loss rule).⁷⁵

While the latter rule hardly applies to cash calls based on expenses directly incurred by the operator in respect of contracts, it could be argued that the “Parties sustain losses arising from the Operator’s performance” in cases where they are held directly liable under a contract entered into by the operator without authorisation. However, this distinction appears to be formalistic, as the reality in both cases is that the direct costs of the contract are charged to the co-venturers. As we have seen, the JOA contains comprehensive systems for authorising such expenses. It seems hard to argue that an obligation to refund the expenses can be established without a basis in these systems – *i.e.*, ultimately in a decision made by the MC.

This would clearly be the case if the operator were positively to violate a decision made by the MC, *e.g.*, by contracting a rig even though the MC had rejected the operator’s proposal to do so. But what if the operator overlooked the need to acquire an authorisation under the JOA prior to incurring the cost?

The simple answer seems to be that overlooking this need normally will constitute “gross negligence by the management or supervisory personnel of the Operator”, and consequently the costs resulting from the contract cannot be charged to the co-venturers, no matter which of the above-mentioned rules is applied. On the other hand, if the threshold for “gross negligence” for some exceptional reason is not passed, the costs incurred under the contract would amount to a loss to the joint venture for which the operator cannot be held liable pursuant to the no-gain-no-loss rule.

Consequently, the JOA system implies that the operator is not at liberty to enter into contracts on behalf of the joint venture just because doing so makes commercial sense under the current circumstances. The right to request a refund from the co-venturers is subject to the “gross negligence” test and therefore the JOA system of MC decisions, not the commercial rationale of the operator’s conduct.

On the other hand, even if the operator exceeds his powers and

⁷⁵ JOA art. 3.1 and 3.5, both first paragraphs.

therefore *prima facie* will be held liable for the costs incurred, meaning that he cannot oblige the co-venturers to refund the costs, the joint venture may still benefit from the unauthorised expenditure – simply because it actually did make commercial sense after all. *Prima facie*, this does not imply that a similar amount can be claimed from the co-venturers – there is simply no basis in the JOA for this. But with an eye to the doctrine of enrichment, it would appear surprising for the operator to be barred from claiming remuneration for expenditure that objectively benefited the joint venture. Should matters be brought to a head,⁷⁶ it would probably be because the non-operators did not want the activity to take place, despite their benefit from it. In this case the decisive factor is likely to be that the joint venture should not be exposed to expenditure beyond what can be incurred based on the rules and procedures for authorising the operator to do so.

Different from all the above situations, but linked to them, is the situation where a contract entered into by the operator pursuant to the necessary authorisations proves to be a commercial failure. If this is due to the operator's conduct under the contract, *e.g.*, its project team is unable to keep control of spiralling variation costs under a construction contract, the economic consequences to the co-venturers will be governed by the no-gain-no-loss rule. This will also be the case if the reason for the failure is to be found in the commercial and technical evaluations that preceded the signing of the contract.

7.4 Payment obligations without cash calls?

So far we may conclude that the obligation to contribute the funds needed to cover expenses arising from the joint activities is defined by the operator's cash calls, which in turn are rooted in the voting system established in the JOA. The financial exposure of each participant – and consequently each participant's exposure under the default provisions

⁷⁶ The fact that cash calls normally relate to *advance* payments implies that the problem will often surface before the operator actually incurs the cost – but this is not necessarily the case.

– thus seems well defined, both in terms of the structure of the decision-making process leading up to it and the way the specific obligation is communicated.

This clarity may be disrupted if payment obligations under the JOA can arise without cash calls.

Under normal circumstances, the operator is likely to request contributions by utilising the format prescribed in the AA art. 1.2.1, which would imply the making of a cash call.

To take a practical example: would a non-operator have a right to request the other participants to cover their proportionate shares of its expenses “relating to the activities of the joint venture” without involving the operator the way described above? Such a right does not follow directly from the JOA (or the AA), but is on the other hand not explicitly excluded in the general provisions on the participants’ obligation to provide sufficient funds to cover joint expenses.

A pre-requisite for allowing a non-operator to claim from his co-venturers directly would be that it must have incurred costs that according to the JOA must be borne by them. This could be the case in three situations: where the non-operator has supplied goods or services to the joint activities and claims remuneration; where the non-operator has suffered loss or damage due to joint activities; or where the non-operator has been held liable by a third party that has suffered such loss or damage.

The operator is generally obliged to “make timely payments in accordance with the Agreement [*i.e.*, the JOA] of all expenses incurred from the activities for the Parties of the joint venture”.⁷⁷ This clause indicates that joint costs should be channelled through the operator, but the reference to “the Agreement” leaves it somewhat open to discussion whether this is meant to be exclusive, *i.e.*, blocking direct claims from one non-operator against the others. The basic principle that all joint costs shall be borne proportionally by all the participants does not seem to contribute much to this discussion.

⁷⁷ JOA art. 3.2. In the early Norwegian JOAs the words “in accordance with the Agreement” were not included in the clause, which otherwise was similar.

The general system for establishing obligations and for making payments and running accounts for the joint activities all indicate that all joint costs should be channelled through the operator – and thereby through the control system of the MC and the technical mechanism for processing payments. There seems to be little reason to make any exception in cases where originally the costs were incurred by a non-operator.

On this basis the conclusion is that payment obligations under the JOA are only valid if they take the form of cash calls.

7.5 Does a cash call imply an unconditional obligation to pay?

A participant receiving a cash call could consider the request to be invalid for material or formal reasons. Does it still have to pay in order not to be in default under the JOA?

Several types of objections to payment are conceivable, *e.g.*, that the expenditure in question is not relevant to the joint activities or has not been approved according to the required procedures, or that the cash call has not been presented in the correct form or at the correct time or provides an incorrect due date.

Unless the MC intervenes to the benefit of the objecting party, and provided the objection is maintained, the objection will constitute a “dispute arising in connection with this Agreement”, which “shall be settled by arbitration in Norway pursuant to Norwegian law.” While awaiting such clarification, there is nothing unusual about the situation: the objecting party has to make a choice between paying under protest (and obtaining a refund if successful at arbitration) or refraining from paying, and running the risk of being declared in default in a subsequent arbitration.

In the latter case, interest on late payments will start to run from the due date. But what about the other consequences of being in default – does the party lose its voting right five days after the cash call due date, or only if the arbitration panel subsequently declares it to be in default? The problem is that the decision on the voting right has to be taken long

before the legal situation is sorted out – and this decision may well have irreversible consequences irrespective of whether the participant is excluded from voting and information or not. Normally this uncertainty will force the objecting party to pay under protest – there is usually no inherent economic risk in doing so because of the participants' secondary joint and several liability. But what if the party refuses to pay, insisting that no obligation exists?

The problem is basically whether the refusal to pay in accordance with the cash call should unconditionally constitute default for the purposes of applying the sanctions for default contained in the JOA.

One situation can be dealt with initially: if the cash call clearly lacks any material or formal foundation in the JOA, there can hardly be an unconditional obligation to pay. Supposedly, such a situation would be extremely unusual, but should it nevertheless occur it would presumably be handled by the MC – bringing the issue within the realms of the ordinary voting system. Similarly, it must be a pre-requisite that the operator when presenting the cash call asserts it to be a valid cash call according to the JOA and the AA.

Disregarding this unlikely situation, a general rule needs to be established.

The wording of the agreement indicates that the decisive factor is whether there actually is a payment obligation: according to the JOA articles 8.1 and 8.2, the obligation to provide sufficient funds depends materially upon the funds being needed to cover “expenses relating to the activities of the joint venture” and formally upon the procedural requirements of the JOA and the AA being fulfilled. These provisions can hardly be taken as arguments for the existence of an unconditional obligation to pay in accordance with any cash call.

On the other hand, the joint venture has some characteristics that seem relevant in this context. First, all joint activities depend on the availability of running contributions from the participants. If funds called for are not paid by a participant, there is no joint capital available to cover the missing contribution – hence the co-venturers' obligation to cover defaulted amounts in addition to their own shares. Second, due

to the general power vested in the MC, any dispute over a cash call is in reality a dispute between a minority and a majority under the voting rules – not between a non-operator and the operator issuing the cash call. And, finally, because the joint activities require a continuous stream of financial contributions from the participants, there will usually be a convenient practical opportunity to offset any claim for reimbursement of payments made under a cash call that is later declared invalid.

These factors have to be viewed in conjunction with the above-mentioned argument concerning irreversibility (*i.e.*, decisions may be made with consequences that cannot later be changed).

On this basis it must be concluded that there is less risk for both the participant opposing the cash call and to his co-venturers if the cash call is paid under protest than if matters are brought to a head by a refusal to make payment. This would seem to justify the general rule that non-payment under a cash call unconditionally constitutes default in relation to the default provisions of the JOA. But it should be noted that the MC at any time may intervene, implying that a majority of the co-venturers may suspend the cash call or confirm it, removing the risky uncertainty.

According to general contract law, default under a payment obligation cannot normally be excused by reference to *force majeure* – the debtor is strictly liable no matter the reason for the default.⁷⁸ In line with this the JOA's provisions on the consequences of default do not distinguish between the various possible reasons for the default. And, as a general rule, the defaulter cannot avoid these consequences by proving that the default was not attributable to any reason within its control – either on the basis of the JOA (or the AA) or on the basis of general contract law.⁷⁹ There is one modification to this: if a “continuous default is due to intervention by Norwegian authorities”, a demand for

⁷⁸ See e.g. Hagstrøm, *Obligasjonsrett* (2003) p. 507.

⁷⁹ Including company law, which in principle could be relevant even though the JOA is not subject to the Company Act, see Kaasen, *Samarbeid i olje* (footnote 8 above) on pp. 165-169.

the assignment of the defaulter's participating interest "may not be asserted on the basis of such default", nor will it be deprived of its rights to data and information.⁸⁰ But the defaulter loses its right to vote, which depending on the circumstances may have drastic consequences, and the co-venturers will have to cover the defaulted contribution(s) (and may consequently acquire the defaulter's part of the production), as no exceptions are made in this respect. It may be added that situations covered by this provision may well have other implications that render the modification less interesting.

8 Concluding remarks

The JOA art. 8.1 states that the participants are obliged to provide funds necessary to perform the joint activities that have been determined by the MC, and art. 7.1 obliges each participant to cover its proportionate part of funds not contributed by a (defaulting) co-venturer. Viewed in isolation, this would seem to indicate that a need for funds to cover joint activities is sufficient to cause a payment obligation to arise.

This might have been the case under the early Norwegian JOAs.⁸¹ But under the present regime⁸² we have seen that comprehensive mechanisms are employed to specify the basis and extent of the payment obligation. The *purpose* of these mechanisms is to allow the non-operators to stay in control of the expenditure the operator undertakes on behalf of the joint venture. The *means* range from the general system for decision-making within the joint venture, through to the procedures for establishing work programmes with related budgets and procurement mechanisms, further via the specific authorisation for expenditure, and finally to the technical nitty-gritty of cash calls. Compared to the early Norwegian JOAs, this system of regulation provides a strict

⁸⁰ JOA art. 9.5.

⁸¹ See Kaasen, , *The Co-operation ...* (footnote 34 above) at p. 3-123 to 3-125.

⁸² Implemented retroactively in PLs dating back to 1972, cf. Section 2 above.

structure of proposals, plans and decisions in an interplay between the MC and the operator, leading up to much more precise system of authorisation for the operator to incur costs on behalf of the joint venture.

Consequently, under the present JOA regime, the basis for payment obligations is not to be found in the provision obliging the participants to provide funds to cover joint activities, but rather in the provision stating that “The Operator may only incur expenses and financial obligations on behalf of the joint venture within the limits of the authorizations for expenditure as approved by the management committee pursuant to the exploration, operation and investment budgets.”⁸³

It is this latter provision, rather than the “link of causation” indicated in the former provision, that defines the limits for valid cash calls. The cash call expresses the ultimate conclusion of a lengthy process prescribed by the JOA. A cash call that allegedly does not constitute such a conclusion accordingly does not impose a payment obligation and cannot give rise to sanctions for default.

In other words, though the JOAs have changed over the years, the general rule is still that any payment obligation under the JOA has to be rooted in the power vested in the MC, subjecting a minority to the decisions of a majority. This implies that valid payment obligations must be based on, *i.a.*, the scope of the JOA, the voting rules of the JOA and the general rules on abuse of power limiting the application of the voting rules even within the framework of the scope of the JOA. So far, little is new under the sun. But the extended system for defining payment obligations, found in the standardised JOAs since 2007, adds to this by requiring detailed procedures to be followed leading up to the crucial instrument – the cash call. These procedures have the effect that two aspects of the internal life of the joint venture are taken care of better than before: in the relationship between the minority and majority participants the formal requirements may offer some protection to

⁸³ JOA art. 12.5 first paragraph. Certain joint costs can for practical reasons hardly be processed along these lines, but may still form the basis for a valid cash call, *e.g.*, third-party claims for damage caused by joint activities, cf. Section 7.2 above. This does not, however, alter the general application of these observations.

the minority, while in the relationship between the operator and the MC the procedural requirements contribute to the shift in balance we have seen over the years.

New laws on passenger rights

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People they rush everywhere
Each with their own secret care
So ferry 'cross the Mersey
and always take me there
Gerry Marsden

1 Introduction

Legal issues relating to passengers have been subject to piecemeal regulation in international instruments, in particular concerning compensation for death and personal injury. Now, however, a more comprehensive European system is emerging, with passenger rights regulations that will supplement the international conventions.¹ This system is in turn supplemented by legislation on package travel² – the passenger counterpart to the multimodal transport of goods.

Obtaining an overview of the new law is no easy task. Part 2 below summarises some of the key new legal features in order to demonstrate the interaction of the different instruments. Part 3 then takes a somewhat closer look at certain aspects of the provisions relating to delay and cancellation. The rules on package travel will not be addressed.

2 A survey of the new law

2.1 Death and personal injury

The international rules relevant to Europe in respect of liability for death and personal injury are summarised in the following table:

¹ See the tables below for references. For a policy context, see Jens Karsten: *Passengers, consumers and travelers: The rise of passenger rights in EC transport law and its repercussions for consumer law and policy*, *J Consum Policy* (2007) 30:117-136.

² Council Directive 90/314/EEC of 13 June 1990 on package travel, package holidays and package tours.

	Instrument	Limit of liability per capita	Global limitation?	Basis of liability	Exceptions to limitation?	Insurance
Air	Montreal Convention, 1999 ^a	SDR 113,100, art. 21 ^b	No	Strict, art. 17	Negligence with reversed burden of proof, art. 21	Unspecified obligation, art. 50 and somewhat more specific in Reg. 2027/97 ^c art. 3
Rail	COTIF/ CIV ^d 1999	SDR 175,000, art. 30	No	Unavoidable operational event, art. 26	Yes, art. 48	Unspecified obligation, Dir. 95/18 ^e art. 9 and Reg. 1371/2007 ^f art. 12
Seagoing vessels	Athens Convention, ^g 2002	At least SDR 400,000, art. 7	Yes, LLMC, ^h 1996 etc; Reg. 392/2009 ⁱ art. 5	Quite strict for the first SDR 250,000 in operational events; otherwise negligence (with a reversed burden of proof in operational events), art. 3	Yes, art. 13	For the first SDR 250,000, art. 4bis
Inland waterways	CVN, ^j 1976	SDR 66,667 ^k	Yes, CLNI ^l	Negligence (with a reversed burden of proof in operational events), art. 5)	Yes, art.13	No
Bus and coach	CVR, ^m 1978	At least SDR 83,333, art. 13 ⁿ	No	Unavoidable operational event (with exceptions), art. 11	Yes, art. 18	No
	Dir. 103/2009 ^o	Not addressed	No	Not addressed	Not addressed	At least EUR 1 mill. per victim or EUR 5 mill. per claim
	Reg. 181/2011 ^p	At least EUR 220,000, art. 7	No	National law, art. 7	No	See above

^a Convention for the unification of certain rules for international carriage by air, 1999. All conventions referred to in the following are available at folk.uio.no/erikro/WWW/corrgr.

^b The limits of the Montreal Convention are revised by means of the tacit amendment procedure, see ICAO State Letter LE 3/38.1-09/87 dated 4 November 2009.

^c Regulation (EC) No 2027/97 of the Council of 9 October 1997 on air carrier liability in respect of the carriage of passengers and their baggage by air.

^d Convention concerning international carriage by rail (COTIF) of 9 May 1980 in the version of the Protocol of modification of 3 June 1999; Uniform Rules concerning the contract of international carriage of passengers by rail (CIV - Appendix A to the Convention).

^e Council Directive 95/18/EC of 19 June 1995 on the licensing of railway undertakings.

^f Regulation (EC) No 1371/2007 of the European Parliament and of the Council of 23 October 2007 on rail passengers' rights and obligations.

^g Athens Convention relating to the carriage of passengers and their luggage by sea, 2002.

^h Convention on limitation of liability for maritime claims, 1976, with Protocol of 1996.

ⁱ Regulation (EC) No 392/2009 of the European Parliament and of the Council of 23 April 2009 on the liability of carriers of passengers by sea in the event of accidents.

^j Convention on the contract for the international carriage of passengers and luggage by inland waterway (CVN), 1976.

^k As amended by the Protocol to the Convention on the contract for the international carriage of passengers and luggage by inland waterways (CVN), of 5 July 1978.

^l Strasbourg Convention on the limitation of liability of owners of inland navigation vessels (CLNI), 1988.

^m Convention on the contract for the international carriage of passengers and luggage by road (CVR), 1978.

ⁿ As amended by the Protocol to the Convention on the contract for the international carriage of passengers and luggage by road (CVR), of 5 July 1978.

^o Directive 2009/103/EC of the European Parliament and of the Council of 16 September 2009 relating to insurance against civil liability in respect of the use of motor vehicles, and the enforcement of the obligation to insure against such liability.

^p Regulation (EU) No. 181/2011 of the European Parliament and of the Council of 16 February 2011 concerning the rights of passengers in bus and coach transport and amending Regulation (EC) No. 2006/2004.

Despite – or perhaps because of – the long-standing international cooperation in this field, the regulation of liability for death and personal injury tends to diverge rather than converge as between the different modes of transport.

First of all, the levels of liability vary considerably, from some SDR 60,000 per capita in inland waterways traffic to SDR 400,000 for seagoing vessels. There seems to be no justification for this. The lack of consistency is emphasised by the differences in the circumstances in which the limitations on liability may be set aside. For air carriage negligence suffices, but the limitation rules are almost impossible to set aside where carriage is by sea.

A justification for imposing different limits on liability can hardly be found in the differences in total risk exposure. Although seagoing ships may be said to have greater exposure because very many passengers may be carried on a single vessel, seagoing ships nevertheless have the highest per capita limit.

The total exposure becomes more manageable through the application of global limitation. But there is no consistency in when a global limit applies and when it does not. The law on global limitation is generally not harmonised.³

³ Regulation 392/2009 art. 5.

Secondly, the basis of liability varies, from negligence to strict liability.

Thirdly, insurance requirements are very different for the different modes of transport. This applies both to whether insurance is required at all and, if it is, what is covered under the insurance and how specific the requirements are. While maritime insurance is required to include an element of war insurance, inland vessels are subject to no insurance requirement at all. Buses and coaches are subject to the general motor vehicle insurance regime.

Even within each mode of transport, the limits may vary to some extent due to national law. In addition, the effects of the limits vary considerably depending on what expenses are covered by social security systems without recourse. A limit on liability will, of course, have quite a different effect if most necessary expenses are covered by social security and kept out of the liability system (as is the situation in Norway) than if this is not the case.

2.2 Luggage

The provisions for compensation for damage to and loss of luggage also vary considerably according to the mode of transport, both in respect of the basis for and limits on liability:

	Air Reg. 261/2004^a	Rail Reg. 1371/2007^b	Vessels Reg. 1177/2010^c	Bus and coach Reg. 181/2011
Luggage, etc.	Montreal Convention art 22 (SDR 1,131) ^d	Art. 11, referring to CIV ch. III (SDR 1,200)	Athens Convention art. 3 and 8 (SDR 2,250 for hand luggage)	Art. 7 (EUR 1,200); supplemented by Dir. 103/2009
Wheelchairs etc.	Reg. 1107/2006 ^e art. 12	Art. 25 (unlimited)	Art. 15 (unlimited); Reg. 392/2009 art. 4	Art. 7 and 17 (unlimited)

^a Regulation (EC) No 261/2004 of the European Parliament and of the Council of 11 February 2004 establishing common rules on compensation and assistance to passengers in the event of denied boarding and of cancellation or long delay of flights, and repealing Regulation (EEC) No 295/91 .

^b Regulation (EC) No 1371/2007 of the European Parliament and of the Council of 23 October 2007 on rail passengers' rights and obligations.

^c Regulation (EU) No 1177/2010 of the European Parliament and of the Council of 24 November 2010 concerning the rights of passengers when travelling by sea and inland waterway and amending Regulation (EC) No 2006/2004.

^d The limits of the Montreal Convention are revised by means of the tacit amendment procedure, see ICAO State Letter LE 3/38.1-09/87 dated 4 November 2009.

^e Regulation (EC) No 1107/2006 of the European Parliament and of the Council of 5 July 2006 concerning the rights of disabled persons and persons with reduced mobility when travelling by air.

It is difficult to see any reason for these variations.

An interesting feature of EU law is the special provisions providing for compensation in respect of wheelchairs and other equipment for the disabled. Such compensation is generally exempted from the limits that otherwise apply to luggage (or even personal injury), perhaps because such items are not seen as "luggage" that as such is subject to the limits laid down in international conventions. While the idea may be to provide enhanced protection for the disabled, it may just as well be to ensure that the social security systems responsible for funding such equipment shall not suffer loss.

2.3 Advance payments

After an accident, an injured claimant will often be in a desperate financial position. He may have lost his income and also have incurred injury-related expenses. Dependents may be in a similar position. It is therefore important to secure the claimant's cash-flow position so that he is able to meet his expenses and so that his bargaining position will not be weakened by extreme financial pressure when negotiating a settlement:

	Air Reg. 261/2004	Rail Reg. 1371/2007	Vessels Reg. 1177/2010	Bus and coach Reg. 181/2011
Advance payment and relief	Montreal Convention art. 28 Reg. 2027/97 art. 5	Art. 13	Reg. 392/2009 art. 6	

The only international convention (in this area of the law) that provides for advance payments is the Montreal Convention on air carriage.⁴ Under EU law, similar rights are secured for passengers carried by rail services and by sea, even though this may require the carrier to make unrecoverable payments that go beyond his obligations under the international conventions. Strangely, no similar right is secured for bus and coach passengers.

2.4 Alternative bases of claims

A general problem in relation to the EU passenger rights regulations is their relationship with international conventions. In particular, if the EU as such has ratified a convention – as is the case with the Montreal Convention – the regulations cannot put passengers in a better position than what is allowed under the convention. A similar problem arises if the Member States would have to denounce conventions they have ratified in order to accommodate rights granted under the regulations.

To a great extent there is no overlap, or at least there are no competing rules. This is so in respect of claims for death and personal injury, where the EU instruments do not address the issue unless the international conventions open the way for them to do so (as is the case with the CVR).⁵ However, *e.g.*, the carrier's duty to cater for passengers in the event of delay and to give them cash compensation, which clearly has economic implications, may need to be coordinated with limits on lia-

⁴ See regarding the relationship with the EU instrument, Kenneth M Nielsen *Passageransvaret ved international luftbefordring* (Copenhagen 2009), pp. 293-5 and Stephen Paul Dempsey and Svante O. Johansson: *Montreal v. Brussels: The conflict of laws on the issue of delay in international air carriage*, *Air & Space Law* (2010) 35:207-224.

⁵ See the table above in 2.1.

bility (if any) for delay contained in the conventions (which is the case in respect of the Montreal Convention).⁶

The conventions typically state that they apply regardless of the basis for claims. The regulations address this by means of special conflict rules:

	Air Reg. 261/2004	Rail Reg. 1371/2007	Vessels Reg. 1177/2010	Bus and coach Reg. 181/2011
Alternative bases of claims	Art. 3, 8, 12 and 13 Montreal Convention art. 29	CIV art. 52	Art. 21; Athens Convention art. 14 and 3(5)(d)	Art. 2 and 22

The regulation on air passenger rights (article 12) thus provides that cash compensation – but apparently not other benefits⁷ – provided to passengers shall count towards compensation provided under the convention. Presumably the same is true under the regulation on rail passenger rights, although in this regulation, the matter of conflict is not even expressly mentioned. The other regulations merely suffice to allow further claims.

2.5 Provisions limited to certain modes of transport

Some of the provisions in the EU regulations are remarkable first of all because their scope is limited to one or two modes of transport. This applies to the provisions on overbooking, upgrading and downgrading, as well as price discrimination:

⁶ See the table below in 3.1.

⁷ See regarding the legality of this (answered in the affirmative), ECJ Case C-344/04 *The Queen on the application of: International Air Transport Association and European Low Fares Airline Association v Department for Transport*, para. 45 and Nielsen *l.c.* pp. 244-9.

	Air Reg. 261/2004	Rail Reg. 1371/2007	Vessels Reg. 1177/2010	Bus and coach Reg. 181/2011
Overbooking; procedure and compensation	Art. 4 and 7-9			Art. 19
Upgrading and downgrading	Art. 10			
Prohibition of price discrimination			Art. 4	Art. 4
Assistance with claims against third parties		Art. 14		

In carriage by air, overbooking (“denied boarding”) is a classic problem. Without penalising the practice, the regulation on air passenger rights lays down quite detailed procedures for dealing with the problem, through voluntary agreements and providing compensation when too many passengers turn up.

The regulation on bus passenger rights briefly mentions that overbooking should be dealt with as a form of delay where passengers are left behind as a result. The other regulations, however, are totally silent on the matter. In respect of carriage by sea in particular, limited capacity of lifesaving equipment can make it necessary to leave passengers behind. However, overbooking does not seem to be as common in this sector as in aviation.

Similarly, the rules on upgrading and downgrading in the regulation on air passenger rights are not found in the other regulations. A train passenger who is downgraded due to lack of space thus has no right to a standardised level of compensation.

A third example of the lack of cross-modal thinking concerns the provisions against price discrimination, found in the regulations affecting vessels and buses/coaches. For some reason, similar provisions do not apply to air and rail carriage.

Finally, the regulation on rail passenger rights includes a unique provision:

Article 14

Contestation of liability

Even if the railway undertaking contests its responsibility for physical injury to a passenger whom it conveys, it shall make every reasonable effort to assist a passenger claiming compensation for damage from third parties.

It makes sense that the passenger should not suffer due to, *e.g.*, the splitting up of rail services into infrastructure-related services (track maintenance *etc.*) and rolling stock-related services (train services). Even if the train company is not responsible because the accident resulted from a defect in the rail infrastructure, the least it can do is assist the passengers with their claims. But why not simply make it clear that a rail company is responsible for the agents and infrastructure it makes use of to fulfil its contractual obligations? And why is this duty to provide assistance limited to rail services?

2.6 Disabled passengers

All the regulations include detailed provisions on non-discrimination against disabled passengers:

	Air Reg. 261/2004	Rail Reg. 1371/2007	Vessels Reg. 1177/2010	Bus and coach Reg. 181/2011
Arrangements for the disabled	Art. 11 Reg. 1107/2006	Ch. V	Ch. II	Ch. III; art. 24

3 Cancellation and delay

3.1 Introduction

One of the hallmarks of the passenger rights regulations is their provisions on cancellation and delay. All four regulations contain provisions to this effect, giving rights to travel information and information on rights, standardised compensation, rerouting and care (meals, accommodation):

	Air Reg. 261/2004	Rail Reg. 1371/2007	Vessels Reg. 1177/2010	Bus and coach Reg. 181/2011
Cancelling; care and compensation	Art. 5 and 7-9	Art. 7 and 15-18; CIV art. 32	Art. 16-19	Art. 19-21; 23
Delay; care and compensation	Art. 3 (check-in) and 6 -9 Montreal Convention art. 19 and 22 (SDR 4,694) ^a	Art. 15-18; CIV art. 32	Art. 16-19	Art. 19-21; 23
Travel Passes		Art. 17	Art. 19 and 20	Art. 19 and 23
Poor regularity	Licensing and slot conditions	Art. 17 and 28 (service quality standards); licensing and slot conditions	Licensing conditions	Licensing conditions

^a The limits of the Montreal Convention are revised by means of the tacit amendment procedure, see ICAO State Letter LE 3/38.1-09/87 dated 4 November 2009.

The provisions vary slightly, in particular in respect of the number of minutes of delay necessary to trigger the delay provisions. This makes it difficult for passengers to find out exactly which rules apply.⁸

⁸ The passenger rights instruments do, however, include provisions on information to passengers.

Sometimes passengers have better rights for cancellation and rebooking than for delay. This means that in the case of prolonged delays, it is necessary to have rules limiting the scope of the delay rules, so that the cancellation rules are triggered. The ECJ accepted this approach in a recent case on the regulation on air passenger rights.⁹

“... Articles 5, 6 and 7 of Regulation No 261/2004 must be interpreted as meaning that passengers whose flights are delayed may be treated, for the purposes of the application of the right to compensation, as passengers whose flights are cancelled and they may thus rely on the right to compensation laid down in Article 7 of the regulation where they suffer, on account of a flight delay, a loss of time equal to or in excess of three hours, that is, where they reach their final destination three hours or more after the arrival time originally scheduled by the air carrier.”

Although there is some case law relating in particular to the regulation on air passenger rights,¹⁰ this is a rare example of the court actually adding to the stipulated rights rather than simply specifying them.

A matter that has not been addressed in the regulations is delay at terminals, such as airports. The regulation on air passenger rights makes it a condition that passengers must present themselves for check-in at the time stipulated by the carrier or 45 minutes before departure, unless they are transferring from another flight (article 3). The regulation is silent on delays caused by unusually lengthy check-in queues (which may prevent passengers from presenting themselves for

⁹ C-402/07 *Christopher Sturgeon Condor Flugdienst GmbH and C-432/07 Stefan Böck v Air France SA*. For a critical comment, see John Balfour: *Airline liability for delays: The Court of Justice of the EU rewrites EC regulation 261/2004*, *Air & Space Law* (2010) 35:71-75.

¹⁰ The case law relating to each article is listed in the bibliographical pages of Eur-Lex, e.g., <<http://eur-lex.europa.eu/Notice.do?val=342673:cs&lang=en&list=493083:cs,461583:cs,443076:cs,438143:cs,342673:cs.&pos=5&page=1&nbl=5&pgs=10&hwords=>>>.

check-in)¹¹ or extraordinary waiting times for security control (so that passengers miss their flights), and does not prevent a carrier from insisting that passengers present themselves for check-in or at the gate unduly far in advance of the departure time. Thus passengers carry a considerable risk regarding delay at this stage, perhaps even delay caused by the carrier's understaffing at the check-in counter or that could have been avoided had the carrier provided information about expected delays at security. This is perhaps the regulation's major shortcoming.

The other regulations do not address check-in at all (except in relation to the special rights of disabled passengers). There is a possibility, then, that passengers may lose some benefits of the regulations by not adhering to strict check-in requirements.

3.2 The regulations and regular travellers

Some attention appears to have been paid to regular travellers in the more recent EU regulations. It is expressly stated that holders of open tickets do not have any rights in respect of cancellation and delay, even apparently if they turn up for a particular departure. However, holders of travel passes (for unlimited travel within a certain period) are exempt from this rule even if they are not booked on the delayed or cancelled departure.¹² Their compensation may be proportional to the price paid.¹³ The outcome is that the best customers get the least compensation.

The problems for regular travellers do not stop here. Delays and cancellations are, of course annoying for all passengers. However, such events are perhaps even more annoying for commuters and other regular users of transport services. Indeed, for these travellers daily

¹¹ A proposal that "the airline shall be responsible for identifying those passengers still in the queue at the time of closing the check-in for a flight, who shall be deemed to have presented themselves for check-in" was rejected, see Commission amended proposal for a Council Regulation (EC) amending Council Regulation (EEC) No 295/91 establishing common rules for a denied boarding compensation system in scheduled air transport (98/C 351/06).

¹² See the table above in 3.1.

¹³ Reg. 181/2011 art 19; Reg. 1371/2007 art. 17.

delays are extremely annoying, even if they are way below the limits that trigger the delay or cancellation provisions in the regulations.

Requiring strict adherence to timetables is not a good way of dealing with this problem. Carriers may, of course, provide ample time when scheduling timetables. Not all routes are much exposed to competition in this respect, so carriers will not risk losing passengers even if their advertised journey times are some minutes longer than the alternatives or the connection time stipulated is longer than strictly necessary. Regular travellers in particular often experience that services arrive before the scheduled time and that connections are often successful even though the actual connection time is shorter than that recommended. Timetables are not always a good benchmark for performance if poor regularity is to be penalised.

A better mechanism that is relevant for addressing poor regularity is the slot system that operates in air and rail carriage.¹⁴ One cannot arrive ahead of the slot time. And at busy airports and on busy railway lines, a delayed service that misses its slot will be further delayed waiting for the next free slot. Carriers very much prefer to avoid such situations, all the more so because a carrier that is often late is likely to lose its slot in the next negotiating round, as slots are allocated on the basis of historical data. The slot system is the regular traveller's best friend.

Poor regularity may also be penalised in the licensing conditions. Although these conditions are often not made available to the public, they are apparently not effective in this respect in relation to all modes of transport. With the exception of a few provisions in the regulation on rail passenger rights,¹⁵ such service standards fall outside the scope of the passenger rights regulations.

The most recent regulations, those on rail and vessel carriage, include

¹⁴ See IATA: *Worldwide Scheduling Guidelines* 16th ed., July 2008 <<http://www.iata.org/NR/rdonlyres/2C1BA18-6297-4984-A74E-4A6D1F945A55/0/WSG16thEdition.pdf>> and, e.g., Bordörfer *et al*: *An Auctioning Approach to Railway Slot Allocation*. ZIB-Report 05-45 (2005) <<http://www.zib.de/Publications/Reports/ZR-05-45.pdf>>.

¹⁵ See the table above in 3.1.

a provision that may apply to this type of frequent service irregularity:¹⁶

Passengers who hold a travel pass or season ticket and who encounter recurrent delays or cancellations during its period of validity may request adequate compensation in accordance with the railway undertaking's compensation arrangements. These arrangements shall state the criteria for determining delay and for the calculation of the compensation.

At least the problem is addressed. However, the rights of passengers are rather vague. The applicable sanctions and the definition of relevant irregularities are not at all clear.

3.3 The background law

Due to the incompleteness of the regulations, some remarks on the law otherwise applicable are warranted.

Delay is in many ways the 'stepchild' of contract law: it cannot be ignored, but it doesn't always fit in very well. This is also true of delay in the context of contracts for the carriage of passengers.

The regulation of carriage of passengers has, perhaps for this reason, traditionally been more preoccupied with claims for death and personal injury – and even for damage to and loss of luggage – than with delay.¹⁷ There are three main reasons for the special nature of problems associated with delay.

Firstly, delay in itself causes passengers no physical injury. In many legal systems, it has been more difficult to recover losses where there is no damage to person or property. Contractual problems concerning delay are, however, perhaps less problematic in this respect than issues arising from doubts as to whether there is a duty of care towards the person suffering loss, or where the only way the loss can be established is by reference to a contract to which not both parties in the delay dispute are ("obligatory rights").

¹⁶ Reg. 1371/2007 art. 17; Reg. 1177/2010 art. 19.

¹⁷ Two important discussions on the concept of delay in the context of transport are Lena Sisula-Tulokas: *Dröjsmålsskador vid passagerartransport* (Helsinki 1985) pp. 136 *et seq.* and Kurt Grönfors: *Tidsfaktorn vid transportavtal* (Gothenburg 1974).

Secondly, delay claims are special because often it is not clear at what point a delay actually occurs. Obviously, there are ETAs or even timetables. But the circumstances may often be such that one would not expect remedies for breach to be triggered by a delay. So how much delay is acceptable before a breach occurs? The result – arrival on schedule – is in any event not guaranteed, but is there a guarantee to use best endeavours? The vagueness of the obligation makes applying sanctions difficult. Indeed, this difference from the situation where damages are sought for physical loss may perhaps in itself have been a reason for limiting remedies to situations involving physical loss, as described in the previous paragraph.

Thirdly, remedies for delay challenge the system of contract law, in that compensation to preserve the bargain – the ratio between the exchanged values – is the exception rather than the rule. It may be that there is a market loss, as the value of the transport services may diminish during the delay: the value of transport to a weekend resort will perhaps be lower on a Saturday than on a Friday. But losses caused by delay are almost invariably consequential losses, and differ considerably. An example is loss caused by missing a connecting flight. Indeed, the delay may negate the whole purpose of the journey, such as where a passenger misses the football match he had tickets to attend. But even these consequential losses may to some extent be standardised, such as compensation (if any) for loss of private time. In particular for non-standardised consequential losses, one may well ask if they should be the risk of the individual passenger or the carrier.

Despite these special traits, there is, as already mentioned, a marked tendency to attempt to fit claims for delay into the system of contractual remedies. This is all well and good, but the contractual framework can seem rather narrow – in particular for claims concerning delay. Once again, it is worth considering some examples:

Firstly, the cause of the delay may often be outside the scope of the contract, because the contracts are consecutive. For example, the plane may have been delayed because of an event affecting a previous flight (“late incoming aircraft”). Should the causes for the delay be handled in

the same way whether they arise within or outside the scope of the contract? While what has happened in relation to the other contracts is of no direct relevance for the passenger, for the carrier it is highly relevant. Indirectly, however, it is very relevant for the passenger, as carriers that run tight schedules often offer lower prices.

Secondly, the passenger's expectations are not always based on the individual contact, even though his position is interpreted within the contractual paradigm. A person waiting for a scheduled train may not yet have a contract (have booked a ticket) with the train operator for that particular journey. Even so, that person may be just as much affected by any delay as a fellow passenger who has booked a seat in advance. This is another way in which problems to do with delay challenge the contractual framework.¹⁸

Thirdly, arguments concerning expectation are weakened rather than strengthened by pointing out the poor regularity of the service concerned. Looked at from the point of view of expectation, a passenger who knows that a train often runs late really has nothing to complain about when it does so yet again. Timetables are not guarantees, in particular not for those regular passengers who ought to know better.

So have the courts recognised remedies for passengers affected by delay?

The Swedish Supreme Court had to address a claim for damages against Swedish Railroads just before the regulation on rail passenger rights was adopted.¹⁹ A holder of an annual travel pass for a long-distance rail journey had between August 2000 and August 2001 been delayed on 103 of 398 journeys and had also had to abandon two journeys. The total delay was about 35 hours. No compensation was payable pursuant to the terms and conditions of the railroads and the Swedish court found no reason to use its powers under Swedish law to set aside the terms and conditions as unreasonable.

¹⁸ See on this Nicolay Bugge: *Nogen bemerkninger om transportselskapers ansvar for rutefravigelser m.v.*; Rt. 1915.353.

¹⁹ Case T 3734-05; NJA 2009 note N3 (the case was not fully reported in the official reports NJA).

The opinion of the dissenting judge, Professor Torgny Håstad, was more helpful to the claimant. He would not grant compensation for lost time on a *quantum meruit* basis (“*prisavslag*”), but he did suggest that delays of more than one hour should give a right to a 50 % refund. Even so, the resulting compensation would only have totalled SEK 600 (some EUR 70).

It seems as though the law leaves the regular traveller without any remedy for repeated delays. For this author’s part, it would seem that the problem here is not really the time lost, but the poor quality of the service. If the service really is poorer than what the passenger is reasonably entitled to expect, he should have a remedy for overall substandard performance (“*mangel*”) of the entire contract rather than for either the individual delays or all the individual delays added up. In that case, compensation on a *quantum meruit* basis would be available. And regular passengers could be remedied without any need to remedy the occasional traveller.

It is submitted that this approach would be far better than that adopted in the provisions on “recurrent delays or cancellations” in the regulations.²⁰ Although the latter approach does recognise that regular travellers have a need for other remedies than the occasional traveller, it still focuses on individual delays. But as the regulations as well as the conventions focus on performance in relation to individual journeys, it is suggested that the approach recommended here could be used in tandem with the regulations and the conventions.

4 Conclusion

The passenger will often benefit from invoking the EU regulations on passenger rights. But grasping the whole picture is not easy, either for passengers or lawyers. In many ways, this is an area of law still under construction, where the sets of rules need to be harmonised, completed and polished.

²⁰ See above in 3.2.

At the margins of carrier liability

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Introduction

What are the limits of the scope of the carrier's liability in the Inland Carriage of Goods by Road Act? Where does the carrier's liability end and one or more other forms of liability start? This is an issue that has become more important since carriers have started to take on a whole range of obligations in their contracts in addition to the transport of the goods. The nature of these other obligations varies considerably. They could involve a simple service such as lifting a pleasure boat from the water at a marina or storing goods in connection with transport, but sometimes the services are complex in nature, such as planning the logistics of transporting certain components and then assembling them into the final product.

This paper aims to discuss these issues in the aftermath of the Swedish Supreme Court case *If v Vikingstad*.¹ In particular we will discuss the carrier's mandatory liability in relation to mixed contracts, *i.e.*, contracts including a number of other obligations in addition to the transport obligation. We will also deal with liability for consequential damage and loss and the scope of application of the time-bar provision in the Inland Carriage of Goods by Road Act.

The case

In *If v Vikingstad* the road haulier Vikingstad Åkeri AB (Vikingstad) had entered into an agreement with Lars O. Andersson Olje AB (LOAB) to mix and transport by truck bunker oil from LOAB's terminal to the ferry *The Rogalin*, owned by Polish Baltic Shipping Co. The driver did not follow LOAB's instructions regarding the mixing of the oil, with the result that the mixed oil was of the wrong viscosity and caused damage to the ferry engine. LOAB paid compensation to the shipowner. This lia-

¹ NJA 2007.879 (ND 2007.10).

bility was covered by liability insurance provided by If Skadeförsäkring AB (If). Later If turned against Vikingstad in a recourse action claiming damages corresponding to what LOAB had paid the Polish Baltic Shipping Co. (less the excess).

Vikingstad repudiated the claim on the grounds that it was time-barred under section 41 of the Inland Carriage of Goods by Road Act (1974:610). If argued, however, that the Inland Carriage of Goods by Road Act did not apply to damage of this type and, in the alternative, that even if the Act did in principle apply, it did not apply to this situation, as it only regulated liability for loss and damage to the goods that occurred from the moment the carrier received the cargo until he delivered it to the consignee. Consequently, according to If, the special provision in section 41 of the Inland Carriage of Goods by Road Act establishing a time-bar period of one year was not applicable in this case, which instead was subject to section 2 of the Limitations Act (1980:130) establishing a general time-bar period of 10 years.

Carrier liability and mixed contracts

One of the key issues in *If v Vikingstad* was how to characterise the obligation to mix the oil in relation to the obligation to transport the goods. Essentially the Supreme Court had two choices: to view the obligation to mix the oil according to the instructions as a separate obligation; or alternatively to view it as an integral part of the transport obligation. The Supreme Court chose the latter alternative: the mixing of the oil had to be viewed as an integral part of the transport obligation.

The consequences of this choice were quite dramatic for If. Firstly, the claim was time barred, as it was subject to the special one-year time-bar period in section 41 of the Inland Carriage of Goods by Road Act. This would not have been the case if the Supreme Court had chosen to treat the obligation to mix the oil as a separate obligation, as then

section 41 would not have applied and the claim would have been subject to the general time-bar period. Correspondingly this decision was very favourable in relation to *Vikingstad*; the court's conclusion here meant that the carrier was covered by its own liability insurance – this would not have been the case if mixing the oil had constituted a separate obligation as, with regard to road carriage, liability insurance covers only liability arising under the Inland Carriage of Goods by Road Act. Liability arising outside the scope of the Act has to be covered by separate insurance.²

But what are the precise limits of the scope of carrier liability in this respect? It is quite clear that the mere fact that a certain obligation is included in a transport contract does not automatically entitle the carrier to limit his liability or benefit from the short time-bar period in the Inland Carriage of Goods by Road Act.

In *If v Vikingstad*, the Supreme Court justified its conclusion by stating that the mixing of the oil was carried out in immediate connection with the loading of the goods onto the truck. This was a natural conclusion, since the oil was mixed such that certain amounts of heavy and thin oil were pumped directly into the truck's tank. However, the Supreme Court case *Tekstil v Tedder* had already illustrated that timing cannot be the only decisive factor here.³

Tekstil v Tedder concerned the distinction between the transport and storage of goods. A Swedish company, Tedder, bought a parcel of clothing from a Danish company, Tekstil. The goods were sold “u franco Odense” and carried by Transportkompaniet to Borås. There the goods were stored in a warehouse belonging to the carrier. Tedder went bankrupt and, in order to protect itself against losses, Tekstil ordered Transportkompaniet not to deliver the goods to Tedder. Transportkompaniet, however, surrendered the goods to Tedder's bankruptcy estate against the payment of debts for performed transports and the storage of goods. Tekstil claimed compensation from both the bankruptcy estate and Transportkompaniet corresponding to the value of the goods on the

² See below regarding Bulk 91.

³ NJA 1985. 879 (ND 1985.1).

grounds that it was entitled to exercise its right of stoppage in transit.

Since entitlement to exercise the right of stoppage in transit ends once the buyer takes custody of the goods, one of the key issues in the case became the precise time at which the transport had ended and storage had commenced. Here the Supreme Court noted that as between Tedder and Transportkompaniet a practice had developed whereby the latter would always inform Tedder of the arrival of specific consignments at the warehouse in Borås. Tedder would then issue instructions as to how the goods should be handled. The Court concluded here that an instruction to continue to store the goods had to be considered equivalent either to an actual delivery to Tedder or to a transfer of the goods to an independent company for storage. The right of stoppage in transit had therefore lapsed.

Although *Tekstil v Tedder* must be construed in the light of property law principles, it does in any event indicate that factors other than timing may be relevant for determining whether a certain obligation should be viewed as a separate obligation or an integral part of the transport obligation. The storage of the goods occurred in immediate connection with the transport, but part of the storage was considered to represent a separate obligation from the transport obligation. The problem here seems to be how to establish a precise formula for determining whether additional obligations should be viewed as integral to the transport or as separate from it. Although they differ from each other in nature, the services performed under many modern logistics contracts are interrelated. Indeed this is the rationale behind these contracts. An example here would be a single contract that covers the transport, storage and assembly of components into computers that are finally carried to the customers by the same logistics service provider under the same contract. Is that provider a carrier, a freight forwarder,

or a manufacturer – is he all or none of the above?⁴ The logistics service provider appears in this respect to represent a sort of chameleon. It may be that the issue will have to be decided on a case-by-case basis. The relevant factors here seem to be not only whether the specific obligation was performed in immediate connection with the transport, but also the nature of the obligation, the terms of the individual contract and the conduct of the parties in relation to each other. To a certain extent these issues have been regulated in the standard freight forwarding contracts on the market. For example, the General Conditions of the Nordic Association of Freight Forwarders, NSAB 2000, § 27 A, explicitly provides that the transport of the goods becomes storage 15 days after arrival at the place of destination.

Consequential damage and loss

Liability

The other key issue in *If v Vikingstad* was liability for consequential damage and loss. Even if the mixing of the oil was considered an integral part of the transport obligation, did the Inland Carriage of Goods by Road Act apply to damage caused to other property than the actual goods, in this case the ferry engine? As regards the relationship between LOAB and Polish Baltic Shipping Co., the damage to the ferry engine appears to represent product-related damage, *i.e.*, damage to property owned by the buyer caused by the goods purchased. Such damage falls outside the scope of the Sales of Goods Act (1990:931).⁵ Since LOAB had

⁴ Heidbrink, J., *Logistikavtalet*, Uppsala 2005, 70, advocates the view that the logistics service provider performs none of these roles. According to Heidbrink, the logistics contract constitutes a special type of contract (*sui generis*), not subject to any mandatory transport legislation. This would, however, make it easy for the parties to circumvent the mandatory carrier liability just by entering into a logistics agreement rather than a transport agreement.

⁵ Section 67 of the Act.

not regulated its liability for damage of this type in its sales agreement with the Polish Baltic Shipping Co., it was fully liable in tort and had no possibility to limit the level of compensation.⁶

However, in the recourse action between LOAB and Vikingstad, the Supreme Court seems to have viewed the damage to the engine as consequential to the damage to the goods, and for such damage the carrier has the right to limit its liability under sections 32 and 34 of the Inland Carriage of Goods by Road Act.⁷ Although it was not explicitly stated, the fact that the Court emphasised that the oil had been mixed contrary to instructions and that the mixing formed an integral part of the transport obligation points in that direction. In other words, the wrongful mixing damaged the goods and this damage caused consequential damage to the ferry engine.

The conclusion of the Supreme Court in this respect corresponds with the Danish CMR case *Cementa v Codan*, even though the latter case concerned the issue of actual liability rather than a time-bar.⁸ Here Cementa AB had bought a parcel of cement from a manufacturer in Denmark. The cement was sold directly to Systembetong in Märsta, where it was to be used in the production of elements for a building facade. The cement, which was transported in a tank, became contaminated during the transport from Denmark to Sweden and as a result the facade elements became discoloured. Cementa paid compensation to Systembetong and then brought a recourse action against the Danish carrier's liability insurer.

In *Cementa v Codan* the Danish Supreme Court decided to apply the CMR Convention rather than product liability rules. The Court viewed the discolouration of the facade elements as consequential damage

⁶ The Product Liability Act (1992:18) is not applicable to property damage where the property is used for commercial purposes (section 1 of the Act).

⁷ The corresponding article 23(4) of the CMR Convention explicitly states "but no further damage shall be payable". See also Ulfbeck, V., *Produktansvarsskader i transportretten*, Copenhagen 2007, 150, who has questioned whether a carrier can be liable for product-related damage at all, since the carrier does not sell or manufacture any products, but merely transports them.

⁸ ND 1995.173 DH.

arising from the contamination of the cement. The Court emphasised also that the cement formed an essential part of the facade elements. In other words, the cement and the facade elements were so strongly identified with each other that effectively they could be considered to constitute the same goods. Thus the carrier was entitled to limit his liability to the value of the goods carried.⁹

The rationale behind the carrier's right to limit his liability for consequential damage arising from the loss of or damage to the goods is that revenues from transporting goods are very low compared to the potential consequential losses (such as loss of production) that may be suffered by the consignee. Such risks would be virtually impossible or at least very expensive to cover under liability insurance.

However, it is worth noting that the limitation only applies with regard to damages for consequential losses, *i.e.*, losses that arise following the loss of or damage to the goods. Neither *Cementa v Codan* nor *If v Vikingstad* can be construed to suggest that the carrier has the right to limit his liability for loss or damage to other property unless the transported goods have been lost or damaged. This is illustrated by the English CMR case *Shell Chemicals U.K. Ltd. v. P&O Roadtanks Ltd.*¹⁰

This case concerned a transport of ADIP (a liquefied chemical) from France to a refinery in the UK. During a stop in Hull the tank trailer containing ADIP was accidentally switched for one loaded with detergent, which upon arrival at the final destination was pumped into the refinery. As a result the refinery had to be shut down and cleaned. Subsequently Shell claimed compensation for loss of production.

In his judgment Saville J. found that the damage concerned was not covered by the CMR. He stated that: "the Convention deals with the liability of the carriers for loss of or damage or delay to the consigned goods during the period specified in art. 17(1) and with certain other cases for example failure to collect the "cash on delivery" charge".

This did not, however, imply that the carrier had no liability at all.

⁹ See also Johansson, S. O., *The scope and liability of the CMR – is there a need for changes*, *Transportrecht* 2002, 390–391.

¹⁰ [1993] 1 Lloyd's Rep. 114 Q.B.

On the contrary, Saville J. concluded with regard to the CMR Convention that: "I am prepared to assume for the purposes of the argument that the intent was to provide a complete code for the period stipulated in art. 17(1); but it does not begin to follow that the intent was therefore to exclude every other type of possible liability which is unrelated to loss of or damage or delay to the consigned goods unless expressly included elsewhere in the Convention".

The essence of the reasoning of Saville J. implies that damage arising in connection with the discharge of the goods, such as where the cargo is pumped into the wrong tank, would fall outside the scope of carrier liability in the Inland Carriage of Goods by Road Act. Such damage is not consequential in nature, since no damage to the transported goods has occurred during the relevant period, *i.e.*, between the time the goods were taken over and delivery.

It could perhaps be argued that in situations where the goods transported are damaged in connection with the discharge, because, for example, they are mixed with other goods, the resulting damage could be seen as a sort of cargo damage combined with consequential damage to the other property. Even though the latter damage would have materialised after the delivery, it would still be a result of the wrongful discharge of the goods. In such a case the carrier would be entitled to limit his liability to the value of the goods. A practical example here would be the pumping of a consignment of diesel into the gasoline tank at a gas station. Both the diesel and the gasoline would then be contaminated, but the carrier would be entitled to limit his liability to the value of the diesel. However, such a solution would lead to discrepancies with regard to the final allocation of liability. For example, if a third party were to claim compensation for damage to a car caused by the contaminated gasoline or diesel, the carrier would be liable to pay full compensation in tort. If, on the other hand, the third party were to claim compensation from the owner of the gas station, the carrier would be able to limit his liability in a recourse action.

This may support the view that all loss and damage caused to property other than the actual goods that occur as a result of the wrongful

discharge of undamaged cargo should be considered to fall outside the scope of carrier liability in the Inland Carriage of Goods by Road Act. In practice the parties involved in these types of transports have avoided the problem of determining who is liable for damage of this kind by developing specialised insurance (Bulk 91) to cover these risks. This insurance supplements the ordinary road hauler liability insurance. Even after *If v Vikingstad* there would still seem to be a need for such insurance.

The time bar period

Even if the provisions on liability and the right to limitation in the Inland Carriage of Goods by Road Act do not apply to damage to other property that occurs as a result of the wrongful discharge of undamaged cargo, does the special one-year time-bar provision apply in any event to claims relating to such damage? In other words, does section 41 of the Inland Carriage of Goods Act have a wider scope of application than the other provisions of the Act?

In *Shell Chemicals U.K. Ltd. v. P&O Roadtanks Ltd.*, Saville J. stated *obiter dicta* that, even if the provisions on carrier liability did not apply, article 32(1)(c) of the CMR was applicable in any event, since it provided a special limitation period for all cases other than those of loss of or damage or delay to the consigned goods. *If v Vikingstad* can be construed to suggest that the Supreme Court here agreed with the conclusion reached by Saville J., in that the Supreme Court stated that section 41 of the Inland Carriage of Goods by Road Act was applicable to all claims that could objectively be considered to derive from the transport agreement. It did not matter whether the claim was founded in contract or tort. Likewise it did not matter whether the claim was founded in the liability provisions of the Inland Carriage of Goods by Road Act or in general tort principles. A claim could derive from the transport agreement even though it did not concern compensation for damage regulated by the Act as long as there existed, objectively speaking, a connection between the claim and the transport agreement. In deciding whether a

claim derived from the transport agreement a number of factors were relevant: the identity of the claimant; the nature of the claim; and other circumstances regarding the origin of the claim.

We might be wise, however, not to exaggerate the conclusion reached by the Supreme Court on the scope of application of section 41 of the Inland Carriage of Goods by Road Act. As indicated above, the Court most likely viewed the damage to the ferry engine as consequential in relation to the damage to the cargo. With regard to claims based on tort law, the Supreme Court also referred to section 37 of the Inland Carriage of Goods by Road Act, which aims to prevent the consignor or consignee from circumventing the carrier's right to limitation by alleging that the claim is based on tort rather than the Act. In other words, it seems something of a stretch to assume that section 41 would cover all types of loss and damage whatsoever. For example, the Supreme Court has in older case law considered claims for personal injuries as completely outside the scope of transport law regulation, even though it could be argued that the claim objectively speaking derived from the transport agreement.

In *Darnell v ASG et al.*, Darnell agreed with ASG that the latter should transport two machines from Jönköping to Ljungbyholm. ASG sub-contracted the transport to Karlsson. While the truck was being unloaded in Ljungbyholm, one of the machines overturned and Darnell himself was badly injured. Karlsson had been in charge of the discharge operations. Later Darnell claimed compensation from ASG for the personal injuries he had sustained in connection with the discharge of the goods.

The Supreme Court here stated that nothing in the contract indicated that ASG had relieved itself from liability for injuries in connection with the discharge of the goods. According to general tort principles, ASG was liable for the acts performed by Karlsson. Even though the Supreme Court decided this case prior to the entry into force of the Inland Carriage of Goods by Road Act, this suggests that even today the Court would consider cases involving personal injuries as totally outside the scope of the Act, including the time-bar provision in section 41.

This is because the nature of this type of claim is totally different, even if the injury comes about as a direct result of the wrongful handling of the goods.

The scope of application of section 41 of the Inland Carriage of Goods by Road Act will most likely be highlighted in the future also with regard to property damage such as damage to other property than the transported goods that occurs in connection with the discharge of the cargo. It remains to be seen whether the Supreme Court will find that the time-bar provision in section 41 applies also to such damage, even though it is not subject to the provisions on liability and limitation in the Act.

Some final remarks

The above discussion illustrates that even after *If v Vikingstad* it is far from clear where carrier liability ends and other forms of liability start. In order to avoid disputes it seems important for parties entering into mixed contracts, such as complex logistics agreements, to define precisely the scope of the contractual obligations and the relationships between them. The more complex a logistics contract is, the more necessary it becomes to take a view on these issues. To a certain extent this has already been done in the existing standard freight-forwarding agreements used on the market, and the parties to certain types of transport agreements where there is a risk that property other than the actual goods will be damaged have solved the problem by developing specialist insurance. But if carriers start to take on other obligations in addition to the transport, such as planning the flow of components and the assembly of them into final products, it will become necessary to develop further the terms of the contracts in this respect. The parties will also need to ensure that the different risks are covered by insurance. And is this not what good practical legal work is all about: the foreseeing of risks in order to enable the parties to avoid them?

Limitation of shipowners' liability
and forum shopping in
EU/EEA states

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Innhold

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1 The framework

In most states within the EU/EEA the law on limitation of shipowners' liability is based either on the 1976 Limitation Convention or on this convention as amended by a Protocol of 1996 (1976/1996 Convention). Both these liability regimes establish an overall limit on the liability of a shipowner for the most important claims which may arise out of marine casualties. This statutory limitation of liability overrides the rules of liability applicable to particular maritime claims. The statutory limit, which determines a shipowner's maximum total liability for claims arising out of a particular casualty, is calculated on the basis of the tonnage of the ship that has caused the damage. The result is that in any particular case the limitation amount is distributed among the claimants in proportion to their established claims and the shipowner is relieved from liability for the portion of the claims not so covered.

There are substantial differences between the laws of the various EU/EEA states in this important area of maritime law. This is mainly because the 1996 Protocol implemented a substantial increase in the limits contained in the 1976 Convention, on which the laws of many EU/EEA states are still based. Another reason is that in relation to both instruments many states have made reservations exempting important types of claims from the overall limit, *e.g.*, claims relating to damage to harbour works, removals of wrecks and other clean-up operations after marine casualties, *cf.* NOU 2002: 15 pp. 30-31. In particular cases, consequently, questions as to applicable law may be important.

The rules on applicable law in respect of limitation of shipowners' liability are generally based on the *lex fori* principle. The current differences as to substantive limitation law consequently mean that in particular cases of shipowners' liability the law on the international jurisdiction of the courts often becomes decisive for the outcome. Accordingly, after a marine casualty, issues of jurisdiction often need the immediate attention of the parties. Each party will attempt to establish jurisdiction in the state offering the best prospects of success, while trying to avoid

any jurisdiction where the applicable limitation law will be more favourable to the other party. It is also difficult for the parties to negotiate settlements until they are in a position to assess where any trial of the liability questions involved will take place. Any realistic assessment of the relative bargaining powers of the parties can hardly be made before any jurisdictional issues are resolved.

The 1976 and the 1976/1996 Conventions lay down substantive rules relating to the overall liability of a shipowner for claims arising in respect of marine casualties. They do not contain rules on jurisdiction. In the EU/EEA states, questions concerning the international jurisdiction of courts are to be determined according to the almost identical regimes on the jurisdiction and the recognition and enforcement of judgments in civil and commercial matters contained in the Brussels I Regulation (EC) No 44/2001 and the Lugano Convention 2007. The provisions thereof contain:

- rules on jurisdiction determining at which court or courts in the EU/EEA states an action may be brought (Lugano articles 2 to 7). The court competent in a particular case is also competent to decide any question relating to limitation of shipowners' liability involved (Lugano article 7)
- rules on international *lis pendens* recognising the jurisdiction of the court where an action has first been brought (time priority), *cf.* Lugano articles 27 and 30. Any other court receiving an action in a dispute between the same parties and related to the same cause of action has a duty to suspend its proceeding and, when the first court has concluded that it is competent, to decline jurisdiction in the action. Thus, the decision on competence made by the court first seized has to be recognised by other EU/EEA courts even if the other court should consider that the jurisdictional issue was wrongly decided by the court first seized
- rules on reciprocal recognition of judgments of courts of the

EU/EEA states without substantive review at the time of recognition or enforcement (Lugano articles 32, 33, 38 and 39).

The rules on jurisdiction of the Brussels I/Lugano regimes only apply to actions against persons domiciled within the EU/EEA states (Lugano article 3). In actions against other persons the national jurisdictional rules of the state where the action is brought will apply (Lugano article 4). However, the rules on *lis pendens* and recognition of judgments are of general scope and will consequently apply even in such cases (Lugano articles 27, 32, 33 and 38).

The purpose of the Brussels I/Lugano regimes is both to prevent the continuation of parallel proceedings in the EU/EEA states relating to the same dispute between the same parties and to avoid the risk of mutually irreconcilable decisions in the same dispute being arrived at by courts in the various EU/EEA states. Thus the purpose is not to ensure that a dispute will be resolved in the same manner irrespective of the state in which a particular case is decided. There are general rules on applicable law in Regulation (EC) 864/2007 and Regulation (EC) 593/2007 that are designed to achieve this, but this body of law usually is of little interest in cases involving limitation of shipowners' liability. In any event, however, a judgment by an EU/EEA court shall be recognised in the other EU/EEA states without review even in a state where the applicable substantive law would have led to a different result, e.g., because of different rules on the limitation of shipowners' liability.

2 The problems

As already mentioned, the Limitation Conventions (1976 and 1976/1996) do not contain jurisdictional rules. However, both instruments contain provisions on how limitation of liability shall be implemented in particular cases (articles 10 to 13). Each of the instruments provides that the

shipowner has a right to establish a limitation fund for all claims arising out of a casualty or otherwise to invoke limitation at the court where an action for a limitable claim is brought against him. Each also gives a shipowner who has established a limitation fund a certain protection against subsequent actions in respect of claims which have been or may be raised against the fund. The objective is to avoid to the extent possible that shipowners shall be held liable for claims subject to limitation in excess of the limits of liability contained within the 1976 and 1976/1996 Conventions.

The relationship between this system for implementing the shipowners' right to limitation of liability and the EU/EEA legal regimes on jurisdiction and recognition and enforcement of judgments in the Brussels I Regulation and the Lugano Convention has been a controversial issue. The background is that the Brussels I/Lugano regimes both contain provisions making an exception for other conventions which in relation to particular matters govern jurisdiction or the recognition or enforcement of judgments (Lugano article 67). This exception applies, *e.g.*, to the Arrest Convention 1952 and the CMR Convention 1956. While it has been forcefully argued that this exception also covers the conventions on limitation of shipowners' liability, it is now established that such an interpretation is not correct. The reason is simple: the 1976 and 1976/1996 Conventions set out the substantive law on the extent and limitation of shipowners' liability, but they do not deal with matters of procedural law. Consequently, the Brussels I/Lugano regimes also apply to actions and judgments relating to limitation of shipowners' liability.

This matter was settled partly by the Court of Justice in *Mærsk Olie & Gas AS v. Firma M. de Haan en W. de Boer* (Case C-39/02), and partly by the final decision in that case subsequently made by the Danish Supreme Court (Scandinavian Maritime Law Report (ND) 2005 p. 631). In *The Lugano Convention and Limitation of Shipowners' Liability*, Scandinavian Institute of Maritime Law Yearbook 2005 (SIMPLY 2005) pp. 1, this author dealt extensively with the implications of *Mærsk* in the context of limitation of shipowners' liability.

In *Mærsk* the Court of Justice held that the decision by a Dutch court to establish a limitation fund was a “judgment” in relation to the Brussels I/Lugano regimes (Lugano article 32). Consequently, the Dutch decision had to be recognised by the Danish courts when a Danish claimant subsequently brought legal proceedings in Denmark instead of raising a claim for damages in the previously established Dutch limitation fund. Furthermore, at the time when the Danish action was to be decided by the Danish Supreme Court, the Dutch court had already decided to conclude the limitation proceedings and to release the fund because no claim had been filed in the fund before the time limit for filing claims had expired. In accordance with the view of the Court of Justice and the Dutch decisions establishing and concluding the limitation proceedings, the Danish Supreme Court held that the Dutch decisions relating to the limitation fund had to be recognised by Danish courts (ND 2005 p. 631). Consequently, it was held that the Danish claimant’s action was time-barred, and that the Dutch shipowner had to be acquitted. The Supreme Court also made it clear that the 1976 and 1976/1996 Conventions did not justify any exception from the Brussels Convention (the predecessor to the Brussels I Regulation). In 2007 this decision was relied on by the Norwegian Supreme Court when expressly holding that the equivalent exception in the Lugano Convention 1988 article 57 did not apply to the 1976 and 1976/1996 Conventions (Norsk Retstidende (*Rt.*) 2007 1759, at p. 1764). For a further discussion of this case see section 4 below.

Although the question of principle has thus been resolved, there are nevertheless a number of questions relating to the interaction in particular cases between the 1976 and 1976/1996 Conventions and the Brussels I/Lugano regimes on jurisdiction and recognition and enforcement of judgments. Generally speaking, the Brussels I/Lugano regimes contribute, on the one hand, to increasing the efficiency of the implementation systems of the 1976 and 1976/1996 Conventions and, on the other hand, to redefining the rules of the game for forum shopping, and also giving rise to new forms of forum shopping in cases involving limitation of liability. The purpose of this article is to draw attention to some of the resulting problems.

3 Establishment of limitation funds

3.1. According to article 11 of the 1976 and 1976/1996 Conventions, a shipowner is entitled to establish a limitation fund with the courts of the state where a claimant has initiated legal proceedings in respect of a claim subject to limitation. This condition is met if an action for damages or for the arrest of the ship is brought against the shipowner or – as held by the Swedish courts – if arbitral proceedings have been initiated against him (ND 2003 p. 40 and ND 2006 p. 73). The Conventions do not, however, contain provisions as to the jurisdiction or state in which a claimant may initiate legal proceedings against the shipowner. Consequently, whether the court where legal proceedings against the shipowner have been initiated is actually competent to deal with the claimant's action and the establishment of a limitation fund by the shipowner, is a question which in EU/EEA states is to be decided according to the rules on jurisdiction in the Brussels I/Lugano regimes. If the court chosen by the claimant is competent, the scope of its competence also covers questions relating to limitation of the liability of the shipowner (Lugano article 7), and the court may decide that according to article 11 of the 1976 and 1976/1996 Conventions the shipowner is entitled to establish a limitation fund with the court.

According to article 11 a limitation fund may be established only if the legal proceedings brought by the claimant actually relate to a claim subject to limitation according to the law on limitation of shipowners' liability in the state where the proceedings are initiated. This is important because article 18 paragraph 1 of the 1976/1996 Convention allows contracting states to make a reservation for the purpose of excluding from limitation the types of claims covered by article 2 paragraphs 1 (d) and (e) of the convention. These provisions deal with claims arising from clean-up operations after marine accidents and cover claims in respect of raising, removal, destruction or the rendering harmless of a ship which is sunk, wrecked, stranded or abandoned, including anything that is or has been aboard such ship, as well as claims in respect of

the removal, destruction or the rendering harmless of the cargo of the ship. Article 18 of the 1976 Convention allows equivalent reservations by the State Parties to that convention, but not to the 1996 Protocol. Many EU/EEA states have exercised these options and have excluded such claims wholly or partly from limitation according to the 1976 or 1976/1996 Conventions, cf. NOU 2002: 15 pp. 30-31. However, some states have instead adopted separate national limits of liability for excluded claims, cf. for instance the Norwegian Maritime Code §§ 172a and 175a.

It also follows from article 11 of the 1976 and 1976/1996 Conventions that a shipowner shall not be entitled to establish a limitation fund with the court where the shipowner himself has chosen to bring an action against one or more claimants holding claims subject to limitation. Even if the court is competent according to the Brussels I/Lugano regimes to deal with an action by the shipowner against such claimants, article 11 is a rule of substantive limitation law preventing the shipowner from invoking or asserting his right to limitation of liability in cases where legal proceedings have not yet been initiated against him by any claimant holding a limitable claim. In other words, even if the court is competent according to the Brussels I/Lugano regimes to deal with an action against the claimant, the court, applying the substantive limitation law governing the relationship between the parties involved, has to deny the motion by the shipowner to establish the limitation fund with the court. In such a case the condition for establishing a limitation fund contained in article 11, that legal proceedings against the shipowner have been brought at the court by a claimant, is not met and, consequently, the shipowner is not entitled to establish a limitation fund with the court which he himself has chosen.

3.2. Irrespective of article 11 of the 1976 and 1976/1996 Conventions, it is, as mentioned above, a precondition for the shipowners' right to establish a limitation fund that the court is competent to deal with the action for damages brought against him by a claimant. The legal proceedings against the shipowner must fall within the competence of the court according to the rules on jurisdiction applicable in the EU/

EEA state where the legal proceedings are brought. According to the Brussels I/ Lugano regimes, a limited number of jurisdictions – including the arrest jurisdiction – would be available to a claimant for an action against the shipowner. If, however, the particular claim is already subject to an action against the shipowner in another EU/EEA state, the rules on *lis pendens* (Lugano article 27) will prevent the court chosen by the claimant from accepting jurisdiction. In such a case, consequently, no limitation fund may be established by the shipowner at the court second seized of the action against the shipowner based on this particular claim.

On the other hand, the fact that an action in respect of a particular limitable claim for damages arising out of a casualty has been brought against a shipowner in one state, does not in itself necessarily prevent the shipowner from subsequently establishing a limitation fund before a competent court in another state where an action in respect of another claim arising out of the same casualty has been brought against the shipowner. The new action by another claimant gives the shipowner an opportunity to establish a limitation fund with the court where this action has been brought, provided that no limitation fund has already been established by the shipowner in connection with any former action against him. Moreover, this limitation fund will have effect for all limitable claims arising out of the same casualty. This fund normally also covers any limitable claim that is already the subject of a separate action in another state and, consequently, in accordance with the rules on *lis pendens* based on time priority, the shipowner would no longer be entitled to establish a limitation fund with a court of that state.

The basis for these views is that the rules on *lis pendens* only apply when the actions in two states are between the same parties and the cause of action for the two legal proceedings is the same. It follows from the decision of the Court of Justice in *Mærsk* that an action for damages and a motion for establishing a limitation fund do not have the same cause of action, *cf.* also ND 2006 p. 73 Svea Appellate Court. However, if the shipowner has already established a limitation fund with a court of another EU/EEA state where a claimant from the same casualty has

brought an action against the shipowner, such court is the court first seized of the claim to establish a limitation fund, and its competence and decision on the establishment of a limitation fund should be recognised in other EU/EEA states. Accordingly, no new fund may subsequently be established at a court in another state even if the limits of liability in the two states are different. This is a consequence of *Mærsk*. Although *Mærsk* does not prevent a particular claim arising out of the casualty from being made or from continuing to be the subject of a separate action in another EU/EEA state than the state where the limitation fund has been established, any judgment given in that action cannot be enforced independently of the previously established limitation fund, *cf.* the Danish Supreme Court decision ND 2005 p. 631 and the Norwegian Supreme Court decision in Rt. 2007 p. 1759).

A Swedish case (ND 2003 p. 40 and ND 2006 p. 73) illustrates some of the resulting problems. The case dealt with liability for costs incurred by the Dutch authorities relating to the removal of the wreck of *The Assi Eorolink*, which had sunk after a collision in Dutch waters. The facts of the case are not entirely clear. Actions relating to liability for the costs of wreck removal brought before Dutch courts apparently involved at least three parties, *viz.* the Dutch maritime authorities (claiming to recover the cost of the wreck removal), and one Swedish and one Dutch shipping company (both potentially liable for the cost of wreck removal as, respectively, the owner and charterer of the sunken ship). The Dutch actions also involved claims relating to the reciprocal liability of the two shipping companies. However, none of the Dutch actions involved questions of limitation of liability, since claims for wreck removal were not subject to limitation according to Dutch law.

At an early stage the Dutch company initiated arbitration proceedings against the Swedish company in Stockholm on the basis of a recourse claim for the wreck removal costs that it might have to pay to the Dutch government. According to Swedish law, however, a claim for the costs of wreck removal was subject to limitation, and at the request of the Swedish company the Swedish courts approved the establishment of a limitation fund with the court in Stockholm

(ND 2003 p. 40). Subsequently, the Swedish company asked for a declaratory judgment that pursuant to the establishment of the limitation fund its liability for any recourse claim from the Dutch company was subject to limitation according to the Swedish limitation fund procedure. The Swedish court agreed (ND 2006 p. 73 Svea Appellate Court). In accordance with *Mærsk*, the Dutch proceedings relating to claims for damages did not have the same cause of action as the limitation proceedings in Sweden. Regardless of other legal disputes between the parties, the Swedish company was entitled to a declaratory judgment that a right to limitation of liability existed and that the recourse claim would be subject to limitation in the fund.

It should be noted that in this case the Swedish company would not have been entitled to establish a limitation fund at a Dutch court or otherwise to invoke limitation since claims for the costs of wreck removal were not subject to limitation according to applicable Dutch law. By bringing a recourse claim in Sweden, instead of pursuing any recourse claim against the Swedish company in the actions before the Dutch courts, the Dutch company provided the Swedish company with an opportunity to establish a limitation fund in Sweden before any question of limitation of liability had been raised or finally decided by the Dutch courts. A consequence of this would also seem to be that, in accordance with *Mærsk*, the Dutch courts would later – in relation to any recourse claim between the two companies, perhaps also the claim by the Dutch authorities against the Swedish company – have to recognise the decisions relating to the limitation fund in Sweden. This result could probably have been avoided, at least by the Dutch authorities, by asking, at the time when the action was brought, for a declaratory judgment by the Dutch court that neither of the companies was entitled to limitation of liability in respect of its claim for the costs of wreck removal.

In view of the above, any claimant should carefully consider in which state to bring legal proceedings against the shipowner in respect of a claim subject to limitation. However, the lack of available jurisdiction for an action against the shipowner may force the claimant to initiate

the action in a state where the law on limitation of liability is less favourable, *e.g.*, based on the 1976 Convention, rather than in a state where the substantially higher limits of liability of the 1976/1996 convention would apply. Moreover, time may be of the essence. A claimant awaiting negotiations or a final decision of his claim may discover that in the meantime another claimant has brought an action against the shipowner in a state less favourable to him, giving the shipowner the opportunity to establish a limitation fund in that state. It may sometimes even happen that claims for recourse between a shipowner and a charterer with common interests in relation to a third-party claimant may be used as a basis for establishing a limitation fund in a jurisdiction less favourable to the third party.

4 The effects of a limitation fund being established

4.1 In the 1976 and 1976/1996 Conventions, the effects of the establishment of a limitation fund in accordance with article 11 of the conventions are dealt with in the provisions on “Bar to other actions” set out in article 13. The basic idea is that a shipowner, having established a limitation fund with a court of a State Party to the conventions, should not in other States Parties to the conventions be exposed to arrest or other enforcement action in respect of claims which have been or may be raised against the previously established fund. In the absence of provisions barring independent actions by particular claimants, the shipowner would run the risk of having to cover liabilities in excess of the overall limit of liability provided for in the 1976 and 1976/1996 Conventions for limitable claims arising out of the same casualty. However, the safeguards contained in article 13 of the conventions are not “water-tight”. There are several reasons why this is so.

Firstly, article 13 of the 1976 and 1976/1996 Conventions does not contain any general rule firmly obliging courts of another State Party to

decline an application for arrest or other enforcement action against the property of the shipowner in respect of claims subject to limitation in the limitation fund already established by him. The court has a duty to do so if the claimant already has raised his claim in such limitation fund (article 13 paragraph 1). If this is not the case, whether or not a claimant shall be barred from enforcing his claim independently of the limitation fund depends on the place at which the limitation fund has been established. Article 13 paragraph 2, second sentence enumerates four different situations where a claimant shall not be allowed to arrest or take other enforcement action in respect of a limitable claim against the shipowner who has already established a limitation fund. Thus, the court shall reject a demand by a particular claimant for such relief if the limitation fund has been established with the court at the place of the casualty, at the first port of call after the casualty, or with a court in the state where the arrest has been requested. The same applies if the claim arises out of a contract of carriage and a limitation fund has been established at the port of destination. In all other cases, however, it is left to the discretion of the court whether or not to decline a request for arrest or other enforcement action by a claimant pursuing a limitable claim independently of the limitation fund (article 13 paragraph 2, first sentence).

The provisions of article 13 paragraph 2, however, do not provide any particular guidance as to the circumstances which the court should take into account when exercising its discretion. Obviously, one factor must be whether the claimant has a legitimate interest in enforcing his claim through an action independent of the limitation fund, *e.g.*, because it would be unreasonable to force the claimant to pursue his claim in a foreign country. Even if the shipowner had to cover the claim, this would not necessarily mean that his liability towards the other claimants would increase. According to article 12 paragraphs 2 to 4, the shipowner would be entitled to acquire by subrogation the right to file a claim against the limitation fund in the amount which he has paid or will have to pay to the claimant.

Secondly, the protection afforded to the shipowner by article 13 of

the 1976 and 1976/1996 Conventions will be available only if the state where the limitation fund has been established and the state where the arrest or other enforcement action in respect of a particular claim is being sought are both States Parties to the same limitation convention. In this regard each of the limitation conventions is a separate regime. This is of importance because some of the states within the EU/EEA are parties to the 1976 Convention while others are parties to the 1976/1996 Convention. This means that if the limitation fund has been established according to national law based on the 1976 Convention, the fund will not be relevant as a bar to other actions if a claimant seeks to enforce his claim in a state whose limitation law is based on the 1976/1996 Convention. The court of a 1976/1996 state will have to conclude that the limitation fund in a 1976 state has not been established according to the 1976/1996 Convention and, consequently, that the 1976 limitation fund will not in any event be a limitation fund to be taken into account according to the provisions of article 13 of the 1976/1996 convention. As a matter of law, the situation would be the same if the limitation fund had been established in a 1976/1996 state and the arrest in respect of a limitable claim had been made in a 1976 state.

4.2 However, the interaction between the Brussels I Regulation/Lugano Convention and the international 1976 and 1976/1996 Conventions means that these shortcomings of the latter conventions generally are of little consequence for the effects of limitation funds established in an EU/EEA state. If the limitation fund has been established in an EU/EEA state, a claimant will not be in a position to exploit such loopholes in the 1976 and 1976/1996 Conventions by bringing an action against the shipowner in another EU/EEA state. This is because, according to the rules on *lis pendens* and recognition and enforcement of judgments in the Brussels I/Lugano regimes, the request by the shipowner to establish a limitation fund with a court in an EU/EEA state means that such court is first seized of the question of limitation of the shipowner's liability (*cf.* Lugano article 7) and, furthermore, that the decision by such court in establishing the limitation fund has to be recognised by the courts of other EU/EEA states. This follows from *Mærsk* and the

final decision in *Mærsk* by the Danish Supreme Court in ND 2005 p. 631. These decisions also show that, in the context of the Brussels I/ Lugano regimes, it does not matter whether the law of the state according to which the limitation fund has been established is based on the 1976 or on the 1976/1996 Convention, or on neither one of them. Nor does it matter that there are differences between the law on limitation of the state where the limitation fund has been established and the law of the state where an action in respect of a particular limitable claim is brought against the shipowner. As explained above at 3.2, the establishment of the limitation fund as such does not prevent a claimant from bringing an action for a particular limitable claim against the shipowner before a court of another state. However, it is the duty of such court to recognise the decision establishing the limitation fund, and the consequence of this is that any judgment for the claimant given by this court cannot be independently enforced in that state.

An illustration of the operation of these rules is the decision of the Norwegian Supreme Court in *The General Grot-Rowecki* Rt. 2007 p. 1759. This ship had been involved in a collision in the English Channel that caused the other ship, *The ECE*, to become a wreck. One year later the owner of the latter ship brought an action for damages against the owner of *The General Grot-Rowecki* in the commercial court in Paris, and a month later the court in Paris decided to establish a limitation fund with the court in an amount equivalent to the limit of liability according to French law, which was based on the 1976 Convention. However, a few days before this decision, *The General Grot-Rowecki* had been arrested in a Norwegian port at the request of the owner of *The ECE* in order to obtain security for the alleged claim for damages. At the time the limit of liability applicable according to Norwegian law in this case – where the owner of *The ECE* was not domiciled in a State Party to the 1976 Convention – would have been based on the 1976/1996 Convention, which meant that the limit of liability would be much higher than according to French law.

The owner of *The General Grot-Rowecki* did not request the establishment of a new limitation fund with the Norwegian court.

However, the owner maintained that, according to the Lugano Convention, the Norwegian courts had to recognise the decision of the French court to establish a limitation fund in France and that accordingly the ship should be released from arrest without any necessity for the owner to provide any security for the claim. In particular, it was argued that this followed from the decisions in *Mærsk* of the Court of Justice and of the Danish Supreme Court. On the other hand, the owner of *The ECE* argued that the exception for particular conventions in article 57 of the Lugano Convention also applied to the 1976 Convention and, accordingly, that the Lugano Convention was not applicable.

The Supreme Court first considered whether the request for arrest should be denied according to the provisions of the Norwegian Maritime Code implementing the 1976/1996 Convention article 13 on “bar to other actions”. The court noted that a claimant such as the owner of *The ECE*, which had already raised its claim for damages against the French limitation fund, would ordinarily be barred from requesting arrest in respect of this claim before a Norwegian court. However, the French limitation fund had been established according to the 1976 Convention, and not according to the 1976/1996 Convention, which formed the basis for the Norwegian law on limitation. The 1976 Convention and the 1976/1996 Convention in fact constituted two different regimes for limitation of liability, and the Norwegian provisions on “bar to other actions” at that time generally applied only if the foreign limitation fund had been established according to the 1976/1996 Convention. In some cases, however, these provisions could also be applied *mutatis mutandis* to a limitation fund established according to foreign limitation law based on the 1976 Convention, but this presupposed that the owner of the ship was domiciled in a State Party to the 1976 Convention. This was not the case. Hence, the Norwegian Maritime Code contained no provision according to which the request for arrest had to be denied on the ground that the claimant already had filed his claim for damages in the French limitation fund.

Addressing the question of the effects of the Lugano Convention, the Supreme Court noted that its provisions were given the force of

statutory law in Norway. Accordingly, a judgment given in another State Party to the Lugano Convention (including France) had to be recognised by Norwegian courts, and such a judgment should have the same legal effect in Norway as the judgment actually had in the state where it was given. The Court generally observed – in accordance with its previous decisions – that when interpreting the provisions of the Lugano Convention great weight was to be given to decisions by the Court of Justice relating to the Brussels Convention/Brussels I Regulation. In *Mærsk* the Court of Justice had decided that a decision on the establishment of a limitation fund was to be regarded as a “judgment” in relation to the Brussels Convention article 25. Consequently, the French limitation fund had to be recognised by Norwegian courts as a judgment covered by the Lugano Convention article 26. Furthermore, on the basis of the decision of the Danish Supreme Court in ND 2005 p. 631, the Norwegian Supreme Court held that the Lugano Convention was applicable in this case because the exception in Lugano article 57 did not apply to the 1976 Convention. Consequently, the decision to establish a limitation fund with the French court had to be recognised in Norway, the request to arrest *The General Grot-Rowecki* had to be denied, and the ship was released.

The Supreme Court added that, even if the provisions of the Maritime Code did not prevent the ship from being arrested in Norway, the provisions of the Lugano Convention did so and had to be accorded precedence in relation to the Maritime Code. Norway had pursuant to the Lugano Convention a duty according to public international law to attribute to the French decision the same legal effect in Norway as it had in France.

The Supreme Court also denied a request by the owner of *The ECE* for an arrest in Norway in order to meet a need for mere security for the claim for damages. In view of the security for the claim already provided by the limitation fund in France, there was no need for such additional security. A general condition for arrest in Norway is that there must be a risk that the claim will not be paid unless security is provided by arrest.

The result reached by the Norwegian Supreme Court in *The General*

Grot-Rowicki is based on two conclusions:

- it did not follow from the provisions on “bar to other actions” in the Norwegian Maritime Code that a request to arrest the ship in Norway had to be denied, since the French limitation fund had been established according to the 1976 Convention and not according to the 1976/1996 Convention;
- Norway, being a party to the Lugano Convention, had a duty according to Lugano article 26 to recognise the decision to establish a limitation fund made by the French court as having the same legal effect in Norway as the establishment of the limitation fund had in France, even if French limitation law differed from the provisions on limitation of shipowners' liability in the Norwegian Maritime Code. This meant that a request to arrest the ship in Norway had to be denied.

In the opinion of the Supreme Court this meant, apparently, that there was a conflict between the provisions of the Maritime Code and the provisions of the Lugano Convention which, according to Norway's obligations under international law as a party to the Lugano Convention, should be resolved by giving precedence to the provisions of the Lugano Convention. Another approach would be consider that in this case two different – alternative – grounds could be identified for denying a request to arrest the ship in Norway, one based on substantive Norwegian law relating to limitation of shipowners' liability and the other based on the general rules on recognition and enforcement of foreign judgments that form part of the law of civil procedure.

The provisions of article 13 of the 1976 and 1976/1996 Conventions on “Bar to other actions” are a part of the substantive regimes on limitation of shipowners' liability. In this respect there obviously was a difference between substantive French and Norwegian law. This difference meant that, according to French maritime law, a claimant who had filed his claim in a limitation fund in France would be barred from other actions (including arrest) to enforce his claim; while, according to

Norwegian maritime law, the conditions for applying the provisions “on bar to other actions” were not met in *The General Grot-Rowecki*. The purpose of the Brussels I/Lugano regimes, on the other hand, is to prevent parallel proceedings and irreconcilable judgments in the courts of EU/EEA states. The provisions on *lis pendens* and recognition of judgments contained in these regimes are of particular importance in cases such as *The General Grot-Rowecki* where there is a difference as regards substantive maritime law between the law to be applied respectively by the French and the Norwegian court. Irrespective of such differences, a judgment given by one EU/EEA court has subsequently to be recognised as binding and enforceable by courts in other EU/EEA states. In this context, the Brussels I/Lugano regimes are of general scope determining the effects of legal proceedings and judgments as such in different EU/EEA states. The mere fact that a judgment of a court in another EU/EEA state has to be recognised by a Norwegian court according to the Lugano Convention would by necessity mean that there was no room to take into account the fact that Norwegian substantive law, if applied to the facts of the case, would have led to a different result from that of the foreign judgment.

In *The General Grot-Rowecki* it was in fact possible to identify two alternative and independent grounds for denying the request to arrest the ship. One was the Norwegian Maritime Code. However, as a matter of substantive Norwegian law and, without taking into account any duty for the Norwegian court to recognise the decision made by the French court, the Supreme Court held that there was no rule in the Maritime Code requiring the request to arrest the ship in Norway to be denied. No doubt this is the correct interpretation of the Code’s provisions on “bar to other actions”. However, such provisions cannot be understood also to mean that, conversely, the claimant would actually be entitled to arrest the ship in such a case. According to the Maritime Code § 98, the conditions for the arrest of ships are to be determined according to the general rules on arrest in the Norwegian Act on Civil Procedure chapters 32 and 33, in particular §§ 33-2 and 33-3. Moreover, it follows from § 1-2 of the Act that, in any event, a ship cannot be ar-

rested if this would be inconsistent with the provisions contained in any treaty between Norway and foreign states. The Lugano Convention comes within the scope of this exception, *cf.* also the Act §§ 4-8 and 19-16.

The other ground on which the request to arrest could be denied was the Lugano Convention, as implemented in Norway. The convention's provisions required that the French decision should be recognised in Norway regardless of the hypothetical result of the application of substantive Norwegian law to the case at hand. Accordingly, the Supreme Court quite correctly held that the recognition of the French decision meant that the request to arrest the ship had to be denied in Norway. This part of the decision actually illustrates the regular and unavoidable consequence of rules on the recognition of foreign judgments, but such recognition does not mean that as a matter of law there is a conflict between substantive Norwegian law and the Norwegian provisions on the recognition of foreign judgments. The French court was already (first) seized of the question of limitation of liability at the time when a request for the arrest of the ship was submitted to the Norwegian court, and the decision of the French court establishing the limitation fund had to be recognised by Norwegian courts, even as a matter of Norwegian procedural law, *cf.* the Norwegian Act on Civil Procedure §§ 1-2, 4-8 and 19-16. Had the owner of *The General Grot-Rowecki* for some reason instead requested that a limitation fund be established with the Norwegian court, the court would, according to Lugano article 27, have had to stay the legal proceedings and, eventually, when the French court had decided on its competence, have had to decline jurisdiction, thereby denying the establishment of a limitation fund with the court.

5 The shipowner's forum options

According to article 11 of the 1976 and 1976/1996 Conventions, a limitation fund may be established by the shipowner only in a jurisdiction chosen by a claimant for his action against the shipowner. Thus it is usually difficult for a shipowner to avoid a choice of jurisdiction by the claimant where the law on limitation of liability is unfavourable to the shipowner. The shipowner may sometimes, by directing the ship where to proceed, avoid an unfavourable arrest jurisdiction in an EU/EEA state, e.g., arrest jurisdiction in a 1976/1996 state. Otherwise, there are few defensive options available.

5.1. If the shipowner is domiciled in an EU/EEA state, the jurisdictions generally available for any claimant according to the Brussels I/Lugano regimes are at a minimum the state where the shipowner has his domicile or the state where the casualty took place. However, if the shipowner does not want to have to establish a limitation fund in the state where he is domiciled and, consequently, wants to avoid the claimant bringing his action in that state, he may sometimes succeed in doing so. In a collision case, for instance, where actions against both parties may be brought in the state where the collision took place, the shipowner may without delay bring an action against the potential claimant in that state in order to have the issues relating to collision liability decided by its courts. This can be done by an action asking the court for a declaratory judgment of no liability *vis-à-vis* the other party.

The prevailing view is that it would not be inconsistent with the Brussels I/Lugano regimes to bring an action for a negative declaratory judgment in one of the jurisdictions available for actions against the claimant as defendant, including the state where the claimant is domiciled. It is a precondition for doing so, however, that, according to the law of the state where the action is brought, it is warranted and justified to request a negative declaratory judgment against a potential claimant who has alleged that the shipowner is liable to a claim, but who has not yet brought any action against him, cf. *The Tatry* (C-406/92), *Briggs &*

Rees, Civil Jurisdiction and Judgments, 5th ed. 2009, pp. 626-28, and ND 2006 p. 73 Svea Appellate court (discussed above 3.2). In such an action the court will first have to decide the question whether or not the defendant in the action (the potential claimant) has any claim for damages, as alleged, against the shipowner, *viz.* if and to what extent any liability for the damage caused is attributable to the shipowner. In deciding these questions the court need not address questions relating to the limitation of such liability. For the shipowner, however, time is of the essence. The main purpose of such an action is to ensure that, pursuant to the rules on *lis pendens* of the Brussels I/Lugano regimes, the court of the state where the collision took place shall be first seized of the collision liability question and, accordingly, that the other party shall be prevented from subsequently raising this question in an action in the state where the shipowner is domiciled. Otherwise the shipowner could be sued in his home state and forced to establish a limitation fund there. A successful action for a negative declaratory judgment would consequently mean that the establishment of a limitation fund in the shipowner's home state at any rate would be postponed until there was a final judgment available to be subject to enforcement. Moreover, the resulting delay might in itself strengthen the bargaining power of the shipowner if an out-of-court settlement is to be negotiated.

5.2. Another option for the shipowner is to refrain from establishing any limitation fund in the state where an action is brought by a claimant, and await the time and place of enforcement of any judgment eventually given. A shipowner is entitled, but has no duty, to establish a limitation fund in the jurisdiction of the particular state chosen by a claimant for his action. In fact the shipowner may benefit by postponing the establishment of a limitation fund until he knows the time and place of enforcement of any judgment against him. It may be tempting for a shipowner to adopt this strategy if, for instance, the action relates to a claim which, in the state where the action is brought, will not be treated as a claim subject to limitation of liability on the same footing as other claims arising out of the same casualty. Sometimes such a course of action may also succeed if the shipowner's opponent has not been sufficiently alert.

An illustration is the Danish case *The Uno* ND 2005 p. 484, dealing with a claim for the costs of removing the wreck of *The Uno* from the Kiel Canal. The canal authorities brought their action for damages at a German court since, according to German law, the costs of wreck removal were not an ordinary limitable claim, but subject to a special limit of liability. The shipowner also faced other substantial claims, e.g., for cargo damage resulting from the accident, but these claims were not brought before German courts. In any event, the shipowner chose not to establish a limitation fund with the German court.

The German court issued a judgment for the wreck removal costs in the amount claimed by the canal authority. However, the claim did not exceed the German special limit of liability for wreck removal claims and, consequently, the court was not requested specifically to deal with the question of limitation of the claim, nor did the court do so in its decision. After the German judgment had become final and enforceable, the German claimant sought to have the judgment enforced in Denmark and the shipowner established a limitation fund with the Maritime and Commercial Court in Copenhagen. The shipowner was evidently entitled to establish a limitation fund with the court in respect of other claims arising out of the casualty brought against him in a Danish court. The main question was, however, whether such a decision also had the effect of making even the German claim subject to limitation and only capable of satisfaction when the Danish limitation fund was distributed among the claimants.

This became the principal issue when the German authorities sought to have the judgment enforced in Denmark at the Danish enforcement court designated by the Brussels I Regulation. This court held that the judgment should be recognised and enforced in Denmark although, according to Danish law, a claim for the costs of wreck removal was a limitable claim. Accordingly, the German authorities argued that the Maritime and Commercial Court should exclude the German claim from the limitation fund proceedings. However, this court held that, according to the distinction made in *Mærsk* between an action relating to a particular claim and a limitation fund, the shipowner was entitled to establish a

limitation fund when enforcement of the judgment for a particular claim limitable under Danish law was sought in Denmark (ND 2005 p. 484). The result was that the German claim could only be raised against the limitation fund and would have to be satisfied out of the limitation amount together with other claims against the owner of *The Uno* arising out of the same casualty.

It should be noted that the case was eventually settled by agreement during the subsequent proceedings at the Maritime and Commercial Court relating to the distribution of the limitation fund. Thus the Danish Supreme Court never had an opportunity to consider whether the decision of the Maritime and Commercial Court, that the claim recognised by the German court was subject to limitation in the Danish limitation fund, was consistent with the Brussels I/Lugano regimes on recognition and enforcement of judgments of courts of other EU/EEA states.

With regard to the reasoning of the Danish Maritime and Commercial Court in *The Uno*, it may be argued that, according to the Brussels I/Lugano regimes articles 33 and 38, a German judgment that has become binding and enforceable in Germany should be equally binding and enforceable in other EU/EEA states, including Denmark, and should as such have been recognised in Denmark as enforceable and not subject to further limitation. The preamble to the Brussels I Regulation (paragraph 16) states that mutual trust in the administration of justice in the Community justifies a judgment given in a member state "being recognised automatically". Accordingly it should not have mattered that the German court did not expressly decide or declare that the claim was not subject to limitation according to the international limitation conventions, nor that the owner of *The Uno* made no reservation relating to subsequent limitation of the claim for the costs of wreck removal.

On the other hand, had the German court approved a motion by the canal authorities to the effect that the claim was not subject to limitation, this part of the judgment would at any rate have had to be recognised by the Danish courts, since further limitation of the claim would have meant that a review was required of the substance of the German judg-

ment (Lugano article 36). However, the German authorities never brought such a motion and its absence enabled the Maritime and Commercial Court to point out that the German judgment did not deal with questions relating to limitation of liability and the establishment of a limitation fund. In any event, however, this route would have been closed if the German court had actually applied the special German limit of liability for claims in respect of wreck removal when rendering judgment against the owner of *The Uno*.

In fact, article 7 of the Brussels I/Lugano regimes on the competence of the court to deal with questions of limitation of liability generally covers all forms of limitation of shipowners' liability. Its scope is not limited to any particular form of limitation, such as limitation according to provisions based on the full texts of the 1976 or 1976/1996 Conventions. Accordingly, article 7 also applies to national rules on limitation of shipowners' liability relating to claims in respect of clean-up operations after marine accidents, such as the German rules relevant in *The Uno* or the broader limitation rules in the Norwegian Maritime Code §§ 172a and 175a applicable to claims excluded from limitation according to the limitation conventions. There is no doubt that judgments rendered by a court competent according to the Brussels I/Lugano regimes article 7 are subject to recognition and enforcement according to articles 33 and 38 thereof. In relation to the application of the provisions of the Brussels I/Lugano regimes, it is irrelevant that the result in a particular case would be substantially different according to the law applicable in a state where the rules on *lis pendens* or recognition or enforcement of judgment are invoked.

5.3. Articles 10 to 13 of the 1976 and 1976/1996 Conventions establish how a shipowner may invoke his right to limitation of liability. The establishment of a limitation fund according to article 11 is one of the options but, according to article 10, a shipowner may instead choose to invoke the right to limitation of liability in a particular action in which one or more claims has been brought against him. However, article 10 allows a contracting state to provide that "where an action is brought in its Courts to enforce a claim subject to limitation, a person liable may

only invoke the right to limit liability if a limitation fund has been constituted". In the absence of such legislation, limitation of liability may be invoked by the shipowner without the establishment of a limitation fund. However, a shipowner is not entitled to invoke his right to limit his liability for any particular claims according to article 10 of the 1976 and 1976/1996 Conventions in a case where he himself has brought an action against the claimant or claimants. According to articles 10 and 11, the shipowner may only invoke the right to limitation of liability in an action brought by a claimant.

In cases where article 10 of the 1976 and 1976/1996 Conventions applies the rule is, however, that only the claims covered by the particular action will be taken into account when the right to limitation of liability is invoked. The effect of this is that where there is a judgment concluding that the shipowner is liable, the actual amount to be recovered by the claimant is limited to the applicable limitation amount and, if the action involves more than one claimant, the recovery of each claimant is limited to their proportionate part of the limitation amount. On the other hand, such a judgment is without effect as regards limitation of liability for other claims against the shipowner arising out of the same casualty as the claims included in the action before the court. Consequently, other claimants may enforce their claims by separate actions against the shipowner even if judgments in their favour would mean that the total liability of the shipowner in respect of one and the same casualty would exceed the limit of liability applied by the court in the previous action. The claims covered in an action by the other claimants would be subject to limitation according to the limit of liability applicable in the state where such action was brought, and, if the shipowner wished to do so, he could also establish a limitation fund with the court seized of such action. The claimant in the former action is not a party to these legal proceedings. Nevertheless, according to article 12 paragraphs 2 to 4 of the 1976 and 1976/1996 Conventions, the shipowner himself acquires by subrogation the right to request that the claims which he has paid or will have to pay to the claimant in the former action are taken into account equally with other claims when

the limitation amount applicable in the new action is to be distributed by the court seized. This applies whether or not the shipowner has established a limitation fund with that court.

According to the Brussels I/Lugano regimes article 7, a competent court seized of an action against a shipowner is also competent to decide questions relating to the limitation of the shipowner's liability for the claims covered by the action. Article 7 does not distinguish between cases where the right to limitation of liability is invoked by the establishment of a limitation fund and cases where the shipowner refrains from establishing a limitation fund and instead invokes limitation in relation to the particular claim or claims covered by the action brought against him. Consequently, in the latter case, where the shipowner has invoked limitation of liability according to article 10 of the 1976 and 1976/1996 Conventions in respect of the claims actually covered by the particular action, the court seized of this action is also competent to decide – and seized of – the question of limitation of liability relating to the particular claims included in the action. The consequence of the rules on *lis pendens* of the Brussels I/Lugano regimes is that as soon as limitation of liability has been invoked in respect of the claims brought before the court seized of the action, the question of liability for such claims and limitation thereof cannot be raised in a subsequent action in respect of other claims arising out of the same casualty brought at any court in another EU/EEA state. Also, the court's decision on issues, including limitation of liability, relating to the claims covered by the action at the court first seized, would in other EU/EEA states count as a judgment subject to recognition and enforcement under the Brussels I/Lugano regimes.

On the other hand, the action at the court first seized does not prevent other claimants from enforcing their claims arising out of the same casualty by actions against the shipowner, nor prevent the shipowner from invoking limitation or even establishing a limitation fund in respect of the claims covered by such action or any remaining claims arising out of the same casualty. However, the claims covered by the action at the court first seized, and eventually by its judgment, cannot

be raised against or made subject to further limitation in connection with a limitation fund subsequently established by the shipowner in response to such actions by other claimants. It follows from the rules on *lis pendens*, based on the principle of time priority, that the court first seized of the question of limitation of a shipowner's liability for one or more claims has exclusive competence as regards the limitation of the claims brought before it regardless of whether or not a shipowner has invoked limitation of liability by establishing a limitation fund with the court first seized.

5.4. Another option for the shipowner would be to initiate an action for a negative declaratory judgment for a claim for which he allegedly is liable (above 5.1), and also to include an assertion that, in any event, the liability allocated to the shipowner would be subject to limitation of liability according to the law of the state where he has brought the action. The shipowner might be tempted to do this in cases where such limitation law would be more favourable than the law of a state where he could expect the claimant to bring an action against him. However, this is an option likely to raise quite a few difficult questions, although the shipowner may nevertheless obtain some tactical advantages.

The first question is whether the court where the shipowner has brought his action for a negative declaratory judgment is competent to receive such an action against the potential claimant. If it is, this court may determine whether or not the shipowner has any liability as alleged by the claimant. This means that, according to the Brussels I/Lugano regimes article 7, the court is also competent to decide questions relating to the limitation of any such liability attributed to the shipowner. However, this does not mean that the shipowner is entitled also to a declaratory judgment regarding his right to invoke limitation of such liability.

The provisions of the Brussels I/Lugano regimes – including article 7 thereof – deal solely with matters of jurisdiction. On the other hand, the question whether the shipowner is entitled to invoke limitation of liability *vis-à-vis* a claimant is a question of substantive maritime law as set out in the 1976 and 1976/1996 Conventions. Although the court may

be competent, such matters have to be judged by the court according to the law implementing the provisions of the particular limitation convention in the state where the court is situated. The main substantive question to be decided by the court consequently is whether the shipowner is actually entitled in relation to the claimant to have the question of limitation of any liability decided by the court where the shipowner has brought his action against the claimant. If not, the court shall on substantive grounds refuse to grant the shipowner this part of the relief being sought.

Obviously the shipowner is not entitled to establish a limitation fund with the court where he has chosen to bring his action against a claimant. This would be contrary to article 11 of the 1976 and 1976/1996 Conventions (see above 3.1). As explained above at 5.3, even the right of the shipowner according to article 10 of the 1976 and 1976/1996 Conventions to invoke limitation of liability with respect to a particular claim is limited to cases where an action is brought against him by the claimant. Consequently, the court seized of the action for a negative declaratory judgment may decide issues relating to whether or not the shipowner has any liability in respect of the claim put forward by the claimant. However, the court will on substantive grounds have to conclude that the shipowner is not entitled to invoke limitation of any such liability in the action before the court, and the request that the court by a declaratory judgment should decide whether or not such liability is subject to limitation should accordingly be denied.

Nevertheless, such action by the shipowner may not be without consequences for the claimant. The action by the shipowner for a declaratory judgment to the effect that the shipowner in a particular case has no liability towards the claimant and for a declaratory judgment on the right of the shipowner to limit any liability towards the claimant, has the effect that according to the Brussels I/Lugano regimes article 27, *cf.* article 7, the court where the action is brought is first seized of both these questions. During the period until a final judgment has been rendered in this action, any actions relating to these matters may not be brought by the claimant in another EU/EEA court. This may cause

substantial delay. Moreover, if on the basis of an incorrect interpretation of article 10 the court should render a declaratory judgment as requested by the shipowner, this judgment would be subject to recognition in other EU/EEA states according to the provisions of the Brussels I/Lugano regimes.

The Danish case *Prolific v. Svitzer*, decided by the Maritime and Commercial Court in Copenhagen 2010-11-15, illustrates these problems. The case arose out of a collision in Estonian waters between *The Prolific* – a Danish sailing and training ship – and the Danish tug *The Bestla*. *The Prolific* sustained heavy damage (approx. SEK 12 million) and was towed by the tug to Tallinn. Subsequently the owner of the tug brought an action before the Estonian court for a negative declaratory judgment in respect of the damage sustained by *The Prolific*, asserting also that any liability of *The Bestla* was subject to limitation according to Estonian law, which was based on the 1976 Convention with a limitation amount totalling 83 500 SDR. Shortly thereafter the owner of *The Prolific* arrested *The Bestla* following a petition to a Danish court and the tug was released after a guarantee was provided by its owner. The limitation amount for *The Bestla* according to Danish law, based on the 1976/1996 Convention would be 500 000 SDR.

In the second round of this legal battle, *Prolific* and its insurer initiated an action against *Svitzer*, as the owner of *The Bestla*, before the Maritime and Commercial Court in Copenhagen. The main relief sought was a declaratory judgment that *Svitzer* was fully liable for the damage caused to *The Prolific*, but a subsidiary claim was that *Svitzer* was liable to pay damages in the amount of 500 000 SDR, the limitation amount for *The Bestla* according to Danish law. *Prolific* stated that it would not initiate any action before the courts in Estonia and, consequently, *Svitzer* would not be entitled to establish any limitation fund before an Estonian court, and the Estonian courts could only decide questions relating to the liability for the collision. The question of limitation of liability would accordingly have to be decided according to Danish law.

Svitzer maintained that the court should decline jurisdiction in

respect of Prolific's claims, or alternatively stay the proceedings before the court until a final judgment had been rendered in the Estonian action. Svitzer argued that the Estonian court was first seized of the question of collision liability, and that, according to the Brussels I Regulation article 7, the Estonian court was competent to decide questions relating to Svitzer's right to invoke limitation of liability even if no limitation fund had been established with the court.

The Danish court noted that the Estonian court had concluded that it had competence to deal with the action brought by Svitzer, and that, accordingly, the Estonian court was first seized of questions relating to the extent to which each of the parties was liable for damage arising out of the collision. Consequently, a Danish court was obliged to decline jurisdiction in respect of the claim that Svitzer was fully liable for the damage to *The Prolific* caused by the collision. On the other hand, since the Estonian action did not include issues relating to the amount of damages to be paid by Svitzer, the court decided to stay the Danish proceedings as regards the claims made by Prolific relating to the amount to be recovered by Prolific in the action before the court, including the claim that limitation of liability should take place according to Danish law.

It would seem that the decision of the Maritime and Commercial Court in this case is fully reconcilable with the views expressed above, even if these views also cover issues which the Court did not address in its decision.

The 'Danica White' incident – cause and causation

Do the principles regulating compensation for
occupational injury apply to hijacked sailors
affected by PTSD?

Kristina Siig, Associate Professor
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1 Facts

On 1 June 2007, the *M/V Danica White* was en route from Sharjah in the United Arab Emirates to Mombasa in Kenya with a cargo of drill pipes and cement. At approximately 10.15 hrs the vessel was attacked by Somali pirates, who quickly took control of the vessel. At the time the crew consisted of the master, the mate, the cook and two ordinary seamen. The vessel was taken to the coast of Somalia, entering Somali territorial waters around midnight on 2 June 2007. On 22 August the vessel was released. She then sailed to Djibouti from where the crew was flown home.¹

Following the incident, the Danish Maritime Authority's Division for Investigation of Maritime Accidents issued a Marine Accident Report ('the DMA Report'). The authority found, *inter alia*, that: the master had not received any clear instructions from the shipping company or the charterer regarding the route to be taken off the coast of Somalia; the lookout had been insufficient, given that the vessel was navigating waters where there was a known risk of piracy;² neither the shipping company nor the charterer had provided the master with clear navigational instructions or information about precautions to be taken in that connection;³ and that a proper lookout could have spotted the pirate boats approximately 30 minutes before they reached the vessel. Due to her slow speed, the *Danica White* would have been unable to outsail the pirates in any event, but the crew would have been able to raise the alarm in time and signal to the pirates that they had been spotted.⁴ Finally, the DMA found that the master lacked knowledge of the proper functioning of the vessel's Ships Security Alert System ('SSAS').

¹ Danish Maritime Authority Report DANICA WHITE, Pirate Attack and hijacking on 1 June 2007, Marine Accident Report, Division for Investigation of Maritime Accidents, of 16 November 2007, Case 200711082, downloaded from: <http://www.dma.dk/SiteCollectionDocuments/OKE/Merchant-ships/other-accidents/danicawhiteoversat.pdf> on 8 November 2010.

² The DMA Report, p. 4.

³ The DMA Report, p. 5.

⁴ The DMA Report, p. 5.

The crew suffered no physical harm, but obviously had been subjected to a prolonged and extremely stressful ordeal. For example, the crew had been placed on the wings of the bridge as a human shield when the American naval vessel the *Carter Hall* arrived at the scene.⁵ Subsequently, one crew member was found to be 15% permanently injured due to Post Traumatic Stress Disorder ('PTSD')⁶ and the other crew members spent some time off work.

Under Danish law, only the loss of a breadwinner, permanent injury and permanent loss of the ability to work are covered under the stringent rules of the compulsory Industrial Injuries Security Scheme.⁷ Compensation for temporary loss of income, pain and suffering, and "infringement of integrity"⁸ must be claimed under the general rules of tort law.

Consequently – and probably in the light of the rather damning DMA Report – the trade union 3F initiated proceedings before the City Court of Copenhagen on behalf of the crew. On 26 August 2009 the City Court acquitted the owners of liability, following which 3F appealed to the Eastern Court of Appeal. By a ruling of the 6 October 2010,⁹ the Eastern Court of Appeal confirmed the City Court's decision and – despite acknowledging negligence on the part of the owners – placed the burden of proof of causation on the crew. This ruling will not be appealed so for

⁵ Judgment of the Copenhagen City Court of 26 August 2009 in Case BS 38A-189/200 ('the City Court Ruling') p. 52.

⁶ City Court Judgment, p. 27.

⁷ Promulgation Act 2009-09-07 No. 848 on Industrial Injuries Security.

⁸ Author's translation of the Danish noun 'tort', which signifies that a person has been subjected to humiliating and undignified treatment by the tortfeasor. The noun is generally used in cases involving rape, incest or torture-like acts, and other cases where the tortfeasor has infringed the integrity of another human being by disregarding his or her humanity.

⁹ A resume of the ruling is published in U Zoll. 354 Ø. Here, however reference is made to the original transcript.

now the position under Danish law must be discussed in its light.¹⁰

This article sets out to explore the two rulings in the light of Danish tort law in general and occupational injury law in particular. The focus will be on the Court of Appeal's position on the burden of proof with respect to causation. The article will conclude with a brief look towards the future.

2 The rulings

2.1 The City Court Ruling

The trade union 3F initiated proceedings on behalf of four crew members against the owners,¹¹ who were alleged to be directly liable and also vicariously liable for the actions of the master. The crew claimed compensation for: overtime worked during the period the vessel was hijacked (on the grounds that there was no free time during the hijacking); additional loss of income; and pain and suffering. According to the standardised rules applicable in Denmark to these types of claims, each of the crew were potentially entitled to compensation of around DKK 150,000, plus remuneration for infringement of integrity totalling about DKK 300,000 each.

The City Court found that although the owners themselves had not acted negligently,¹² the master had been negligent in several respects. Firstly, the City Court found that the master had been negligent in only applying one measure to counter the risk of piracy, (*i.e.*, keeping the

¹⁰ Under Danish Law, normally only one appeal is possible. However, under the Danish Code of Procedure § 371, a case heard at first instance by the City Court that subsequently becomes the subject of an appeal before the Court of Appeal may be the subject of a further appeal to the Supreme Court if it concerns an issue of principle. The trade union acting for the sailors has not requested this.

¹¹ Both the actual owners and the investment/holding company behind the owners were sued.

¹² City Court Judgment pp. 51 *et seq.*

vessel more than 200 nautical miles away from the Somali coast). Accordingly, the master had been negligent in failing to ensure that there was a lookout on the bridge. Indeed, the level of lookout should have been stepped up. In this respect, the Court accepted it as a fact that the pirates were able to board the vessel unseen because the master was alone on the bridge and busy with paperwork at the time. Furthermore, the Court found the master had been negligent in failing to ensure that the crew had precise knowledge of the position and operation of the SSAS alarm buttons.¹³

Obviously, there was no doubt that the main *cause* of the incident was the fact that a group of armed Somali pirates with criminal intent had decided to board the vessel. Accordingly, the main question was whether the owners, being vicariously liable for the master's negligence, should be jointly and severally liable with the pirates towards the crew.¹⁴ The City Court bore this in mind when stating: *“Even if it is taken as a fact that [the crew onboard] the ‘Danica White’ ought to have spotted the pirates before they entered the vessel and ought to have been certain that the authorities and other vessels had been informed of the threat, the Court does not find that the plaintiffs have proven how in concreto lookout and vigilance onboard the ‘Danica White’ would have hindered or delayed the attack.”*¹⁵ In this regard the Court focused on the fact that it had not been possible to free the vessel by force, even though the American naval vessel the *Carter Hall* had arrived at the scene more than six hours before the *Danica White* was taken into Somali territorial waters. For these reasons the City Court found that *“the plaintiffs had failed to satisfy the burden of proof that the Master’s negligence had caused the plaintiffs’ losses [in connection with the hijacking]”*.

As the crew had not managed to satisfy the burden of proof regarding causation, their claim was rejected. Indeed, the City Court seems to have required the crew to prove that the hijack would not have taken place – or at least would have been delayed – had the Master not been negligent.

¹³ City Court Ruling p. 51.

¹⁴ City Court Ruling p. 52.

¹⁵ Author’s translation.

2.2 The Court of Appeal Ruling

On appeal, the parties generally repeated their arguments. In its ruling ('the Court of Appeal Ruling'), the Court of Appeal did not find sailing 205 NM off the coast of Somalia to have been negligent.¹⁶ In this regard the Court of Appeal based its finding on the fact that the Maritime Liaison Office (Marlo)¹⁷ and the Danish Ship Owners' Association had recommended¹⁸ that vessels should keep more than 200 NM off the coast of Somalia. Neither the fact that the Marlo Advisory Bulletin had mentioned that pirate attacks had taken place as far as 210 NM out to sea nor the fact that the *Danica White* was – colloquially speaking – “low and slow” could suggest otherwise.

On the other hand, the fact could not be overlooked that the Master had failed to activate the SSAS correctly, and indeed had lacked the knowledge of how to do so. Further, the Court of Appeal found that the Master should have increased the level of lookout and ensured that the crew knew precisely where in the storage room the other SSAS alarm button was situated and how to activate it.

However, despite the inadequacies regarding the lookout and instruction in the alarm system, the Court of Appeal agreed with the City Court that the owners were not liable towards the crew in tort. “*Even with a better lookout the crew onboard the 'Danica White' would only have discovered the pirates, arriving in three fast dinghies, shortly before the attack, and it must according to the evidence given regarding the conditions on June 2007 be taken as a fact that not even a (timely) alarm via the SSAS system could have prevented the hijacking.*”¹⁹ In this regard the Court of Appeal, like the City Court, noted that the American naval vessel had had to refrain from attempting to free the crew due to concerns for the crew's safety.

Regarding the burden of proof in the case, the Court of Appeal

¹⁶ Judgment of the Eastern Court of Appeal 14. Department in case 14.afd. a.s. no. B-2403-09, p. 3.

¹⁷ Marlo Advisory Bulletin, 20 May 2007.

¹⁸ Recommendation of the Danish Ship Owners' Association, 22 May 2007.

¹⁹ Court of Appeal Ruling pp. 3 *et seq.*

found that the failure to observe the precautions mentioned above did not cause a shift in the burden of proof. Accordingly, as the crew had failed either to prove that the hijacking had been *caused* by the failure to have a proper lookout and the failure to inform the crew of the proper operation of the SSAS or that the owners had been negligent during the subsequent events, the owners were acquitted.

In this respect, the Court of Appeal seems to have placed an even heavier burden of proof on the crew. Whereas the City Court would apparently have accepted causation as proven if the crew had been able to prove that the hijacking would have been *delayed* if the Master had not been negligent, the Court of Appeal required the crew to prove that the Master's negligence had *caused* the hijacking.²⁰

3 The burden of proof regarding causation in personal injury cases

3.1 In general

Generally, the burden of proof under Danish tort law is on the injured party: the injured party has to prove that it has suffered a loss that was caused by the negligence of the tortfeasor (unless, *e.g.*, the tortfeasor is liable under stricter rules) and that the loss is not too remote.²¹ As a starting point this is the position for occupational injuries, as well as for personal injuries in general. However, this is just a starting point. For example, the burden of proof may shift in the light of evidence presented, and in certain situations statute or case law provides for the burden of proof to be reversed or reduced. This is the case, *e.g.*, for medical ne-

²⁰ Court of Appeal Ruling, p. 4.

²¹ Eyben/Isager; Lærebog i erstatningsret, 6th ed., Copenhagen 2007, p. 97 *et seq.* and 256 *et seq.*

gligence claims²² and for occupational injury claims covered by the Industrial Injury Security Act.²³ Even so, there is no general rule under Danish law allowing a reduction or reversal of the burden of proof in personal injury claims.²⁴

3.2 The burden of proof regarding causation – the effect of breaches of regulatory requirements

The principle that the burden of proof lies on the injured party applies not only to negligence and losses, but also to causation. For example, in U 2002.1953 Ø, the Eastern Court of Appeal held that “*special circumstances*” were required for it to depart from the starting point that the injured party had to prove causation. In this case a teacher claimed that certain complaints (a skin complaint and a mucosal ailment) were due to the indoor environment at the school where she worked. Consequently the case concerned an alleged occupational injury (although one not covered by the Industrial Injuries Security Act), but despite this the Court of Appeal saw no reason to reverse the burden of proof.²⁵

So the question is what circumstances may be considered sufficiently “special” to allow the burden of proof to be reversed or reduced?

As already mentioned, in the *Danica White* case, the Court of Appeal accepted that the lookout on the *Danica White* had not complied with Regulation No. 1758 of 22 December 2006 on watch-keeping. The Court further accepted that the Master most probably had not used the SSAS correctly and that the crew had also not been sufficiently in-

²² See, e.g., the reduced burden of proof in medical negligence cases (Law No. 547 of 24 June 2005 on complaints and liability within the medical sector, § 20); see further Eyben/Isager; Lærebog i erstatningsret, 6th ed., Copenhagen 2007, p. 350 *et seq.* and Askjær/Hjortnæs/Jacobsen; Erstatning inden for sundhedsvæsenet, Copenhagen 2008, p. 73 *et seq.*

²³ Law No. 422 of 10 June 2003 on Industrial Injury Security.

²⁴ Please note that those occupational injuries that are not covered by the above-mentioned regulation are little discussed in legal theory in Denmark. The reader will consequently have to excuse the very limited number of footnotes.

²⁵ The plaintiff proved that the building was very humid, but did not prove that the school had not followed official instructions in this respect, see the case at p. 1962.

structed in how to use the system. In other words, the Court of Appeal accepted – in accordance with the DMA Report – that aspects of the handling of the situation had been negligent. However, the Court of Appeal found that there was no causative link between the negligence and the attack. In this respect, the Court applied a standard burden of proof as, according to the Court, the failure to observe the above-mentioned precautions did not cause a shift in the burden of proof.

This is somewhat remarkable, as failure to adhere to regulatory requirements has been one of the situations that normally reverses the burden of proof in cases concerning personal and/or occupational injuries.

For a violation of regulatory requirements to reverse the burden of proof, the rule concerned must be intended to prevent the injury or damage which actually occurred.²⁶ In other words, the rule must be intended to regulate a behaviour or condition relevant to the injury (the provision's *Schutzzweck*).²⁷ It seems quite clear, at least to this author, that the purpose of a lookout is not only to maintain the ship's safety in a navigational sense, but also to maintain the ship's security (see, e.g., the direct reference to the STCW Convention made in Regulation No. 1758 of 22 December 2006 on watch-keeping § 5). Also, the obligation on the Master to make sure that the crew knew where and how to operate the other SSAS alarm must be said to be intended directly to ensure that the alarm would be sounded and that help from relevant sources would be requested immediately. Consequently, one must conclude that the Master's negligence and breaches of regulatory requirements were directly relevant to the avoidance (amongst other things) of being attacked by pirates, and thus to the crew's injuries.

²⁶ See U 1997.648 Eastern Court of Appeal, "Rødovre Centrum". A 10-year-old girl had lost her arm when it became trapped between the floor and the wall in an open glass lift in a shopping mall. The distance between the floor and the wall in the lift ranged between 14 and 19 mm, and was thus considerably larger than the permitted distance of 10 mm. The manufacturer of the lift had the burden of proving that this discrepancy had not contributed to the accident. Having failed to do so, it was found liable towards the child.

²⁷ Eyben/Isager; Lærebog i erstatningsret, 6th ed., Copenhagen 2007, p. 72 *et seq.*

Accordingly, in this author's view, the reason for the refusal to reverse the burden of proof in e.g. the *Danica White* case cannot be found in lack of *Schutzzweck*, but must be sought elsewhere.

The following discussion analyses the leading Danish cases on occupational injuries connected with a breach of regulatory requirements in order to pinpoint, firstly, when the burden of proof is reversed, and, secondly, what standard of proof is required. The reader will have to excuse the rather thorough descriptions of the cases, as the facts are needed for the final analysis. These cases are quite rare and seem to come before the Danish Courts approximately every 10 years.

3.3 The leading cases on proof of causation in occupational injury cases involving breaches of regulatory requirements

The first case that lends itself to analysis is U 1974.1014 H, "*the scaffolding case*". An employee, E, was working with a colleague on a scaffolding platform 5.6 m above a concrete floor when the scaffolding collapsed. He directed a claim for occupational injuries against his employer, J. According to the Working Environment Service's report, the scaffolding had not complied with the applicable regulation. However, as the discrepancies were minimal, the Working Environment Service would probably have approved the scaffolding had it been consulted. Expert witnesses found that a hidden weakness (a so-called folding line) in the structure of the boards – rather than the failure to comply with the regulation as such – had caused the collapse. Such a folding line was in principle visible to the naked eye, but would, according to the expert witnesses, not have been discovered during a normal site inspection. The City Court of Silkeborg found for E based on a pure allocation of risk, whereas the Western Court of Appeal in a 2:1 decision found for J, based on the fact that the hidden defect could not be seen during a normal site inspection and that the failure to adhere to the regulation was considered insignificant. On appeal to the Supreme Court, two judges held in favour of the ruling of the Western

Court of Appeal, but the majority of three found that, in the circumstances, where the board in question had not satisfied the requirements as to strength that could be demanded bearing in mind the particular risks encountered when working on scaffolding, J was liable for its employee's injuries. In this respect the Court took into account the *uncertainty as to whether or not the collapse would have occurred, had the scaffolding been erected in accordance with the regulation*.

Regarding the folding line in the platform, rather than evaluating negligence, the Supreme Court applied an allocation of risk or, one might say, a strict liability. Indeed, this is one of the very few cases under Danish law where it may be argued that strict liability was imposed in the absence of any statutory basis for doing so.²⁸ However, the more interesting issue in relation to the *Danica White* case is the proof of causation required by the Court. The Court was left uncertain as to whether or not the collapse would have occurred if the scaffolding had been erected correctly. This establishment of a mere *uncertainty* regarding possible causation sufficed for E. Since it had already been decided that the employer had to bear the risk of the folding line, there was no way in which the employer could have been acquitted. Even if J had managed to prove that it was *certain* that the scaffolding would have collapsed *i.e.*, that the board would have snapped, even if the regulation had been complied with, it would still have borne the risk of the folding line in the wood.

The very lenient approach to the proof of causation in U 1974.1014 H has been followed by the Supreme Court in later cases, see firstly U 1982.50 H, "*the circular saw case*":

About 10 days after employee E had been hired, he was put to work at a circular saw cutting steel pipes. As he tried to remove some of the pipes from under the saw his sleeve got caught and his arm was drawn against the rotating blade, causing the loss of his right arm below the elbow. The Working Environment Service found that although the saw did not have the required safety guard, given the way in which E had operated the machine, even a correctly positioned guard would not

²⁸ See further on this issue *Eyben/Isager*, p. 140 f and *Trolle* in U 1975.B 101f.

have prevented the accident. The Court of Appeal noted that the accident was caused by E's own negligence: he should have switched off the saw before removing the pipes instead of inserting his arm below a rotating saw blade. As a safety guard would not have prevented this accident, and as E's employer was found to have given him sufficient instructions, the employer was acquitted of liability.

E appealed to the Supreme Court. The Court found that the failure to equip the saw with the safety guard made the saw "considerably more dangerous" to operate than it would have been otherwise. One could not disregard the fact that the accident might have been avoided if a guard had been fitted. It could also not be ruled out that more extensive instruction in the use of the saw or more thorough supervision of E would have prevented the accident. For these reasons, the Court found in favour of E. Furthermore, the Court found that E's negligence was not so severe that it should cause his claim to be reduced.

Regarding the issue of contributory negligence, trying to remove anything at all from under a rotating saw blade may reasonably be characterised as negligent. And the Court of Appeal's reasoning that a safety guard would not have prevented the accident in the face of such negligence seems reasonable. However, one must bear in mind the Supreme Court's finding that the saw without the safety guard was "*considerably more dangerous*" than it should have been. The disregarding of E's contributory negligence should probably be seen in this light.

Considering the burden of proof, the expressions used by the Supreme Court, *i.e.*, that causation "*could not be ruled out*", or that one could not disregard that certain alternative measures "*might [have] avoided the accident*" places a burden upon the employer to rule out almost any alternative hypothetical turn of events. While it is obviously possible for the employer to come up with some kind of hypothetical scenario whereby the damage would have occurred anyway, in practice such a burden of proof is almost impossible to satisfy. However, this standard, set by the Supreme Court, seems to be the applicable one, and was also applied 10 years later in U 1992.199/2 H, "*the hydraulic lift*

case”:

Employee E was working in a hydraulic lift at the Lindø shipyard while sandblasting a hull. The lift was operated using a control panel inside the lift. E was found crushed to death between the vessel’s frame and the edge of the lift. His wife and children sued for loss of the family breadwinner.

No technical faults were found and the most likely cause of the accident was thought to be either that sand from the sandblasting had obscured the symbols on the control panel so that E had pressed the wrong button by mistake or that a cable had touched the control panel and caused the lift to rise unexpectedly. After the accident the control panel was shielded off and the lift was equipped with a 60 cm railing connected to a dead man’s switch in order to prevent a similar accident occurring in the future. In general, however, the Working Environment Service found the safety procedures and precautions at the yard to be satisfactory.

The lift had not malfunctioned and E had received thorough instructions in the operation of the lift. Neither the Working Environment Service nor the safety representative at the yard had requested further safety measures for sandblasting operations. Taking this into account, the Court of Appeal found that the shipyard was not responsible for the accident.

On appeal to the Supreme Court, several public guidelines from, *inter alia*, the Working Environment Service were produced. According to the guidelines, control panels in, *e.g.*, lifts should be configured and positioned to prevent them from being manipulated unintentionally. An expert witness stated that such manipulation could have happened if the dust cover was not in place. As the dust cover was only intended to shield the control panel from sand and other dirt rather than to function as a safety measure, the Supreme Court found that the yard should have taken measures to ensure that the control panel was protected in another way. Thus, the Supreme Court accepted that the yard had been negligent. The next question was the standard of proof required concerning causation. The Court stated: “... *the possibility that an unin-*

tentional manipulation of the control panel caused or was a part of the cause of the accident cannot be ruled out.” Consequently, the Court held the yard liable for E’s relatives’ loss of breadwinner.

Ruling out the mere possibility of (partial) causation seems to be the burden that has to be satisfied by the defendant. This was accepted as the position under Danish law by the Western Court of Appeal in FED 2001.2386. Employee E had, with his employer’s permission, used the carpenter’s workshop where he was employed for private use outside working hours, during which time the rules on occupational injuries did not apply. E was injured when using one of the machines. The correct way to operate the machine was stated in the Working Environment Service’s standards. However, the master carpenter himself did not operate the machine in this way, nor had he instructed E to do so. *“Under these conditions one cannot disregard that the accident might have been avoided, if E had been instructed [in how to use the machine correctly]”*. Consequently, the burden of proof for causation had been satisfied and the Court did not consider the damage so remote as not to warrant liability. Accordingly, the master carpenter was found to be liable under the general rules of tort, *“even though the rules on occupational injuries do not apply.”*

3.4 Summing up the existing leading cases

In all the above cases, the Supreme Court found for the injured party. Furthermore, there seems to be a firm rule that the question asked in order to evaluate whether the defendant has satisfied its burden of proof is *whether it is possible to rule out the possibility* that the breach of regulatory requirements *might have contributed* to the accident. As already mentioned, this burden of proof is extremely difficult to satisfy. Indeed, one may ask whether the Supreme Court in these cases has applied an extremely heavy burden of proof or indeed has imposed a type of latent strict liability upon employers in cases where the relevant regulatory requirements have not been adhered to. If the latter is true, the ruling of the Court of Appeal in the *Danica White* case is hard to explain.

Delving slightly deeper into the above cases, it becomes apparent that the Courts of Appeal (at least until the ruling in FED 2001.2386 referred to immediately above) have been more reluctant to impose liability. In particular, the Courts of Appeal seem to have been more reluctant to find both a basis for liability (through either negligence or pure allocation of risk)²⁹ and also proof of causation.³⁰ On that basis, one might well ask whether tactically the trade union in the *Danica White* case would have been well advised to have asked for leave to appeal to the Supreme Court. However, the rulings of the Courts of Appeal are very much tied to the facts of the given cases, so it is impossible to prove any real trend. Instead, it is worth considering whether there are particular factors that might have led the Eastern Court of Appeal to distinguish the situation in the *Danica White* case from the earlier cases.

4 The Court of Appeal ruling in the *Danica White* case seen in the light of existing case law

Superficially, the facts of the *Danica White* case seem to follow precisely the criteria that in the above cases led not only a shift in the burden of proof, but also to a requirement for the tortfeasor to disprove the mere possibility of partial causation. So why in this case did the Courts reach a different result? In this author's view, there are two possible explanations. Firstly, the Courts seem to have accepted that in this case, even if the regulations had been complied with, there would have been no material alteration in the course of events. The slowness of the *Danica White* meant that increasing the level of lookout would not have helped. In addition the American naval vessel was too far away and in any event had to refrain from engaging in the situation out of concern for the

²⁹ See U 1974.1014 H and U 1992.199/2H.

³⁰ See U 1974.1014 H, U 1982.50 H and U 1992.199/2H.

crew's safety, so even if the alarm had been sounded correctly, the outcome would still have been the same. However, there is a second feature of the facts in the *Danica White* case that distinguishes it from the cases mentioned above. In the *Danica White* case, the main cause of the crew's injuries was the criminal intent of a third party.³¹ By contrast, in the above cases, there was either only one possible cause of the injury, for which the employer bore the risk (as in U 1974. 1014 H, "*the scaffolding case*"), or the possible causes were either the negligence of the employer or the possible contributory negligence of the injured party (as in U 1982. 50H, "*the circular saw case*", and U 1992.199/2H, "*the hydraulic lift case*"). In both the latter cases contributory negligence was either found not to be proven (U 1992.199/2H) or was considered to be negligible (U 1982.50H). Accordingly, the breach of regulatory requirements was related to the real cause of the injuries.

In situations where the only possible cause of an injury is either the contributory negligence of the injured employee or the negligence of his employer, and the employer's negligence consisted of a breach of regulatory requirements, the purpose of which was to protect the employee against the precise injury that occurred, it is reasonable to presume that the injury was caused by the employer's negligence. It is also reasonable to make the burden of proving non-liability difficult to satisfy.

In this author's view, however, in situations where the real cause of an injury is a criminal offence committed by a third party, it is no longer obvious that the employer should bear the burden of proof with regard to causation. Where there is an alternative, proven, main cause of the injury, which in any realistic terms is unrelated to the breach of regulatory requirements, the rationale for reversing the burden of proof with regard to causation disappears. In other words, the burden is on the plaintiff. In such a situation the above-mentioned cases simply do not provide relevant precedents.

³¹ City Court Judgment, p. 53.

5 Potential effect of the *Danica White* precedent

So what might be the result if a Danish Court were (regrettably) to be faced once again with a case involving a pirate attack in the Gulf of Aden or Indian Ocean? Obviously, the *Danica White* case would have to be considered, but counsel for the owners should probably not expect the case to be followed automatically.

Firstly, *Danica White* was hijacked in 2007. At that time there was very little focus on this type of piracy, and Somali pirates had not yet really implemented their new *modus operandi*. Secondly, the Master adhered to the main safety measure recommended at the time, namely to sail outside the 200 NM line. Further, the recommendations generally in place were not aimed at this type of piracy, being more focused on robbery at sea in East Asia and South America than on the type of hijackings occurring presently.³² In keeping with this focus, the main recommendations in force at the time concerned avoiding certain waters (IMO Guidelines para. 13), keeping a good lookout (IMO Guidelines para. 10), and not carrying too much cash in the ship's safe (IMO Guidelines para. 4).

If we suppose for a moment that the same circumstances were to arise in 2011 – *i.e.*, a hijacking of a “low and slow” vessel, with no lookout, no specific route planning and a crew that is clearly uncertain or even completely ignorant of what is expected of it in the event of a

³² See MSC/Circ.623/Rev.3, IMO guidelines: Annex to PIRACY AND ARMED ROBBERY AGAINST SHIPS, Guidance to shipowners and ship operators, shipmasters and crews on preventing and suppressing acts of piracy and armed robbery against ships, of 29 May 2002 (“the IMO Guidelines”), para. 3: “The pirates/robbers objective: 3. *In addition to hijacking of ships, and the theft of cargo, the main targets of the South East Asian attacker appear to be cash in the ship's safe, crew possessions and any portable ship's equipment, even including rolls of rope. In South America some piracy and armed robbery attacks are drug related. When there has been evidence of tampering with containers, it has been suggested that the raiders may initially have gained access when the ship was berthed in port and then gone over the side, which what they could carry. Thorough checking of the ships' compartments and securing before leaving ports is therefore recommended.*”

pirate attack – this author considers it highly likely that the Danish Courts would evaluate the issue differently. Considering the content of the current guidelines from the IMO³³, which have been incorporated into and elaborated on in companies' and organisations' own best management practices, simply sailing more than 200 NM off the coast will not suffice as a countermeasure. Also, even though the pirates' criminal intent will still be the main cause of the crew's suffering and loss, the increased knowledge of the risk of piracy and possible countermeasures will have changed the Courts' perception of the gravity of the negligence displayed by the Master in, e.g., neglecting to appoint a lookout. Consequently, should such a situation arise, in this author's view the older precedents should be applied with the result and that this would be precisely one of those "*special circumstances*"³⁴ where the burden of proof should be on the owner to prove that the negligence had no effect whatsoever on the course of events.

³³ The MSC.1/Circ.1334 of 23 June 2009, ("the 2009 IMO Guidelines") may be downloaded from IMO's website at:
http://www5.imo.org/SharePoint/blastDataHelper.asp/data_id%3D25885/1334.pdf
(page visited 14 December 2010).

³⁴ U 2002.1953 Ø, referred to above in point 3.2.

Compensation for interference
with contractual rights
– liability in tort

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1 Introduction

The possible liability in tort of a party who knowingly interferes with another party's contractual relations is interesting both theoretically and from a practical point of view. Suppose that there is a contract between A and B, but a third party C, who is not in a contractual relationship with either A or B, first induces A to breach his contract with B¹ and then concludes a substitute contract with A. Can B claim compensation from C for economic losses he suffers as a result of C's interference? In view of the principle of free competition² and the general principle that a contract cannot confer rights or impose obligations on anyone except the parties to it (*privity of contract*),³ the answer to this question would seem to be negative: C has no obligation to compensate B for any losses. But is this also the proper starting point when examining the question in the light of *tort* law?⁴ The conduct of the third party, C, causes B to suffer loss. What significance, if any, does the nature of C's interference (*e.g.*, inducing, persuading, encouraging, advising or participating in the breach of the contract) have when considering C's potential liability? And is the nature of the actual circumstances relevant? For instance, what if there is an existing contractual relationship between B and C? Or if the purpose of the original contract between A and B is the transfer of a specific (or comparable) object?

This article will examine the question of liability in the light of Finnish tort law and will also make some comparisons with Swedish

¹ This article will focus only on situations where A wrongfully breaches his valid contract with B.

² Market actors have the right to compete for contracts provided that their conduct is legal and conforms with good practice. See *e.g.*, Petri Kuoppamäki, Markkinavoiman sääntely EY:n ja Suomen kilpailuoikeudessa (Helsinki 2003), 118.

³ See *e.g.*, Matti Rudanko, "Sopimussuhteiden häiritseminen", *Defensor Legis* (2009), 540.

⁴ It should be noted that while the principle of *privity of contract* essentially has relevance within the sphere of contract law, the present article discusses liability in tort.

tort law.⁵ In Finland, there is no consistent and firm court practice regarding the issues mentioned above, which are also scarcely discussed in Finnish legal literature (with the exception of some recent commentaries).⁶ There seems to be no general theory or principle dealing with issues concerning compensation in such cases.⁷ Instead we find ourselves in a “grey” area of the law where we need to consider the rules and principles regulating contractual obligations, property law

⁵ Finnish law is a civil law system influenced by the Roman and German legal traditions, among others. It also shares features with the other legal systems often referred to as the Nordic legal family (Denmark, Finland, Iceland, Norway and Sweden). Finnish law has been, and continues to be, influenced in particular by Swedish law. Finland formed a part of Sweden for approximately 600 years and Swedish laws remained in force in Finland after Swedish rule ended in 1809. Swedish contract and tort law in particular continued to have a strong influence on Finnish law. The Finnish Tort Act (412/1974) was largely influenced by the Swedish Tort Act of 1972. Consequently, the meaning and use of legally relevant sources of law (legislation, case law, *travaux préparatoires*, legal doctrine, etc.) are very similar in Finland and Sweden. Cf. *Peter Wetterstein*, *Redarens miljökadeansvar* (Åbo: Åbo Akademi förlag 2004), 19-21 with references. In addition, the use of comparative law to provide guidance for decisions in areas not previously dealt with in case law is also significant in both countries. For instance, the Swedish Supreme Court decision *NJA 2005 p. 608* (12.9.2005 T 4136-03), see *infra*, II.2, mentions Finnish legal doctrine (*Hans Saxén*, *Skadeståndsrätt*, Åbo Akademi 1975).

⁶ See, e.g., *Mia Hoffrén*, “Vahingonkorvausvastuu sopimussuhteen häirinnästä – vertaileva katsaus”, *Lakimies* (2006), 990-991, 1003. But in 2006 *Marcus Norrgård* published an interesting and rather extensive study on improper interference with commercial contractual rights, *Avtalsingrepp. Om otillbörliga ingripanden i kommersiella avtalsförhållanden* (Helsinki: Swedish School of Economics and Business Administration, Research Reports 61, 2006), which naturally is also of interest for the present discussion.

⁷ However, there seems to be agreement in the legal literature that so-called *collusive* (“kollusiivinen”) interference with contractual rights could lead to an obligation to pay compensation. That is, if the common intent of A and the third party C is to deprive B of his contractual rights, C could be liable, in addition to A, to pay compensation to B. See *Hoffrén* (2006), 990, 1002-1003. But see also *Norrgård* (2006), 8-9, who points out that the focus of the discussion has traditionally been more on the intent of A and C to cause damage to B and the legal validity of the subsequent contract (between A and C), than on the actual infringement of the contract between A and B and the legal consequences for C. Furthermore, the discussion has mainly focused on issues within the sphere of property law.

and tort law.⁸ Furthermore, as economic loss caused by a third party's interference with contractual rights is typically so-called *pure economic loss* (that is, economic loss unconnected with personal injury or property damage),⁹ some criteria must be satisfied for such loss to be compensated.

Finnish law, like many other common or civil law legal systems,¹⁰ has traditionally been reluctant to award compensation for pure economic loss. Such loss may typically be caused, for instance, by the negligence of accountants, consultants, attorneys, engineers, surveyors or directors of corporations. An infringement of the rules protecting intellectual property rights may also result in pure economic loss. Various examples can also be found in the context of environmental impairment.¹¹

The restrictive attitude towards compensation for pure economic

⁸ An interesting overview of the interaction between the law of obligations and property law when discussing the legal position of a third party to a contract is presented by *Eva Tammi-Salminen*, "Sopimus ja kolmas – velvoite- ja esineoikeutta yhdistävä vai erottava teema?", *Sopimus, vastuu, velvoite. Juhlajulkaisu Ari Saarnilehto 1947 – 21/11 – 2007* (Turku: Turun yliopisto, Oikeustieteellinen tiedekunta, 2007), 369-392.

⁹ A clear conceptual distinction is made in relation to *consequential loss*, that is, economic loss in connection with personal injury or property damage. This type of loss occurs, for instance, when an injured person loses income or a property owner loses profit because he is not able to use the damaged property. On the notion of *pure economic loss* in Finnish law, see, e.g., Wetterstein (2004), 129-135, *Lena Sisula-Tulokas*, "Rena ekonomiska skador i skuggan av sakskadorn", *Tidskrift utgiven av Juridiska Föreningen i Finland* (2007), 415-430, and *Björn Sandvik*, "Puhdas varallisuusvahinko – mikä se on? Puhtaan varallisuusvahingon kahdesta käsitetulkinnasta", *Defensor Legis* (2010), 25-36 with references.

¹⁰ See, e.g., *Peter Wetterstein*, "A Proprietary or Possessory Interest: A *Conditio Sine Qua Non* for Claiming Damages for Environmental Impairment?", in Peter Wetterstein (ed.), *Harm to the Environment: The Right to Compensation and the Assessment of Damages* (Oxford: Oxford University Press 1997), 33-36.

¹¹ See Wetterstein (1997), 37-46.

loss occurring outside *contractual relationships*¹² is manifested in the Finnish Tort Act (412/1974).¹³ Such compensation is in general awarded only to a limited extent, and the Act provides that compensation for pure economic loss shall be paid only if it is caused by a criminal act, by an administrative body in the exercise of its authority or where there is some other *particularly weighty reason* for awarding compensation (Chapter 5, Section 1).¹⁴ There are also some special laws with provisions on compensating pure economic loss.¹⁵

We will not deal here with economic loss caused either by criminal conduct or by the exercise of administrative authority. Instead we will

¹² In the context of contractual relations, pure economic losses are generally compensated. The distinction between obligations based on contract and non-contractual obligations is, however, not entirely clear. In certain circumstances the Supreme Court has extended principles governing contractual liability also to persons who have not directly entered into the contract. See e.g., the Supreme Court decisions 1992:89, 1999:19, 2005:14 and 2009:45. Cf. also the decision 1999:32, where the Ministry of Commerce and Industry had given wrongful information about the financial position of a shipyard that was later declared bankrupt. The state had to pay compensation to the buyer of a ship who had lost money through relying on the information. The case is commented on by, e.g., *Heikki Halila* in *Lakimies* (1999), 725-751. However, in cases 2008:31 and 2009:92, the Supreme Court seems to have applied strictly the “traditional” dividing line between contractual and non-contractual liability. See the comment by *Olli Norros* in *Lakimies* (2010), 432-444.

¹³ The Tort Act is the general law regulating non-contractual liability for damage or injury. It does not cover liability governed by *special* rules of law (Chapter 1, Section 1). In the Tort Act, liability is based on fault and includes vicarious liability, such as employer’s liability (Chapter 2, Section 1 and Chapter 3). Further requirements for liability are the presence of damage suffered by the victim and a causative link between the tortfeasor’s wrongful conduct and the damage.

¹⁴ Before the Tort Act of 1974 came into force there was no general provision on pure economic loss in Finnish tort law. The legislative history of Chapter 5, Section 1 of the Tort Act shows, however, that there was no intention to make significant changes to the situation as it existed before the Act came into force. The main function of the new provision was to reflect existing court practice and to allow it to continue in special situations where damage was not a consequence of an act of public authorities or a criminal act. However, the meaning of the criteria *a particularly weighty reason* was not specified. For the legislative history of the provision, see *Matti Ylöstalo*, “Vahingonkorvauslain 5 luvun 1 §n tulkintaa”, *Lakimies* (1975), 239-243.

¹⁵ See *Peter Wetterstein*, “Compensation for Pure Economic Loss in Finnish Tort Law”, in Peter Wahlgren (ed.), *Tort Liability and Insurance. Scandinavian Studies in Law. Volume 41* (Stockholm: Stockholm Institute for Scandinavian Law 2001), 574-580, and also *Rudanko* (2009), 545.

focus on the criterion of a *particularly weighty reason*. Since the meaning of this criterion is not defined in the Tort Act,¹⁶ how has this been done in court practice and the legal literature?¹⁷ Is it possible to find any guidelines for answering the questions referred to above? Is it possible, by applying the notion a *particularly weighty reason*, to find and elaborate criteria for distinguishing between cases where compensation for interference with contractual rights should be paid and those where compensation should be denied?¹⁸ What relevance, if any, can be attached in this context to unfair business practices within the meaning of the Unfair Business Practices Act of 1978 (1061/1978)¹⁹ and to general obligations of good faith and loyalty in business relations?

This study is divided into three main parts. Firstly we examine Finnish court practice regarding the notion of a *particularly weighty reason* and make some comparisons with Swedish case law. Is it possible to find any guidelines to help us answer questions concerning compensation for interference with contractual rights? Secondly we present and summarise views expressed in the legal literature. The final part

¹⁶ See, *supra*, fn. 14. The wording of the provision indicates, however, that compensation for pure economic loss should not be awarded too lightly. The aim of the Tort Act is primarily to compensate personal injury and property damage. Cf. also *Mika Hemmo*, *Vahingonkorvauksen oppikirja* (Helsinki: WSOY Lakitieto 2002), 118-121.

¹⁷ Some guidelines have been suggested in the legal literature: The degree of fault or negligence on the part of the person/activity causing the economic loss is relevant. For instance, intentional behaviour (such as acts contrary to good practice) or gross negligence may trigger the obligation to compensate pure economic loss. Furthermore, the scope of the loss, its implications for the person suffering damage, and that person's possibilities for protecting himself against such loss may be of relevance. Analogies should also be made with situations where pure economic loss is compensated without the application of the prerequisites mentioned in Chapter 5, Section 1, for instance, under contract law, company law, and intellectual property law. See Wetterstein (2001), 573 with references. See also *Lena Sisula-Tulokas*, "Goda seder och ersättning för rena ekonomiska skador", *Tidskrift, utgiven av Juridiska Föreningen i Finland* (2009), 553-556.

¹⁸ The issues are examined from the perspective of *de sententia ferenda*, that is, the primary aim is not to suggest amendments to the current legislation, but to study and recommend possible solutions within the existing – albeit unclear – legal framework.

¹⁹ The aim of this Act is to protect businessmen from the unfair conduct of other businessmen. A person engaged in commerce should not affect the position of another businessman by conduct that is commercially or socially unacceptable. See Norrgård (2006), 37-40.

discusses possible answers to the questions posed in this introduction and presents some conclusions.

2 Court practice regarding a particularly weighty reason

2.1 Finnish case law

During the drafting of the Finnish Tort Act, importance was attached to making compensation available – albeit exceptionally – for pure economic loss, including loss caused other than by a criminal act or by an administrative body in the exercise of its authority. It was also felt that some room should be left for the development of this branch of law through court practice.²⁰

So far, however, not only has there been no case law dealing explicitly with compensation for interference with contractual rights, but the rather “open” wording *a particularly weighty reason* has proved problematic, as it is no easy task to find criteria for its interpretation. Regarding the practice of the Supreme Court, reference can be made to the following decisions:

1983 II 187: By placing advertisements in newspapers, a labour organisation had coordinated a boycott of an employer who had dismissed an employee. The purpose of the boycott was to put pressure on the employer. By intervening in the dispute between the employer and the employee, who had resort to legal remedies, the organisation caused economic loss to the employer. The Supreme Court found that the organisation had not acted in accordance with good practice. However, because the employer had also acted improperly, there was no particularly weighty reason to award compensation for pure economic loss.

The Supreme Court thus considered that the conduct of the labour

²⁰ See, *supra*, fn. 14.

organisation had contravened good practice. However, since the Court rejected the claim because of the employer's improper conduct, it is difficult to form any opinion about the Supreme Court's understanding of the criterion a *particularly weighty reason*.²¹ Nevertheless, the case indicates that conduct contrary to *good practice* could fulfil that requirement.²²

1991:79: An editor had written a newspaper article, resembling a product test, in which he and another person expressed their views on baby carriages from five different manufacturers. The article gave readers the impression that impartial tests had been carried out and also contained false information about one of the imported baby carriages. The article featured prominently in a childcare-related context in a widely distributed newspaper. The Supreme Court considered that there was a particularly weighty reason to oblige the editor and the editor-in-chief of the newspaper, both of whom had acted contrary to good journalistic practice, to compensate the pure economic loss suffered by the importer of the baby carriage.

The Court held that the violation of good journalistic practice, taking into account such freedoms as freedom of opinion, amounted to such negligent conduct that compensation should be awarded because the damage was clearly foreseeable. Here again the negligent conduct was the violation of *good practice*, which was done in such an improper and misleading manner that compensation was awarded.

1992:44: An attorney negligently caused economic loss to heirs to an

²¹ Cf. also Norrgård (2006), 161.

²² Cf. *1990:26*: A person had taken out an insurance policy for a market garden. The insurer refused to pay compensation for damage to the garden on the basis that coverage would have presupposed a special clause in the contract. At the time the insured took out the insurance policy, the insurer's agent had wrongly informed the insured that the type of damage would be covered under the general insurance terms. Referring to Chapter 5, section 1 of the Tort Act, the Supreme Court obliged the agent and the insurance company to compensate the insured by paying an amount corresponding to the unpaid insurance claim. But see also *1992:89*, where the Supreme Court in a comparable situation applied the principles regulating contractual liability. Since those cases were decided an explicit provision has been enacted with regard to such liability (Section 9 of the Act on Insurance Contracts (543/1994)).

estate when he assisted in selling assets belonging to the estate without first checking whether a will had been granted legal force. The Supreme Court found that there was a particularly weighty reason to award compensation for the loss, because lawyers have a special obligation to act carefully and properly, and also to consider the interests of other heirs to an estate, not only those of their own client.

Thus the attorney would seem to have acted contrary to good practice, that is, to have violated the duty of care to be expected from an authorised attorney, as well as the trust third parties place in attorneys. In this case, the most plausible explanation for the Court's finding seems to be a view that the heirs were entitled to believe that the attorney would also protect their interests, despite the absence of a contract.

1997:181: The right to commercially exploit a literacy development package was assigned to two companies, X and Y. The parties had agreed on remuneration payable to A, who had made a key contribution to the creation and design of the package. X and Y became insolvent and B, who had held a position of authority within those companies, arranged for another company Z, where B also held a position of authority, to continue to exploit the literacy development package, but without remunerating A. The Supreme Court found Z to have engaged in unfair business practices and, on this basis, awarded A compensation for economic loss on the grounds that a particularly weighty reason existed for doing so:

“In these circumstances it must be considered that [Z], by exploiting the said know-how without paying remuneration in the manner described above, has in accordance with Section 1 of the Unfair Business Practices Act entered into unfair business practices in relation to another entrepreneur, that is, [A]. Thus, there are in these circumstances particularly weighty reasons within the meaning of Chapter 5, Section 1 of the Tort Act for compensating the loss caused to [A] due to the said actions [author's translation].”

The Supreme Court does not give any other reasons for awarding damages other than a violation of Section 1 of the Unfair Business

Practices Act, which seems to suffice. The violation of *good business practices* was “in these circumstances” enough to justify the award of compensation.

The reasons given by the Supreme Court for the decisions cited above are rather vague and brief. They indicate, however, that conduct contrary to good practice is relevant to when evaluating the criterion of *a particularly weighty reason*. But because of the varying circumstances *in casu* (the improper conduct of the employer in 1983 II 187; the clearly foreseeable damage in 1991:79; the trust placed by heirs in an attorney in 1992:44; and the wording “in these circumstances” in 1997:181), it is difficult to evaluate the specific weight attributed to conduct contrary to good practice in this context. Besides, these cases do not specifically involve interference with contractual relations.

However, a later decision from the Supreme Court provides greater clarity in this respect:

2005:105: The copyright holder for a particular design sent a letter to retailers claiming that a competing product violated its copyright and seeking to prohibit the alleged infringement. The courts found subsequently that the competing product did not infringe copyright. The Supreme Court held that the author of the letter had acted contrary to Section 1 of the Unfair Business Practices Act and this was held to be a particularly weighty reason giving rise to liability for damages. The Court further set out the circumstances in which the criterion of a particularly weighty reason might be satisfied:

“If someone in his/her business activities undertakes an intentional act, which is contrary to good business practice or otherwise improper and thus unlawful, in the knowledge that his/her act is likely to cause financial loss to someone else in his/her business activities, the circumstances in question will in principle constitute such circumstances, with regard to the fulfilment of the condition contained in Chapter 5, Section 1 of the Tort Act, as will indicate liability in damages, subject to the existence of special reasons contraindicating such liability [author’s translation].”

Here the Supreme Court in effect sets a four-pronged test. For

liability to arise under Chapter 5, Section 1 to pay compensation for economic loss, there must be: (a) intentional conduct; (b) conduct that is contrary to good business practice or otherwise improper; (c) damage that is foreseeable (*i.e.*, the tortfeasor can be deemed to know that damage would be likely to arise); and (d) no special reasons contraindicating the tortfeasor's liability to pay damages, such as, for instance, similar conduct by the injured party.²³

Thus the Supreme Court has stated an important precedent that is apparently also relevant to our analysis of liability for interference with contractual rights: if a third party C, by interfering, intentionally and contrary to good business practice, with the contract between A and B, causes foreseeable losses to B, he should be liable to pay damages – provided that there are no special reasons precluding liability (*i.e.*, there is a general presumption of liability). We will return to these questions later (see, *infra*, under IV), but before that a comparative examination of *Swedish* case law will be of interest.

2.2 Swedish case law

The Finnish Tort Act was influenced extensively by the Swedish Tort Act (1972:207).²⁴ The Finnish legislator, however, rejected the restrictive Swedish legislative approach, which at least formally appeared to exclude the award of compensation for pure economic loss, unless caused by criminal conduct or the actions of public authorities. The current Chapter 2, Section 2 of the Swedish Act provides “Anyone who causes pure economic loss by criminal conduct shall compensate the damage caused”.²⁵ In addition, the Act contains provisions on the obligation to pay compensation for pure economic loss caused by fault on the part of an administrative authority.²⁶

Despite the lack of a criterion referring to a *particularly weighty*

²³ Cf. the Supreme Court decision 1983 II 187.

²⁴ See, *supra*, fn. 5.

²⁵ Cf. Chapter 3, Section 1.2 (the employer's obligation to compensate pure economic loss caused by the criminal conduct of an employee).

²⁶ See Chapter 3, Sections 2 and 3 in the Swedish Tort Act.

reason or similar requirement for awarding compensation, commentators have long pointed to the *travaux préparatoires* of the Swedish Tort Act. These make it clear that, even though the law refers expressly only to liability, unless damage to property or personal injury is involved, for losses caused by criminal conduct or the acts of public authorities, this was not intended to preclude the award of damages on other grounds.²⁷ In fact, Swedish case law has recognised liability for pure economic loss in several areas: the provision of misleading information in real estate valuations;²⁸ the liability of professionals to persons other than their clients on the grounds of “justified trust”;²⁹ and liability on the part of financial institutions.³⁰

One case of significant interest is a fairly recent decision by the Swedish Supreme Court which dealt with the topic of this article, namely, tort liability for pure economic loss resulting from interference with contractual relations:

NJA 2005 p. 608: Max (M) concluded a contract with Lotsbåten (L) for the transfer of M’s lease of business premises to L. According to the contract, L was not entitled to transfer the lease or sublet the premises to a third party without offering M the option, in certain circumstances, of reacquiring the lease. Furthermore, the contract provided that if L were to give notice of release or if the lease were terminated by a notice from the landlord, M would be entitled to reacquire the lease on certain terms.

It was the parties’ common intention to transfer the lease to L. In no circumstances could M have supposed that L might transfer it to someone proposing to carry on a competing business in the premises, particularly as M was intending during this time to accustom clients to

²⁷ See *e.g.*, *Bertil Bengtsson – Erland Strömbäck*, *Skadeståndslagen*. En kommentar (Stockholm: Norstedts Juridik AB 2008), 57-58 and *Jan Kleineman*, *Ren förmögenhetsskada. Särskilt vid vilseledande av annan än kontraktspart* (Stockholm: Juristförlaget 1987), 138-142. This view has also been expressed in court practice, see *e.g.*, *NJA 2005 p. 608*, 639.

²⁸ *NJA 1987 p. 692*, *cf.* *NJA 2001 p. 878*.

²⁹ *NJA 1987 p. 692*, *cf.* *NJA 1996 p. 700*.

³⁰ *NJA 1998 p. 520*.

its own new premises. L was aware of this and the contract was drafted against this background. A third party, Frasses (F), became interested in renting the premises even before the contract was concluded and expressed views on the drafting of the contract between M and L. The majority of the shares in L were transferred – without M’s knowledge – to F before the contract was concluded.

F thus exercised control over L at the time the contract between M and L was concluded, and even while the contract was being concluded, L was acting with the intention of enabling F to open a competing business in the premises. F acted in concert with L for the purpose of securing possession of the premises. L’s/F’s establishment in the premises proved profitable for both companies, but as a consequence M suffered pure economic loss in the form of reduced turnover. F must have been aware that its establishment in the premises would cause such damage to M.

The case did not involve a situation of unfair competition, rather it constituted a violation of *good business practice* by the respondent (F) against the claimant (M). The Swedish Supreme Court stated: “It is a clear deviation from the standard that can be required of a commercial actor”.³¹ As F had fraudulently acquired the right to the lease with the co-operation of L, against the reasonable expectations of M, of which both F and L were aware, the Swedish Supreme Court awarded damages for pure economic loss, despite the literal meaning of the relevant provisions of the Swedish Tort Act. The Supreme Court held that, under Swedish law, while a contracting party has legal remedy against the other party to the contract, in certain cases a third party may also be liable where his conduct qualifies as grossly improper (*“kvalificerat*

³¹ NJA 2005 p. 608, 641.

otillbörligt”).³²

Thus the Supreme Court seems to have accepted that a third party may in certain circumstances be liable for losses caused by interference with contractual relations that causes a breach by one of the contracting parties. In addition, the Court found that tort liability for pure economic loss arising from interference with contractual rights was accepted in foreign legal systems referring,³³ *inter alia*, to Finnish legal literature.³⁴

3 Views expressed in legal literature

3.1 Finland

As mentioned above, the questions and issues referred to in the introductory part of this article have been scarcely, and even then to some extent superficially, discussed in Finnish legal literature. One reason for this may be that they have seldom been dealt with in our court practice. However, despite the rather scanty views expressed by authors and commentators, there seems to be agreement that so-called *collusive* interference with contractual rights may lead to an obligation to pay compensation. If the common intent of A and the third party C is to cause damage to B by depriving him of his contractual rights, C could

³² *NJA 2005 p. 608, 640*. We may note that as long ago as 1949 Judge Hjalmar Karlgrén stated in case *NJA 1949 p. 645, 651* that “[i]n what has been said, the possibility has not been denied that, if a third party has so to speak been guilty of qualified bad faith in that he, by the acquisition from the party bound by the contractual obligation, has become accessory to the latter’s breach of contract in a way that conflicts with “good practice” or is otherwise clearly improper, then tort liability should rest upon that third party [author’s translation].”

³³ Regarding, English, German and US law, see Norrgård (2006), 66-88 with references. See also Hoffrén (2006), 994-1002, who, in addition to English and German law, discusses French law.

³⁴ See *NJA 2005 p. 608, 640*. On Finnish legal literature, see, *infra*, under III.1.

be liable to pay compensation to B.³⁵ Such interference is considered to constitute unfair business practice.³⁶ But as the notion of *collusive* interference seems unclear in a tort-law context, and as it has been applied mainly to issues within the sphere of property law, the guidance the notion offers when attempting to answer the questions posed in the introduction is rather limited.

One of the most significant and cited works on Finnish tort law is *Hans Saxén's* book *Skadeståndsrätt*.³⁷ As a point of departure concerning his view on liability for contractual interference, Saxén writes that such interference has been disapproved of, as it is in society's best interests that contracts should be performed as agreed.³⁸ Consequently there is a general desire to promote contractual stability and protect contracting parties from the threat of interference by a third party. According to Saxén, even if taking advantage of another party's breach of contract does not usually give rise to liability for damages, liability should attach to conduct that is deliberate, for instance, intentionally inducing a party to breach a contract or preventing the fulfilment of contractual obligations. Additionally, actions that are sufficiently disloyal or contrary to good practice (accepted standards) could trigger an obligation to pay damages.³⁹ However, actions that are only slightly or ordinarily negligent will only rarely fulfil the required criteria. Furthermore, mere persuasion to breach a contract should not lead to liability.⁴⁰ In conclusion, Saxén states:

³⁵ See, *supra*, fn. 7.

³⁶ Cf. *Eva Tammi-Salminen*, *Sopimus, kompetenssi ja kolmas. Varallisuusoidellinen tutkimus negative pledge –lausekkeiden sivullisittovuudesta* (Helsinki: Suomalainen Lakimiesyhdistys 2001), 253.

³⁷ *Hans Saxén*, *Skadeståndsrätt* (Åbo: Åbo Akademi 1975).

³⁸ Saxén (1975), 75.

³⁹ Saxén (1975), 73-74, writes: "Even if it cannot be directly proven that the purpose of [C's] action was to cause damage to [B], but [C] must have realised that damage would most probably occur, it must be possible to oblige him to pay compensation, if his actions are found to be so disloyal, so against good practice, that they cannot be accepted in society. [...] It should be determined *in casu* when the actions go against ethical principles so that liability for such conduct should arise [author's translation]."

⁴⁰ Saxén (1975), 75.

“According to Chapter 5, Section 1 of the Tort Act, compensation for pure economic loss may also be awarded, in addition to circumstances involving criminal acts, when particularly weighty reasons are at hand. Such reasons exist on the one hand when someone causes damage intentionally, on the other hand when damage is caused by especially disloyal conduct. General rules cannot be laid down, instead the question must be resolved *in casu*. In many legal areas there are special rules [author’s translation].”⁴¹

Another frequently cited Finnish commentator is *Mika Hemmo*, who also states that little attention has been paid in Finnish law to the issue of liability for interference with contractual rights.⁴² The reason that there are only a very few situations giving rise to liability is probably a matter of legal tradition. Legal literature and traditional systemisation guide to a large extent the types of claims that are presented in practice. Due to the insufficiency of authoritative material, the position of Finnish law as regards interference with contractual relations is to some extent unclear.⁴³

Hemmo refers to the conflict between the principle of free competition and the obligation to respect concluded contracts. The basis for liability on the grounds of a particularly weighty reason in the context of interference with contractual rights is the third party’s obligation to respect the contract between the two other parties and the rights arising from it. Hemmo does not seem to accept theories of “effective breach of contract”,⁴⁴ but recommends at least a secondary (in relation to the party breaking the contract) obligation for the third party to pay compensation. Hemmo further points out that the more the contractual rights in question may be seen as comparable to property rights, the more justified seems an obligation to pay compensation for interference

⁴¹ Saxén (1975), 77.

⁴² Although, according to him, such interference is hardly more unusual in Finland than in Anglo-American countries. *Mika Hemmo*, *Sopimus ja delikti* (Helsinki: Kauppakaari Oy, Lakimiesliiton Kustannus 1998), 229.

⁴³ Hemmo (1998), 229.

⁴⁴ See Hemmo (1998), 230-231. Cf. also Norrgård (2006), 106-118.

with those rights.⁴⁵ On the other hand, he also mentions arguments in support of restricting liability: uncertainty about the risk of damage (it may be difficult for the third party to find out whether a contract already exists); the *a priori* weaker protection by law of economic interests; and the general principle of freedom of action. Finally, Hemmo states that one could endeavour to compare the issue of liability, for instance, to that of unfair conduct in business practice.⁴⁶

In her doctoral thesis from 2001,⁴⁷ *Eva Tammi-Salminen* also refers to the question of how much weight should be attached to the obligation to respect existing contracts in light of the principles of free competition and business activity. Linking tort liability to interference with contractual rights has been seen as restricting these freedoms. It could also lead to an unpredictable liability to pay damages.⁴⁸ On the other hand, Tammi-Salminen seems to accept liability for a third party who intentionally causes damage to another party by depriving him of his contractual rights. Liability could further arise when a third party, by acting indifferently and against good practice, interferes with existing contracts.⁴⁹

The most extensive study concerning improper interference with contractual rights was published by *Marcus Norrgård* in 2006.⁵⁰ Like other commentators, he refers to the fundamental question of how to establish a reasonable and fair balance between freedom of competition and the need for contractual stability. Free competition is the starting point: parties *prima facie* may compete for contracts. But *after* a con-

⁴⁵ Hemmo (1998), 230.

⁴⁶ See Hemmo (1998), 233. We may note that in a later book, *Vahingonkorvausoikeuden oppikirja* 2002, 119-120, Hemmo discusses the criterion *a particularly weighty reason* and mentions, for instance, the following circumstances that may weigh in favour of liability: the existing quasi-contractual circumstances; the degree of negligence; and the need for compensation to the injured party.

⁴⁷ See, *supra*, fn. 38.

⁴⁸ Tammi-Salminen (2001), 316-317.

⁴⁹ Tammi-Salminen (2001), 318-319. Note, however, that the author makes these statements when dealing with contractual rights tied to negative-pledge clauses - not on a more general level.

⁵⁰ See, *supra*, fn. 6.

tract has been concluded, the third party's potential to interfere with the existing contractual rights should be restricted. Norrgård mentions at least four reasons in support of protecting a contractual party against collusion between a third party and the other contractual party that leads to a breach of the contract: 1) the contract can be viewed as *property*, and as such should enjoy constitutional protection; 2) contractual relations should be protected in view of their fundamental role in the market economy (as without contractual stability and predictability the market economy could not function); 3) liability for interference with contractual rights could also be seen as an expression of a more general principle in civil law, *i.e.*, a party who participates in activity that causes damage should be liable (jointly with the party breaching the contract); and 4) according to the general principles of the law of obligations, specific performance is of primary importance in relation to the duty to pay compensation. Consequently, such performance should be protected against interference by third parties.⁵¹

The strongest argument against imposing liability for interference with contractual relations, according to Norrgård, is the theory of “effective breach of contract”, which has been developed within the field of *Law and Economics*: if breaching a contract leads to a more effective (economic) result than its fulfilment, then the breach should be permitted. This theory is founded, however, on some invalid presumptions.⁵² Nor do the other counter arguments discussed by Norrgård⁵³ support the refutation of his conclusion: *de sententia ferenda* liability should be imposed on a third party C who induces A to breach his contract with B in order to take the latter's place.⁵⁴ Furthermore, Norrgård attempts to elaborate criteria for identifying cases where compensation for interfe-

⁵¹ For a more detailed presentation and discussion of these reasons, see Norrgård (2006), 95-106.

⁵² Regarding these presumptions and the discussion of them, see Norrgård (2006), 106-118.

⁵³ These include: the adequacy of contractual remedies; the principle of privity of contract; the subjective state of mind of the interfering person; and the “opening-the-floodgates” argument. See Norrgård (2006), 118-124. These arguments will be referred to later, see, *infra*, under IV.

⁵⁴ Norrgård (2006), 124.

rence with contractual rights should be paid. We will revert to these issues later (*infra*, under IV).

Summing up the views expressed in Finnish legal literature, all commentators seem to accept the need to protect contractual stability – at least to some extent. Liability for damages should attach to conduct that is deliberate, for instance, when someone intentionally induces a party to breach a contract or prevents the fulfilment of contractual obligations. In addition, conduct that is sufficiently disloyal or contrary to good practice could trigger an obligation to pay damages. As it is difficult to lay down general rules, however, the question of liability must instead be resolved *in casu*.

3.2 Sweden

Turning now to views expressed in Swedish legal literature, we see that long before the Swedish Tort Act of 1972 was adopted, *Hjalmar Karlgren* supported the notion of liability for interference with contractual rights:

“Under special circumstances, such as those where the conduct, when judged by accepted social standards, appears markedly disloyal – there is, for instance, deliberate involvement by the third party in the debtor’s breach of contract (“*kollusion*”) – liability for the third party should perhaps not be excluded [author’s translation].”⁵⁵

Following Karlgren’s comments, the issue of liability for contractual interference was not much discussed until 1993, when *Ulf Bernitz* published his book *Otillbörlig konkurrens mellan näringsidkare*. Here the author studied the few available legal sources and came to the conclusion that there was a possibility under Swedish law to impose liability in tort for conduct of a collusive nature, that is, conduct where the contractual party B and a third party C either co-operate with the intent of causing damage to contractual party A or act in some other grossly improper manner to the detriment of the latter. Bernitz recommended the imposition of such liability under Swedish Law, but pointed out that

⁵⁵ *Hjalmar Karlgren*, *Kollegier i allmän obligationsrätt I* (Lund 1952), 9. See also, *supra*, fn. 34.

the legal situation was unclear.⁵⁶

Subsequently when commenting on the Supreme Court decision *NJA 2005 p. 608*,⁵⁷ Bernitz first emphasised its great value as a legal precedent recognising a right to compensation for pure economic loss falling outside the narrow sphere of Chapter 2, Section 2 of the Swedish Tort Act. He then pointed out that the decision, in which the Supreme Court accepted that a third party might in certain circumstances be liable for losses caused by grossly improper (“*kvalificerat otillbörligt*”) interference with contractual relations, should be seen as an important step in the development of Swedish tort law – especially considering the uncertain legal situation. The fact that tort liability for pure economic loss arising from interference with contractual rights was accepted in foreign legal systems, and also in the ongoing efforts to harmonise the European law of obligations,⁵⁸ obviously influenced the decision of the Court.⁵⁹

However, since this was an *in casu* decision influenced by special circumstances, it is unclear how far-reaching the decision will be. But the position of the Supreme Court sets an important precedent and, according to Bernitz, room needs to be left for further development of

⁵⁶ *Ulf Bernitz*, *Otillbörlig konkurrens mellan näringsidkare* (Stockholm 1993), 199. The study was based on an earlier article from 1987, that is, “*Otillbörligt ingripande i avtalsförhållande*”, in *Festskrift till Lars Welamson* (Stockholm: Norstedts Förlag 1987), 43-70. See also *Lars Gorton - Erik Sjöman*, “*Negativa förpliktelser och tredje män – särskilt om överträdelse av negative pledges i finansiella avtal*”, *Juridisk Tidskrift vid Stockholms universitet* (2002-03), 515-516, who refer to the discussion in Swedish legal literature concerning *collusive* interference with contractual rights. The authors stress that to qualify as such interference, the conduct needs to be grossly improper.

⁵⁷ See, *supra*, under II.2.

⁵⁸ See, e.g., Book VI, Chapter 2, Section 2 VI. – 2:211: “Loss upon inducement of non-performance of obligation” and Section 2 VI. – 2:208: “Loss upon unlawful impairment of business” in *Principles, Definitions and Model Rules of European Private Law. Draft Common Frame of Reference (DCFR)*. Prepared by the Study Group on a European Civil Code and the European Research Group on Existing EC Private Law (Acquis Group). Outline Edition 1-1-2009: http://www.storme.be/2009_02_DCFR_OutlineEdition.pdf.

⁵⁹ See *Ulf Bernitz*, “*Skadeståndsansvar för otillbörligt ingripande i avtalsförhållande och medverkan till kontraktsbrott; HD utvidgar ansvaret för ren förmögenhetsskada*”, *Juridisk Tidskrift vid Stockholms universitet* (2005-06), 627-628.

the law. Cases may arise in the future based on similar circumstances and events, and these should be judged in accordance with consistent legal principles. He concludes by stating that the imposition of tort liability on an interfering third party requires the presence of improper conduct that clearly violates good business practice.⁶⁰

4 Criteria for liability in tort

It is now time to return to the questions posed in the introductory part of this article. Is it possible, by applying the notion of a *particularly weighty reason*, as provided in Chapter 5, Section 1 of the Finnish Tort Act, to identify and elaborate criteria for distinguishing between cases where compensation for interference with contractual rights should be available and those where compensation should be denied?

Our study of Finnish court cases has revealed rather scarce and incoherent Supreme Court practice. Nevertheless, the cases indicate that the presence of conduct contrary to good practice is of relevance when evaluating the criterion of a *particularly weighty reason*. But because of variations in the circumstances in the different cases, it is difficult to draw general conclusions about the significance of such conduct. In addition, none of the cases specifically addresses interference with contractual relations. However, the more recent Supreme Court decision 2005:105 provides greater clarity as regards the circumstances in which the criterion of a particularly weighty reason might be satisfied. The Court stated that a person who in his business activities intentionally (and contrary to good business practice or otherwise improperly) caused foreseeable financial loss to another, should be liable to pay damages, provided that no special reasons contraindicated the imposition of liability. And as indicated previously (*supra*, under II.1), this would mean that a third party who intentionally and contrary to good business practice interfered with existing contractual relations, thereby

⁶⁰ Bernitz (2005-06), 629. Cf. also Gorton – Sjöman (2002-03), 516.

causing foreseeable financial loss to one of the contracting parties, should be liable in tort.⁶¹ The position adopted by the Supreme Court also seems to be in line with views expressed in the literature regarding liability for so-called *collusive* interference with contractual rights (*supra*, under III.1).

Furthermore, views expressed in both Finnish and Swedish legal literature seem to attach considerable weight to *grossly improper* conduct or conduct *contrary to good business practice*⁶² as criteria for triggering the obligation to compensate pure economic loss. But to be more useful in practice, such general notions need to be specified *in concreto*. Consequently, for the purposes of this article, we need to undertake a more detailed analysis. What kind of conduct by a third party (interfering with existing contractual rights) triggers liability to pay compensation? What criteria concerning the third party's intent and knowledge of actual circumstances can be advanced for the purposes of establishing liability?

By way of introduction, we should state that mere negligence on the part of the third party is not enough to trigger liability.⁶³ Despite the need to promote contractual stability, parties may legitimately compete for contracts and the principle of free competition should not be exces-

⁶¹ Such a position is consistent with the Swedish Supreme Court decision *NJA 2005 p. 608*, which accepted that a third party might in certain circumstances be liable for losses caused by interference with contractual rights resulting in a breach by one of the contracting parties.

⁶² Cf. Section 1 of the Unfair Business Practices Act of 1978, which prohibits conduct that is contrary to good business practice or otherwise improper. When evaluating such conduct, account should be taken of business usages and customs and ethical rules. See Norrgård (2006), 63-65. However, conduct contrary to Section 1 does not seem to automatically trigger a right to compensation in accordance with Chapter 5, Section 1 of the Tort Act. Cf. the Supreme Court decision 1991:32. But see also 1997:181 (*supra*, under II.1). In Finnish legal literature the argument has been made that an obligation to compensate economic losses should be linked to violations of the Unfair Business Practices Act. See e.g., Björn Sandvik, "Skada orsakad av otillbörligt förfarande i näringsverksamhet – HD:s praxis pekar på behovet av en särreglering", *Tidskrift, utgiven av Juridiska Föreningen i Finland* (2006), 534-538. Cf. also Tammi-Salminen (2001), 312 and Norrgård (2006), 165.

⁶³ See also Norrgård (2006), 158 and, regarding Swedish law, Gorton – Sjöman (2002-03), 516.

sively restricted. That said, it is important to weigh the interests of the disadvantaged party (*i.e.*, the possibility of getting adequate compensation from the party breaching the contract) against the consequences of a broader application of the criterion of a *particularly weighty reason*. Essentially we agree with Norrgård's observation that there may be situations where contractual remedies are insufficient to secure full compensation for the party who has suffered damage (*e.g.*, the insolvency of the party breaching the contract, contractual limitations on liability and compensation,⁶⁴ *etc.*).⁶⁵ Accordingly there is a need for complementary liability on the part of the interfering third party. On the other hand, the opening-the-floodgates argument is also significant: overly broad liability for third parties could significantly increase litigation costs, as well as uncertainty regarding the extension of liability and the persons liable.⁶⁶

When trying to find a reasonable balance between these conflicting interests in order to elaborate criteria for establishing the interfering third party's tort liability, it seems possible to identify some basic requirements: firstly, the interfering third party (C) must have knowledge of the existing contract between A and B, and, secondly, his intention⁶⁷ must be to interfere in the contract between A and B. Thus "intentional conduct" in the present context means that C by his conduct aims to

⁶⁴ Note, however, the general view in Finnish case law and legal literature has been that actions of a contractual party that are either grossly negligent or intentional will make any clauses excluding or limiting liability ineffective or void. See *e.g.*, *Mika Hemmo*, Vahingonkorvauksen määräytymisestä sopimussuhteissa (Helsinki: Suomalainen Lakimiesyhdistys 1994), 299-304, and from court practice the Supreme Court decision 1993:166.

⁶⁵ See Norrgård (2006), 118-120.

⁶⁶ *Cf.* Norrgård (2006), 122-123 and Tammi-Salminen (2001), 317.

⁶⁷ The importance of intentional conduct as a prerequisite for liability was also stressed by the Finnish Supreme Court in case 2005:105 (*supra*, under II.1). In Finnish tort law there is no requirement for express intent, a person's intention may be implied from his conduct and his knowledge of relevant circumstances.

cause A to breach his contract.⁶⁸ However, no express intention to cause damage to B is required, since it is generally known that a breach of contract will usually lead to economic loss.⁶⁹

Consequently, assessing the intention (state of mind) of the interfering party becomes significant. If it can be shown (the party claiming damages has the burden of proof) that C has induced⁷⁰ A to breach his contract with B, then C should be liable in tort. Furthermore, in this author's opinion, exercising persuasion on A⁷¹ to breach his contract should be judged similarly. In any event, making a distinction in this respect (between inducing and persuading) would lead to insurmountable practical difficulties.⁷² Similarly, intentional (or fraudulent⁷³) collusion between C and A to deprive B of his contractual rights should lead to liability for C. But what if C merely encourages A to breach his contract?

It would seem possible to distinguish between situations where C induces/persuades A to breach his contract with B and those that only

⁶⁸ My starting point has been that C concludes a substitute contract with A. Norrgård discusses such situations and concludes that the prerequisite "intent" is also fulfilled when C endeavours to conclude a contract with A in the knowledge that it is highly probable that this will cause A to breach his contract with B. For more details, see Norrgård (2006), 151-156.

⁶⁹ Cf. Norrgård (2006), 152-153.

⁷⁰ In *Henry Campbell Black*, Black's Law Dictionary (St. Paul Minn.: West Publishing Co. 1979), 697 "induce" is defined as follows: "[t]o bring on or about, to affect, cause, to influence to an act or course of conduct, lead by persuasion or reasoning, incite by motives, prevail on."

⁷¹ Black (1979), 1030 defines "persuade" as follows: "[t]o induce one by argument, entreaty, or expostulation into a determination, decision, conclusion, belief, or the like; to win over by an appeal to one's reason and feelings, as into doing or believing something; to bring oneself or another into belief, certainty or conviction; to argue into an opinion or procedure."

⁷² Compare the definitions cited above in fns 70-71. But cf. Saxén (1975), 75, who in this regard seems to make a distinction between inducing and persuasion.

⁷³ Cf. the Swedish decision *NJA 2005 p. 608* (*supra*, under II.2). We should add that if C has committed a criminal act (e.g. fraud, unlawful threats, bribery), liability to pay compensation arises in any event in accordance with explicit provisions in Chapter 5, Section 1 of the Finnish Tort Act and in Chapter 2, Section 2 of the Swedish Act.

amount to encouragement. The causality required in tort law⁷⁴ would seem to be fulfilled when C's inducement/persuasion leads A to terminate his contract with (and thereby cause damage to) B,⁷⁵ whereas C's mere encouragement of A would appear to have a less significant causal effect on the latter's decision to breach the contract.⁷⁶ In other words, it might be rather difficult to show the necessary causal link⁷⁷ – all the more so if C's conduct amounted only to advising A to terminate the contract. In such cases C would normally lack any intention to conclude a substitute contract with A.⁷⁸

Situations where C and A exchange offers to conclude a contract may be more difficult to judge (here we are still assuming that C knows about the existing contract between A and B). If A sends an offer to C, acceptance of which *de facto* means that A must terminate his contract with B, it is difficult to see that C would be liable in tort.⁷⁹ Such conduct seems to fall within the sphere of free competition and permitted business usage. But if C takes the initiative and sends an offer to A, intending

⁷⁴ The principal legal question arising in tort is whether the *collusion* between C and A suffices to fulfil the criteria of necessary (“*nödvändig*”) and/or sufficient (“*tillräcklig*”) causality between the damage suffered by B and the actions of C, as well as of the foreseeability of the damage. In general, both a necessary and a sufficient cause are required, but in cases of contributory negligence (cf. Chapter 6, Section 2 of the Finnish Tort Act) sufficient cause may be enough to impose liability on a tortfeasor. The assessment to establish whether the criterion of causality is met is largely based on evidentiary grounds. Evidentiary support may be derived, *inter alia*, from the behaviour of the parties. Regarding causality, see e.g., Saxén (1975), 53-58.

⁷⁵ Cf. Norrgård (2006), 148 who uses the concept *psychological causality* to describe the necessary causality, for instance, C, by stressing (increased) expected economic benefits influences A so that he breaches his contract with B.

⁷⁶ “Encourage” is defined in Black (1979), 473 as follows: “[i]n criminal law, to instigate; to incite to action; to give courage to; to inspire; to embolden; to raise confidence; to make confident; to help; to forward; to advise.”

⁷⁷ C's conduct must have a sufficient influence on A's decision to breach his contract with B (for instance, such a causal link would be lacking if A had decided to terminate the contract even before C's interference). Of course, in a situation where C and A are engaged in a close, and perhaps long-lasting, cooperation, it may in practice be difficult to distinguish between different kinds of conduct (inducing, persuading, encouraging) and a judgment will have to be made based on all the proven circumstances *in casu*.

⁷⁸ See also Norrgård (2006), 127-128.

⁷⁹ Cf. regarding Swedish law, Gorton – Sjöman (2002-03), 517.

to replace B as a contracting party with A, the situation may, depending on the proven circumstances *in casu*,⁸⁰ resemble inducement or persuasion. However, simply offering better terms or conditions than those provided for in the contract between A and B should not normally be enough to trigger liability for C.⁸¹ As stated above, it is necessary to show an adequate causal link between C's intentional act that aims to cause the breach of the contract between A and B and the economic loss suffered by B.

In the introductory part of this article we also raised the issue of the relevance in this context of an existing contractual relationship between the injured party B and the interfering third party C. Suppose, for instance, A has concluded a long-term contract with B for the supply of a certain product, and B has in turn entered into a contract with C for a supply of the product in question ("chain contracting"). Subsequently C, being aware of B's agreement with A, both causes A to breach his contract with B and terminates his own contract with B. Thereafter C contracts directly with A to supply the product. As a result, B is out of the picture and suffers economic loss.

In this author's view, C's conduct in this situation is particularly improper and accordingly should result in the application of a lower threshold for liability to compensate B's pure economic loss,⁸² especially in those situations mentioned above, where B's right to compensation seems less certain. The parties to a contract (here C and B) should be *loyal* to each other, that is, they should not only promote their respective

⁸⁰ For instance, business practice, trade usages and published commercial ethical codes may be of relevance. The court will conduct an assessment of all the relevant circumstances of the case, weighing up the rights, interests and conduct of each party to determine whether, in the case at hand, there are especially weighty reasons to impose liability.

⁸¹ Norrgård (2006), 128 states that a mere offer from C to A cannot trigger liability: some kind of closer contact is needed, that is, C and A must have some degree of common intent to accomplish the breach of the contract with B and enter into a substitute contract between themselves. Norrgård also talks about "dual causality", that is, the intentions of both C and A have caused the breach of the contract (150).

⁸² Once again note that the contractual remedies available to B against C and A may be insufficient to secure full compensation. For instance, the contract between A and B might be longer-lasting than that between C and B.

interests, but (to a certain extent) should also take into account the rights and interests of the other party.⁸³ The duty of loyalty⁸⁴ is a core element of contract law and good business practice.⁸⁵ It is especially relevant in long-term contractual relationships, more specifically as concerns the trust and expectations for the future that the parties to the relationship rely on.⁸⁶ But even if the duty of loyalty has its roots in contract law, it may also have relevance when evaluating non-contract-

⁸³ In general, the more quasi-contractual the relationship, the lower the threshold applied by the courts when awarding compensation. Breaches of the duties of good faith, performance and loyalty will be significant factors.

⁸⁴ In Finnish legal literature, the requirement of good faith has often been called the duty of loyalty. However, the duty (or, sometimes, principle) of loyalty (*”lojaliteettiperiaate”*) may easily be confused with another principle, namely the duty of fidelity (*”lojalisuusvelvollisuus”*) which is the unilateral, fiduciary duty of an “agent” in respect of his client. However, the principle of loyalty is a bilateral duty, applicable to both parties. It has been suggested in legal literature that speaking of “good faith”, rather than of the principle of loyalty, would help avoid confusion. The duty to inform and the duty to co-operate may be seen as forming part of the requirement of good faith, but not as synonyms. See *Jukka Mähönen*, Chapter 7 “Lojaliteettivelvollisuus ja tiedonantovelvollisuus”, in *Varallisuus oikeuden kantavat periaatteet*, Ari Saarnilehto (toim.) (Helsinki: WSOY Lakitieto Oy 2000), 129 – 143.

⁸⁵ A distinguished professor of Finnish contract law, Lars Erik Taxell, stated as long ago as 1972, that: “the principle of loyalty expresses the idea that parties to a contract are not allowed unilaterally to promote their own interest to detriment of the other party to the contract. A party is, within certain limits, obliged to take into account the right and interests of its opposite party... The idea that a party has a duty of loyalty is not explicit in law. However, it is in any event firmly rooted in Finnish contract law... As a supplementary general principle (standard), the principle of loyalty may be applied on a broad basis in contractual relationships and especially in connection with disturbances to the contractual relationship. It is also possible that non-observance of the duty of loyalty itself amounts to a breach of contract [author’s translation]”. *Lars Erik Taxell*, *Avtal och rättsskydd* (Åbo: Åbo Akademi 1972), 81-82.

⁸⁶ See *Juha Häyhä*, “Lojaliteettiperiaate ja sopimusoppi”, *Defensor Legis* (1996), 317. See also *Olli Norros*, “Sopimus oikeudellisten periaatekokoelmien oikeuslähdearvo”, *Lakimies* (2007), 40, who states that international legal principles (*i.e.*, the Principles of European Contract Law and the UNIDROIT Principles of International Commercial Contracts) in general play a supplementary role to domestic law. However, such principles (including the principles of good faith and fair dealing) may be relevant when interpreting Finnish law where it is necessary to take into account international methods of interpretation.

tual liability.⁸⁷ Once again, this will depend on all the proven circumstances *in casu*.⁸⁸

The purpose and object of the contract between A and B may also be of particular interest in the present context. Take, for example, an agreement whereby a specific (type of) object or a product of a generic nature but in limited supply is sold to B. C's interference with the contract between A and B may actually mean that the same product⁸⁹ is sold twice. Chapter 13, Section 2 of the Commercial Code of 1734 expresses an important and ancient principle of property law, which still applies today:

“If someone lets the same [object] to two [persons], the first lessee shall keep it, had the second promised more or not, and the lessor shall pay ten [daler] in fine, and compensate the damage. The law shall be the same for him, who rents something he knows to have been let to another [author's translation].”

The quoted text provides that, in cases of “double” renting/hiring, timing is decisive: the first lessee has the right to keep the object of the

⁸⁷ Sisula-Tulokas (2009), 562 also writes that conduct contrary to principles of good faith and fair dealing, including the duty of loyalty, may have relevance when evaluating non-contractual liability. However, Rudanko (2009), 544 stresses that the duty of loyalty has relevance only between parties tied to a contract, that is, it has no significance when assessing tort liability.

⁸⁸ Cf. Saxén (1975), 77. Sisula-Tulokas (2009), 571-572 also mentions the necessity of *in casu* assessments in difficult and unclear cases.

⁸⁹ In this example we assume that the contract between A and B concerns a generic product of which all exportable quantities have been contractually secured by B.

lease.⁹⁰ The lessor has to pay a fine and compensate any losses.

In the present context, however, our interest is focused on the second sentence of the provision. Here we find an old legal rule concerning compensation for interference with contractual rights: a third party who rents something he knows has been let to another shall be liable to pay damages. This liability arises regardless of whether the third party has an intention to cause the breach of the existing lease (no inducing, persuading or other such improper conduct is needed). It is enough that he takes advantage of the breach.⁹¹

There is no equivalent explicit rule with regard to sales contracts.⁹² However, if C by his improper conduct causes A to breach his contract with B, C should be liable in tort in accordance with the principles and criteria mentioned above. The fact that the sales contract concerned a specific object⁹³ should be taken into account when asses-

⁹⁰ The quoted rule can also be considered against the background of principles relating to the so-called double sale of movables. This refers to the situation where a seller has sold the same object twice, giving rise to the question of a non-contractual situation between two buyers. According to Chapter 1, Section 5 of the Commercial Code the first buyer shall obtain possession of the object. If, however, the second buyer has obtained possession of the object and has acted in good faith, both at the time of the conclusion of the contract and at the time of the transfer of possession, the second buyer will be entitled to the right of ownership. "Good faith" here means that the second buyer did not know and could not have known about the first transaction. The requirement of good faith has also in general been given a central status in the form of a requirement for the validity of the buyer's title. Cf. Chapter 11, Section 4 of the Commercial Code and Chapter 13, Section 3 of the Act on Land (540/1995). From legal literature see e.g., *Esko Hoppu - Kari Hoppu*, Kauppa- ja varallisuusoikeuden pääpiirteet (Helsinki: WSOYpro 2005), 115-116.

⁹¹ See also Norrgård (2006), 15.

⁹² However, Tammi-Salminen (2001), 316 indicates that the provision in Chapter 13, Section 2 of the Commercial Code could express a more general principle of liability for a person who consciously infringes another person's rights. Even though this view has much to recommend it, it seems that the existence (and content) of such a principle outside the explicit framework of Chapter 13, Section 2 remains uncertain, cf. also Norrgård (2006), 105.

⁹³ Even if B has a right to the specific object, see *supra*, fn. 90, he may suffer economic losses. As examples of such losses, Hemmo (1998), 229, fn. 79 mentions costs related to the clarification of the legal situation and losses caused by delayed delivery of the object.

sing the liability of C to compensate pure economic loss.⁹⁴ Similarly this rule may be of relevance in the case of a (perhaps long-term) sales contract between A and B concerning a product that is of a generic nature but which is in limited supply. The proven facts may reveal that B is having great difficulties obtaining – or is even unable to obtain – the product elsewhere.

5 Conclusions

Against the background of the Finnish Supreme Court decision 2005:105 (*cf.* the Swedish decision *NJA 2005 p. 608*), as well as views expressed in both Finnish and Swedish legal literature, accepting that grossly improper conduct (contrary to good business practice or otherwise improper) may trigger liability to pay compensation, we have in this article examined what kinds of conduct by an interfering third party (C) could give rise to such liability. We have concluded that inducement/persuasion to breach an existing contract fulfils the criterion of a *particularly weighty reason*, while conduct amounting only to encouraging/advising a contractual party (A) to breach his contract would normally not have that effect, because of the requirements in tort law for a causal link. We have also stated that an existing contractual relationship between the injured party (B) and C, as well as the purpose and object of the contract between A and B, should be accorded significance when assessing C's liability.

⁹⁴ *Cf.* Norrgård (2006), 104, who in such situations speaks of a “special interest” of the person having contracted for the object.

When pirates capture the cargo

CICG § 35 in the light of *Masefield AG v Amlin
Corporate Member Ltd*

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1 Introduction

The topic of this article is the cargo owner's right to a total loss settlement according to the Norwegian Cargo Clauses¹ (the "CIGC") when pirates capture a cargo that is being transported by ship. As the carrier will not normally be liable for damage to, or loss of, cargo due to piracy,² the capture of cargo will be an issue between the cargo owner and his cargo insurer. Cargo insurance is a variety of casualty insurance that covers cargo loss or damage occurring during transportation from one place to another. Piracy is a peril that may be covered under cargo insurance. Piracy is not a new peril, but recent developments have highlighted problems associated with pirate attacks. In recent years, the steady increase in pirate attacks, including vessel hijackings, in the Gulf of Aden and off the coast of Somalia has once again put piracy on the insurance agenda.³ Between 1 January 2008 and 21 June 2010 there were 495 attempted and successful pirate attacks in the seas off Somalia.⁴

These attacks have raised questions primarily in relation to the insu-

¹ Conditions relating to insurance for the Carriage of Goods of 1995, Version 2004, CEFOR Form no 261.

² According to § 275 of the Norwegian Maritime Code, the carrier is liable in cases of negligence with a shifted burden of proof. Accordingly, capture by pirates will not normally trigger carrier's liability unless he is in breach of safety regulations, *cf.* further Trine-Lise Wilhelmsen, "Challenges in modern marine insurance of shipowner's interest: piracy and terrorism", *The modern law of marine insurance* volume 3, edited by Rhidian Thomas, London, 2009 (Wilhelmsen 2009) pp. 177-211, pp. 201-202.

³ According to the Annual Report from the International Maritime Bureau, there were 31 reported hijackings off the coast of Somalia in 2007. From January to December 2008, more than 100 pirate attacks were reported, including more than 40 hijackings, *cf.* Knott *Piracy off Somalia: Naval Responses* <http://www.hfw.com/news/articles/2008/piracyoffsomalianavalresponses> and http://www.icc-ccs.org/index.php?option=com_content&view=article&id=332:imb-reports-unprecedented-rise-in-maritime-hijackings&catid=60:news&Itemid=51. Taking a longer perspective, more than 3,000 actual or attempted acts of piracy were reported worldwide during 1996-2005, *cf.* Mejia, Cariou and Wolf *Ship Piracy: Ship type and flag*, in Talley (ed) *Maritime Safety, Security and Piracy*, p. 103.

⁴ Exclusive Analysis, as referred to by Henrik Rak at a seminar in Reykjavik August/September 2010.

rance of the ship, *i.e.*, hull insurance and loss of hire insurance, and, in particular, in relation to salvage measures and general average.⁵ So far, there has been less focus on cargo insurance. Recently, however, the question of coverage for total loss of the cargo in the event of capture by pirates was addressed in the English case *Masefield AG v Amlin Corporate Member Ltd* (“*Masefield v Amlin*”).⁶ It is of interest to discuss the relevant Norwegian provision in CIGC § 35 in the light of this decision. A key issue to consider is the extent to which the Norwegian and English systems produce the same result. The international nature of cargo transport has brought about an international approach to cargo insurance and has often led to international harmonisation.⁷ Consequently it is of interest to see whether harmonisation exists in this type of situation.

Another reason to discuss this issue is that Hans Jacob Bull, to whom this edition of SIMPLY is dedicated, was the chairman of the committee that drafted the CIGC clauses. So far these clauses have appeared to function well in the sense that there are very few cases concerning cargo insurance issues and apparently very few disputes. It is worth investigating whether the clauses are equally robust in the face of recent developments concerning the piracy risk.

In the following we will briefly address coverage for piracy under the CIGC before examining coverage for total loss in the light of *Masefield v Amlin*. First of all, however, it is convenient to provide an overview of the legal sources relevant to cargo insurance.

⁵ Cf. Wilhelmssen 2009 pp. 177-211.

⁶ (2010) EWHC 280 (Comm).

⁷ Svante Johansson, *Varuförsäkringsrätt*, Stockholm 2004, p. 25 and p 43.

2 The legal sources

2.1 The legislation

Insurance in Norway is regulated by Act no. 69 of 16 June 1989 relating to insurance contracts (“the ICA”). In general the provisions of the ICA are mandatory.⁸ There are, however, several exceptions for insurance relating to commercial activities. One such exception relates to the insurance of goods being transported internationally.⁹

This article, however, is about total loss, which is part of the scope of cover, and the ICA contains no rules on this issue. The scope of cover is regarded as an aspect of product development, and as such free competition is thought to be in the best interests of those buying insurance.¹⁰ Thus there is freedom of contract in relation to the questions discussed here.

2.2 The Norwegian Cargo Clauses

The insurance conditions used in Norway for cargo insurance are the Norwegian Cargo Clauses: Conditions relating to Insurance for the Carriage of Goods of 1995, Version 2004, CEFOR Form No. 261 (“the CICG”). The conditions constitute a so-called “agreed document”, which has been drafted by a committee consisting of representatives of all the interested groups, *i.e.*, the insurers, the Federation of Norwegian Commercial and Service Enterprises, the Confederation of Norwegian Business and Industry, and legal practitioners.¹¹ The chairman of the committee responsible for drafting the 1995 conditions and the 2004 version was, as already mentioned, Professor Hans Jacob Bull of the Scandinavian Institute of Maritime Law.

The use of agreed documents in marine insurance has a long tradi-

⁸ ICA section 1-3 first subparagraph.

⁹ ICA section 1-3 second subparagraph letter (d).

¹⁰ Hans Jacob Bull: *Forsikringsrett*, Oslo 2008, pp. 206-207.

¹¹ The participants are listed in the preface to the 1995 Conditions.

tion in Norway. The first so-called Marine Insurance Plan, which contained provisions relating to both ship and cargo insurance, was published in 1871. This plan was amended in 1881, 1894, 1907 and 1930. In 1967, in connection with the revision of the 1930 Plan, a separate Cargo Insurance Plan was issued. This was revised again in 1995, resulting in the conditions in use today. The 1995 conditions were amended in 2004.

A characteristic feature of the CICG is that the conditions are supplied with a Commentary¹² which reflects the parties' negotiations during the drafting process. According to Norwegian legal method, the Commentary constitutes a preparatory document that carries significant weight when interpreting the conditions.¹³

The CIGG applies to both the national and the international transport of cargo. With regard to the provisions discussed here, both types of transport are similarly regulated.

3 Piracy as a peril under the CIGG

The definition of perils covered determines the kinds of risks for which the insurer is liable. A key characteristic of cargo insurance is that the perils to be covered are divided into three levels and it is up to the person effecting the insurance to choose what level of cover should apply. The most narrowly defined list of perils – the so-called C Clauses – includes five named perils. In relation to carriage by vessel, the C Clauses cover situations where the vessel has “collided, struck any object, sunk, capsized or suffered a similar serious accident”, “fire, light-

¹² Commentary to Norwegian Cargo Clauses: Conditions relating to Insurance for the Carriage of Goods of 1995, Version 2004, CEFOR Form No. 261 A.

¹³ The status of preparatory documents to contractual regulation is discussed in ND 2000.442 NA *Sitakathrine*, ND 1998.216 NSC *Ocean Blessing*, ND 1991.204, NSC *Hardhaus*, ND 1978.139 NA *Stolt Condor*, cf. also Trine-Lise Wilhelmsen and Hans Jacob Bull, *Handbook in hull insurance*, Oslo 2007, p. 29-30, and Hans Jacob Bull, “Avtalte standardvilkår som privat lovgivning”, *Lov, dom og bok*, Festskrift til Sjur Brækhus, ed. Thor Falkanger, Oslo 1988, pp 99-114, pp. 110-111.

ning or explosion” and natural disasters.¹⁴ Somewhat broader coverage is offered on the B Clauses, which in addition to the perils already mentioned cover part of the storage and loading risk.¹⁵ As no coverage is provided for events falling outside the scope of the named perils, piracy is outside the scope of the B and C Clauses.

The widest coverage is provided by the A Clauses, which cover “all risks of loss or damage to which the insured goods are exposed”. As a point of departure, the A Clauses therefore provide cover for piracy as a peril. However, the cover is subject to exclusions specified in §§ 17, 18 and 19. Of interest here is the list of exclusions provided in § 18. While this list does not refer to piracy directly, it does include some perils that may overlap with the concept of piracy. The overlap may concern the person who performs the act of piracy, the motive for the act and how the act is performed.¹⁶

As the CIGG do not mention piracy as an insured peril, the concept is not defined in the conditions. The Norwegian term for piracy is “sjørøveri”, for which the literal translation is “sea robbery”. The term “sea robbery” suggests that someone is “robbed” of his possessions. The Norwegian term “røveri” is not used in modern Norwegian criminal law, but seems to be synonymous to the Norwegian term “ran”,¹⁷ which is defined as an act where one person takes a possession belonging to another by the use of force against a person or by putting that person in a position where he may not defend himself, or by making threats that cause a serious fear of violence against any person.¹⁸

An act of “robbery” is by its nature illegal. This means that the capture of the ship and cargo by State authorities lies outside the scope

¹⁴ CIGG § 5 nos 1, 3 and 4.

¹⁵ CIGG § 4 nos 7-9.

¹⁶ For a more extensive discussion of this issue see Mats Fielding, *Insurance and Piracy. A cargo insurance perspective*, unpublished master’s thesis, University of Oslo, 26.08.2009, <http://www.duo.uio.no/sok/work.html?WORKID=94336>

¹⁷ The Penal Code 1902/10 § 269 states that anyone who equips or plans to equip a ship for the purposes of “ran” may be punished by up to three years’ imprisonment. In the index to Norwegian statutes, this provision is denoted “preparation to commit sea robbery”.

¹⁸ The Penal Code § 267.

of this concept. Capture by a State authority is excluded by § 18 no. 8. Normally there should be no difficulty in distinguishing between State authorities and pirates. In some cases, however, acts of piracy may be undertaken by people purporting to exercise government authority (e.g., an exile government may sponsor vessel captures in order to draw global attention to its cause and/or finance its campaign). In these circumstances it will be necessary to draw a distinction between “piracy” and “measures by a foreign State power”.

A robbery is normally undertaken for economic gain. However, a ship may also be captured by groups with political or social motives. The concept of “robbery” requires an act of stealing and the use of force – there is no restriction as to motive. Accordingly, where actions such as capturing ships, making threats against ships, cargoes and crews, and demanding ransoms are undertaken in order to pressurise governments into complying with the wishes of political groups, all such actions may, as a starting point, constitute piracy. However, since acts of terrorism are excluded from the scope of coverage by virtue of § 18 no. 3, it is necessary to make a distinction between piracy and terrorism. The concept of “terrorism” is not defined in the CICG, but according to the Commentary at page 33, the term “primarily covers the wilful destruction of objects, perpetrated for a political, social or similar purpose”. As the piracy risk so far has concerned the capture of ships and cargoes in order to claim ransoms for economic gain, the distinction between piracy and terrorism has not been an issue in Norwegian cargo insurance.¹⁹

Pirates normally use weapons when attacking a ship. The CIGC contain no exclusion regarding the use of conventional weapons such as guns, knives or explosives. CIGC § 18 no. 11 does, however, contain an exclusion for chemical, biological, biochemical or electromagnetic weapons. As far as the writer is aware, there are no reports indicating the use of these kinds of weapons by pirates, and the use of such weapons might indicate that the acts were being performed by terrorists rather

¹⁹ In the NSPL, the piracy risk and terrorist risk are both covered by the war risk insurance, cf. NSPL § 2-9 and Wilhelmssen 2009 pp. 179-188.

than pirates, implying that the attack would be excluded from cover also for this reason.

In short, any illegal attack by individuals or private groups carried out against ships and cargoes for economic motives is covered so long as the attack does not involve the use of the weapons listed in § 18 no 11.

4 Coverage for total loss in the event of capture

4.1 Introduction and overview of the problem

The losses covered under the ordinary scope of cover in the cargo conditions are total loss, partial loss and damage.²⁰ If the goods were damaged when the ship was attacked or captured by pirates, the insured can claim compensation according to CICG § 37. In cases of partial loss, *i.e.*, where part of the insured consignment of goods has been totally lost, compensation is paid according to § 36. These rules do not seem to raise any special problems in relation to our topic here.

The rules on total loss, however, may give rise to certain problems in relation to capture by pirates. CICG § 35 first paragraph defines a total loss as follows:

There is a total loss when:

1. The entire consignment of goods has been destroyed.
2. The Assured is deprived of the entire consignment of goods with no possibility of retrieving it.
3. The transit to the named place of destination has been abandoned in accordance with § 27 or § 28.

²⁰ CICG § 6 *cf.* § 35, § 36 and § 37.

4. The entire consignment of goods has been so severely damaged that at least 90 per cent of the value must be deemed to be lost.

A characteristic feature of capture by pirates today is that once the pirates have taken control of the ship, cargo and crew, they will sail either to an unknown place or to an area outside the flag State's jurisdiction. If the cargo is destroyed or so extensively damaged that only 10 % of the insured value remains, the insured may claim for total loss according to § 35 nos. 1 or 4. The interesting part of the paragraph in relation to capture, however, is no. 2, which states that there is a total loss if the assured is deprived of the entire consignment of goods with no possibility of retrieving it.

The question of total loss in this situation becomes significant if the value of the cargo changes during the period of captivity. Once a total loss is established, the insurer becomes liable for the sum insured, but not in excess of the insurable value, *cf.* § 35 second paragraph, first sentence. According to § 29, the insurable value shall be deemed to be the market value of the goods at the place of loading at the inception of the insurance. If the goods belong to the seller, this will be the maximum value, *cf.* § 29 first paragraph. If they belong to the buyer, charges, insurance, freight and anticipated profit will be added, *cf.* second paragraph. If the value of the goods has increased above the sum insured/insurable value by the time the cargo owner recovers them, he will not be interested in claiming for total loss. However, if their value is reduced, a total loss settlement would mean that the insurer would have to pay the sum insured up to the limit of the insurable value, subject to a right of subrogation in respect of the lower valued goods, *cf.* CICG § 52. Accordingly the insurer in this case takes over the risk of a reduction in the value of the goods during the period of captivity. This may be particularly relevant for goods where the market value varies substantially, such as oil, and in cases where the vessel spends a long time in captivity. A recent example of the latter situation was the capture of *The UBT Ocean*, which was captured on 5 March 2010 and released 136 days later in June.

CICG § 35 no. 2 raises several problems. Firstly, when is the assured

“deprived” of the goods? Secondly, at what point in time should the evaluation of the possibility of retrieving the cargo take place? Thirdly, should this evaluation be objective or subjective? Fourthly, what material is relevant when making this evaluation? Fifthly, how should we define the meaning of “no possibility of retrieving” the cargo? And finally, is recovery of the goods against payment of a ransom acceptable?

4.2 “Deprived”

Saying that the assured is “deprived” of the goods implies that the goods are a total loss in the sense that they are not at the assured’s disposal in purely physical terms.²¹ If the pirates have stolen the goods, there is indeed a total loss. However, the word “deprived” only indicates that the assured is unable to get his hands on the goods: there is no requirement that the goods must have been physically degraded.²² This means that if the goods have been captured by pirates and the assured is unable to get hold of them, the assured is “deprived” according to CICG § 35 no. 2. This deprivation is, however, subject to a qualification: the assured must have been deprived of the consignment “with no possibility of retrieving it”. This qualification is discussed further below.

4.3 When to assess the possibility of recovery

CICG § 35 no. 2 requires the assured to be deprived of the cargo “with no possibility of retrieving it”. Apparently the timing for assessing the possibility of recovery is tied to the point in time at which the assured was deprived of the cargo. If the cargo has been captured by pirates, it will normally be in physical existence. If, however, the pirates have escaped and either the pirates’ whereabouts is unknown or the retaking of the vessel by State authorities is impossible due to the risk to the crew,

²¹ See also the Commentary at p. 55.

²² Commentary p. 55.

there will be no immediate possibility of retrieving the cargo. If the assessment is tied to the point in time of the capture, this may imply that a total loss will be established immediately.

The Commentary, however, seems to presume that deprivation is not sufficient if the fate of the cargo at the time of capture is uncertain.²³

“No demand may be made for certain knowledge that the assured will not retrieve the consignment at some future date. If the assured has been deprived of the consignment for a certain period of time and there are no definite indications that he will retrieve it, it must therefore be regarded as totally lost pursuant to this provision.

How long a period of time must have passed must be determined in each individual case, see also Section 31 of the Act relating to the Carriage of Goods by Road (CMR), which states that goods transported by road are to be regarded as totally lost if they are not delivered within 30 days after the agreed delivery date, or 60 days after the carrier took charge of them. See also Special Clause No. 2, which lays down that the goods shall be regarded as totally lost in the case of a delay of at least 30 days. This means that an assured person without such additional coverage must wait for at least that period of time before he can claim compensation for total loss, unless there are clear indications that he will never retrieve the goods. In evaluating individual cases, due account must be taken of the transport distance and the points between which the goods are to be transported.”

As there will always be a possibility that the ship and cargo will be re-delivered to the owner, the fate of the cargo at the time of capture will normally not be certain. This means that the cargo owner must normally wait until at least 30 days after the initial capture before making a claim for total loss. If the pirates make no ransom demand during this period, it becomes reasonable to presume that their intention is to steal the ship and cargo. Although this is not the normal way pirates operate, there is always the possibility they may want to use the captured ship as

²³ Commentary p. 55.

a mothership for launching future pirate attacks. In such cases, the assured should be able to claim for total loss. But until at least this 30-day period has expired, the assured will have to “wait and see”.

This interpretation is also supported by policy considerations. An assured who could claim for total loss from the time of initial capture would be able to speculate against his insurer. If the value of the cargo were to rise, he would gain by not making a claim. If, on the other hand, the value were to fall, the assured would gain by making a claim which would be to the insurer’s detriment. There is no reason to provide the assured with such an opportunity to make a gain to the detriment of the insurer.

The position on this issue has been somewhat unclear in English law. It has been argued that capture by pirates automatically constitutes an actual total loss since it follows that the insured has neither the possession of the vessel nor the means of obtaining it. The basis for this claim is the old English case *Dean v Hornby* from 1854.²⁴

An insured ship was captured by pirates in December 1851 in the Straits of Magellan. In January 1852 she was recaptured by an English war steamer. A prize master took the command, and brought her to Valparaiso. The owner received information about the situation about the end of April 1852. They gave notice of abandonment to the underwriters, stating that intelligence had arrived “of the condemnation at Valparaiso” of the vessel “as a prize to Her Majesty’s steamer.” The underwriters refused to accept. The vessel was sent home by the recaptors from Valparaiso, under the command of a prize master, with instructions to proceed to Liverpool, and obtain an adjudication in the Court of Admiralty. She met with bad weather, and put into Fayal on 19th August 1852, where she was sold by the prize master, being then in a state not justifying the sale.

²⁴ *Dean v Hornby* (1854) 3 El & Bl 180. Jonathan Gilman and Robert Merkin *et al*, in *Arnould’s Law of Marine Insurance and Average*, 17th ed, London 2008, para 28-03 note 9, argue that this is “doubtful”, and that as “a general rule, the loss cannot immediately be said to be irretrievable in a case of capture or similar perils; the better view appears to be that capture results immediately in a constructive rather than an actual total loss.”

The court found that the assured was entitled to claim for total loss, stating “in December 1851 she is taken by pirates. Then, in fact, a total loss has occurred. After that, she never is restored to the owners; nor have they had an opportunity of regaining possession. They have lost the possession by events over which they have no control, and therefore are entitled to the indemnity for which they have paid. The cases referred to establish this principle: that, if once there has been a total loss by capture, that is construed to be a permanent total loss unless something afterwards occurs by which the assured either has the possession restored, or has the means of obtaining such restoration. The right to obtain it is nothing: if that were enough to prevent a total loss, there never would in this case have been a total loss at all; for pirates are the enemies of mankind, and have no right to the possession.”

In *Masefield v Amlin*, however, the court found that because the claim in *Dean v Hornby* was advanced in respect of a constructive total loss (CTL), rather than an actual total loss (ATL), the judgment was not decisive for an ATL claim.²⁵

Masefield v Amlin concerned the seizure by Somali pirates on 19 August 2008 of the chemical/palm oil tanker *Bunga Melati Dua* (“the vessel”) while transiting the Gulf of Aden en route from Malaysia to Rotterdam. The vessel, together with her crew and cargo, was taken to Somali waters. The assured was the owner of two parcels of bio-diesel which had been shipped on board the vessel. The two parcels were insured under an open cover contract which covered loss by piracy. Soon after the seizure, negotiations commenced between the pirates and the owners of the vessel (“MISC”), a state-owned Malaysian company, with a view to obtaining the release of the vessel, cargo and crew. During the course of these negotiations (and about a month after the vessel had been seized), the assured served a Notice of Abandonment on the insurer. This was declined, but the parties entered into an

²⁵ The Norwegian system does not make an equivalent distinction between an ATL and a CTL, but rather defines the concept of “total loss” through four listed criteria for establishing the existence of a total loss. Accordingly the CICG do not contain any counterpart to the English concept of a CTL.

agreement that proceedings should be deemed to have commenced on 18 September 2008. About 10 days later, MISC paid a ransom to the pirates and the vessel was released shortly thereafter together with her crew. The vessel arrived at Rotterdam on 26 October, where the cargo was discharged.

The assured referred to *Dean v Hornby* in claiming, *inter alia*, that upon the capture of the vessel by the pirates and its removal into Somali waters the cargo had become an ATL in accordance with the provisions of section 57(1) of the *Marine Insurance Act 1906* because the assured had been “irretrievably deprived” of the cargo.

The court, however, concluded that *Dean v Hornby* concerned a case of CTL (see paragraph 40 of the judgment), where the principle was that “the assured should not be obliged to wait till he had definitely ascertained whether his ship had been recaptured or not” (paragraph 47). By contrast, where the assured was deprived of possession in a case of ATL, a “wait and see” approach should be adopted in order to ascertain if and when a total loss actually occurred (paragraphs 48-51).

This interpretation of the expression “irretrievably deprived” seems to correspond to the presumption in the Norwegian Commentary: it is not sufficient for the assured to be deprived of the goods, he must wait and see whether there is a chance of recovery. However, policy considerations do not form any part of the argumentation in the English case. Rather, the judge analyses the proposition from *Dean v Hornby* that there is an ATL, because the “insured has neither the possession of the vessel nor the means of obtaining it”, as well as the distinction between an ATL and a CTL in the light of several court cases.²⁶

The common conclusion under both the Norwegian and English systems therefore appears to be that the assured must “wait and see” if the pirates demand ransom in return for redelivering the ship with cargo and crew. In this case, the next issue to consider is the assessment of the possibility of recovery of the cargo.

²⁶ The judgment in *Masefield v Amlin*, paras 38-52.

4.4 An objective or subjective assessment?

The issue here is whether the possibility of retrieving the cargo should be assessed objectively, or whether any such possibility must be considered to lie within the control of the assured. As the cargo is being transported by ship, and as such is beyond the control of the assured, the assumption seems to be that the possibility must be evaluated objectively. This interpretation is supported by the judgment in *Masefield v Amlin* in relation to the similar expression “irretrievably deprived” in section 57 (1) of the MIA and in the English cargo conditions:

The issue was whether the assured on 18 September 2008 was “irretrievably deprived” of the cargo. The judge states (in paragraph 29) that the “test is objective and is to be assessed on the true facts as at that date whether or not known or apparent to the assured: *Marstrand Fishing Co Ltd v Beer* (1936) 56 Ll. L. Rep. 163.”

4.5 Information relevant to the assessment

On the assumption that the assessment will be objective, the next issue concerns the nature of information that may be relevant. An obvious starting point is to look at how the parties involved – the shipowner, the cargo owner, the insurer *etc.* – evaluated the situation. If any of the parties are engaged in negotiations with the pirates in an attempt to retrieve the vessel, general information and more specific research about the likelihood of success of such negotiations should be relevant. Further, if the ship and cargo as a matter of fact are redelivered, this may be argued to lend weight to a view that recovery was likely, even if actual recovery occurred after the initial assessment was made. For example, in paragraph 29 in the *Masefield v Amlin* judgment, the judge considers the correlation between the evaluation of the probability of retrieving the cargo and the actual recovery:

“Although the actual fact of recovery within a short period is not directly material let alone decisive the court is entitled to consider what in fact happened after the relevant date as this “may assist in

showing what the probabilities really were, if they had been reasonably forecasted”: see *Bank Line, Limited. v Arthur Capel and Company* [1919] A.C. 435 per Lord Sumner at p 454.”

Further, paragraph 30 summarises the relevant information as follows:

“The material set out above demonstrates:

i) Both the contemporaneous correspondence and the information in the public domain showed that all interested persons (including the Claimant) were fully aware that the cargoes were likely to be recovered.

ii) This is entirely consistent with the unchallenged expert evidence.

iii) Other vessels seized by Somali pirates had been promptly released following negotiations over a relatively short period.

iv) Indeed the vessel and cargo were safely recovered only 11 days later upon payment of a ransom representing a tiny proportion of the value of the ship and cargo.”

4.6 What degree of impossibility is “no possibility”?

The next issue to consider is how unlikely recovery must be in order to conclude that there is “no possibility” of retrieving the cargo. “No possibility” means that retrieving it is impossible. If the cargo is sold to a third party or physically destroyed, it will be impossible to retrieve it. Broadly speaking, however, if it is legally and physically possible to recover the cargo, recovery is not impossible. This view conforms to that stated in *Masefield v Amlin* at paragraph 31. The consequence of this view is that the amount of ransom claimed or paid is not decisive: as long as there is any possibility of recovery against payment, there is no total loss.

Should, however, we interpret the requirement for there to be “no

possibility” of retrieving the cargo more narrowly? That is, should the “possibility” of retrieving the cargo be viewed in the context of the resources required to achieve this goal? From an economic perspective, it makes no sense to pay more than the cargo is worth to recover it. If the cargo owner had to pay the costs of recovery and the insurer only become liable once recovery proved impossible, this could create a conflict of interests between the two parties. However, payments to achieve the recovery of cargo that has been captured and is in danger of becoming a total loss will normally qualify as salvage measures to be covered by the insurer.²⁷ Seen within this framework, it seems appropriate to interpret the provision in accordance with its wording.

This also seems to conform to the general view in English law. The judge in *Masefield v Amlin* (paragraph 32) stated that “an assured is not irretrievably deprived of property if it is legally and physically possible to recover it (and even if such recovery can only be achieved by disproportionate effort and expense)”. This statement is supported by references to previous English court practice.²⁸

4.7 Is the possibility to pay ransom sufficient to make recovery “possible”

The wording “no possibility of retrieving” is unqualified with regard to measures that may be taken in order to retrieve the cargo. Thus the natural interpretation is that there is no total loss if payment of ransom makes recovery of the cargo possible.

It may, however, be argued that ransom payments are procured through the use of threats, and as such it is illegal or unfair to consider such measures when assessing whether there is a total loss. Under Norwegian law, we need to consider whether this interpretation is contrary to NL 5-1-2 (agreements that are against the law are invalid), or § 36 of

²⁷ CIGG §§ 39 and 40.

²⁸ *George Cohen, Sons & Co v Standard Marine Insurance Co* (1925) 21 Ll. L. Rep. 30, *Panamanian Oriental Steamship Corporation v Wright* [1970] 2 Lloyd’s Rep. 365, *Fraser Shipping Ltd v Colton* [1997] 1 Lloyd’s Rep. 586

the Contract Act²⁹ (agreements that are unfair do not have to be fulfilled).

NL 5-1-2 provides that agreements that contravene the law or morality (“*ærbarhet*”) are void. The insurance agreement and the clause defining the total loss are clearly not illegal. Nor is it illegal to pay ransom to pirates according to Norwegian criminal law. There is, however, also a presumption that the provision will apply to an agreement that is acceptable legally if the agreement is linked to an illegal “main element”.³⁰ The illegal element here would be the capture of the ship and the demand for ransom. However, these factors are only relevant to the assessment of total loss in certain circumstances – they cannot be characterised as a “main element” in relation to the cargo insurance as a whole. It can also be argued that, even if the capture itself is illegal, the necessity of the ransom payment in order, *inter alia*, to recover the crew, makes the payment a morally desirable – rather than an immoral – act. As the application of the rule would render the whole insurance void, it is difficult to see that this limited and remote illegal element should have such a draconian result.

§ 36 of the Contract Act states that a contract may be wholly or partially set aside if it is unfair. Relevant factors for the assessment of fairness include: the circumstance under which the contract was concluded; the position of the parties; the content of the contract; and subsequent developments. Here the question is whether it is unfair to consider payment of ransom as relevant to the definition of total loss. If so, this factor should be set aside. This would make the insurer liable for total loss regardless of the possibility of recovery through payment of a ransom. It is difficult to see that recovery in return for payment of a ransom is an unfair factor when assessing whether there is a total loss. The only consequence for the cargo owner is that he will have to wait and see what happens. If the cargo has been lost or damaged as a result

²⁹ Act 31 May 1918 no 4 on contracts.

³⁰ Knut Selmer, “Skadeforsikring og ulovlig virksomhet”, *Lov, dom og bok*, Festskrift til Sjur Brækhus, Editor Thor Falkanger, Oslo 1988, pp. 467-481, pp. 476-478 with further references.

of the capture, he will be compensated. The declaration of a total loss regardless of the possibility of recovery will, on the other hand, enable the cargo owner to speculate against the insurer and make a claim if the cargo's value declines. This is contrary to considerations of fairness.

And even if the value does not go down, the cargo owner may get compensation regardless of any loss. In this case, the insurer would be entitled to take over the cargo to compensate for the total loss payment. But as the cargo owner is the professional party in relation to handling the cargo, this shift in possession does not seem to be an efficient or fair solution. It has also been accepted that payment of ransom is covered by the York Antwerp rules and comes within the general average settlement under the insurance.³¹ It seems inconsistent for ransom payments to be covered according to one part of the conditions but to be disregarded as unfair under another.

The English equivalent to this evaluation is whether the payment of ransom is contrary to public policy. This issue was addressed in *Masefield v Amlin*, as the assured argued that even if the payment of a ransom was not illegal, it was contrary to public policy. Accordingly the ability to recover property by payment of a bribe should not be treated as relevant or appropriate when considering whether a vessel and her cargo were in practice irretrievable. The judge, however, did not agree.

The judge started (at paragraph 59) by referring to Lord Atkin in *Fender v St John Mildmay* [1938] AC 1:

“the doctrine should only be invoked in clear cases in which the harm to the public is substantially incontestable, and does not depend upon the idiosyncratic inferences of a few judicial minds.”

The judge found that the payment could not be categorised as contrary to public policy, due to the following arguments (paragraph 60):

“i) The payment of ransom is not illegal as a matter of English law [...].

³¹ Wilhelmssen 2009 p. 207.

ii) Circumstances have arisen where legislative action has intervened to make such payments illegal: see e.g. the *Ransom Act 1782*. The courts should refrain from entering into the same field.

iii) So far as harm is concerned it is true that payments of ransom encourage a repetition, the more so if there is insurance cover: the history of Somali piracy is an eloquent demonstration of that. But if the crews of the vessels are to be taken out of harm's way, the only option is to pay the ransom. Diplomatic or military intervention cannot usually be relied upon and failure to pay may put in jeopardy other crews."

The judge concludes that in "short the 'balance of convenience' is far from clear cut. In these circumstances with no clear and urgent reason for categorising the activity as contrary to public policy the court should resist any temptation to enter the field." A different solution would also imply that kidnap and ransom cover, which has been a long-standing and important feature of the insurance market should be rendered unenforceable (paragraph 62) and would be contrary to the majority's view in *Royal Boskalis Westminster NV v Mountain* [1999] QB 674, where payment of ransom was accepted as a sue and labour expense (paragraph 63).

Thus, even if the approach in the English system is different from the Norwegian, the argumentation appears to be similar.

5 Some reflections

In general the English and Norwegian solutions on the issue of total loss in the case of capture by pirates are very similar, even if the systems do take somewhat different approaches. One difference is the English distinction between a CTL and an ATL. This distinction is not found in the Norwegian system, where total loss is treated as a common denominator for four listed situations in which the cargo has been lost. This seems to correspond with a more general view on the different European total

loss clauses, that even if there seems to be a lack of formal harmonisation this does not have any practical consequences for actual settlements.³² Another difference is the question of the acceptability of ransom payments as an element in the total loss evaluation. This question is resolved through different legal approaches, but apparently with the same result.

The CICG and the English regulation both seem to provide an appropriate solution on this issue. Several countries have chosen to convert delay for a certain number of days into total loss. The shortest period is provided for in the Swedish and Finnish clauses, where total loss is established once the cargo has been delayed for more than 60 days.³³ This would not have resulted in a total loss in *Masefield v Amlin*, but other pirate seizures have taken longer to resolve. A recent example is that of *The UBT Ocean*, which was released after 136 days. In such cases, the Swedish and Finnish conditions would result in a total loss settlement for the cargo, even if it was ultimately recovered undamaged. This solution does not seem appropriate.

³² Johansson p. 433.

³³ Allmänna villkor för transportförsäkring av varor 2000 12.6, Johansson p. 434-435.

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