Who Pays the Pirates?: *Herculito Maritime Ltd v Gunvor International BV* [2024] Bus LR 580; [2024] UKSC 2

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Introduction

In *Herculito Maritime Ltd v Gunvor International BV*[1] the Supreme Court of the United Kingdom considered insurance funds and the incorporation of charterparty terms into bills of lading in a striking factual context. The matter ultimately at issue was: who pays the ransom for freeing a ship that had been seized by Somali pirates?

Facts and Procedural History

The *MT Polar* was captured by pirates on 30 October 2010 in the Gulf of Aden on a voyage from St Petersburg to Singapore laden with a cargo of fuel oil. She was released ten months later after the shipowner paid a random of US$7,700,000.[2] Most of the cargo was intact.[3] The Gulf of Aden is a 'High Risk Area' for the purpose of marine insurance. The shipowner had taken out Kidnap and Ransom insurance before entering the area.[4] The shipowner declared general average.[5] The ransom formed a major part of what was claimed.[6] The general average adjustment concluded that the cargo interests should pay US$4,829,393.22.[7]

The cargo interests contended that they were not liable for the ransom payment.[8] This claim was upheld by a panel of arbitrators (Timothy Young QC, Dominic Kendrick QC and Simon Gault).[9] However, this decision was overturned on appeal by Sir Nigel Teare in the Admiralty Court.[10] The Court of Appeal (Peter Jackson and Males LJJ and Sir Patrick Elias), in a judgment delivered by Males LJ, dismissed the cargo interests' appeal.[11] The cargo interests appealed again to the Supreme Court. Their appeal was dismissed in a judgment delivered by Lord Hamblen (with whom Lord Hodge, Lord Leggatt, Lady Rose and Lord Richards agreed).

Contractual Provisions

The case turned on the interpretation of the voyage charterparty and the bills of lading. The charterparty contained a Gulf of Aden clause.[12] The third paragraph of this clause stated:

> Any additional insurance premia (including, but not limited to, those in respect of H&M, crew, P&I kidnap risks and ransoms), crew bonuses (which to be in accordance with the international standard) shall be for chrtrs account. Max USD40,000 for charterer's account for any additional insurance premium except for crew bonus which to be max USD20,000 for charterers account.[13]

The charter also contained a war risks clause, which 'provided that any additional premia payable in respect of war risks incurred by reason of the vessel trading to excluded areas not covered by the shipowner's basic war risk insurance were to be for charterer's account'.[14]

Clause 39 of the BPVOY 4 standard form of tanker voyage charterparty was incorporated into the charterparty and was to the following effect:

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[1] *Herculito Maritime Ltd v Gunvor International BV* [2024] Bus LR 580; [2024] UKSC 2 ('Supreme Court Decision').
[2] Ibid [1].
[3] Ibid [12].
[4] Ibid [9].
[5] Ibid [13].
[6] Ibid [2].
[7] Ibid [14]. At [2] Lord Hamblen said that the figure was US$5,914,560.75, but this appears to be an error as it is inconsistent with the figures in the lower court judgments as well as with that given at [14]. All the other figures are in agreement.
[8] Ibid [15].
[9] Ibid [5].
[10] *Herculito Maritime Ltd v Gunvor International BV* [2020] EWHC 3318 (Comm); [2021] 1 Lloyd's Rep 150 ('Trial Decision').
[11] *Herculito Maritime Ltd v Gunvor International BV* [2021] EWCA Civ 1828; [2022] 1 Lloyd's Rep 375 ('Court of Appeal Decision').
[12] Supreme Court Decision (n 1) [16].
[13] Ibid [17].
[14] Ibid [18].

(i) Pursuant to clause 39.2 the Owners were entitled to cancel the charter if, at any time before the vessel commences loading, it is considered that performance of the contract of carriage may expose the vessel to war risks.
(ii) Pursuant to clause 39.3, the Owners were not required to continue to load or to sign bills of lading or to proceed or continue on a voyage where it appeared that the vessel may be exposed to war risks. If it should so appear the Owners were entitled to request the Charterers to nominate a safe port for the discharge of the cargo. If within 48 hours the Charterers failed to nominate such a port, Owners were entitled to discharge the cargo at any safe port of their choice in complete fulfilment of their obligations under the charter. The extra expenses of such discharge were payable by the Charterers.
(iii) Pursuant to clause 39.4, if, at any stage of the voyage, it appeared that the vessel may be exposed to war risks on any part of the route and there is another longer route to the discharge port, Owners were entitled to give notice to Charterers that this route should be taken. The extra expenses of such route, if the extra distance exceeded 100 miles, were payable by the Charterers.
(iv) Pursuant to clause 39.5, the Owners were at liberty to comply with the orders of identified third parties.
(v) Pursuant to clause 39.6, anything done or not done in compliance with the clause shall not be a deviation.[15]

There were six bills of lading for the various cargo.[16] All had words of incorporation stating that they were 'pursuant and subject to all terms and conditions, liberties and exceptions as per TANKER VOYAGE CHARTER PARTY indicated hereunder, including provisions overleaf'.[17] One bill of lading also stated: '[a]ll terms and conditions, liberties and exceptions of the Charter Party, dated as overleaf, including the Law and Arbitration Clause are herein incorporated.'[18] The bills of lading provided: '[b]y taking delivery of the cargo the Consignee shall make himself liable for unpaid freight, deadfreight, demurrage and other charges.'[19] All the bills of lading contained 'general average clauses' providing for general average to be settled in accordance with the York-Antwerp Rules 1974 (or the 1994 Rules in the case of one bill of lading).[20]

The Insurance Fund Issue

Parties to a contract may agree that particular loss or damage will be covered by insurance, rather than the other party.[21] In a shipping context this is known as an 'insurance fund' or 'insurance code'.[22] An insurance fund was held to exist in relation to a demise charter by the Supreme Court in *The Ocean Victory*[23] and in relation to a time charter by the House of Lords in *The Evia [No 2]*.[24] But this was the first case where there was an insurance fund in a voyage charter.

Lord Hamblen drew several propositions from *The Ocean Victory*.

- '[W]hether or not the parties have agreed an insurance code or fund is a matter of construction of the contract … It is the necessary consequence of the contractual scheme which has been agreed rather than of any express words which have been used. As such, it is akin to a necessarily implied term and involves a similarly high threshold.'[25]
- '[J]oint names insurance is clearly a powerful factor in favour of there being an insurance code or fund', but it is not decisive.[26]
- There is no prima facie position that 'where a contract requires a party to that contract to insure should be that the parties have agreed to look to the insurers for indemnification rather than to each other.'[27]

In *The Evia [No 2]*, Lord Roskill identified four features of the time charter which supported his conclusion that there was an insurance fund.

[15] Ibid [19], citing Trial Decision (n 10) [9].
[16] Supreme Court Decision (n 1) [21].
[17] Ibid [22].
[18] Ibid [23].
[19] Ibid [25].
[20] Ibid [26].
[21] Ibid [29].
[22] Ibid [30].
[23] *Gard Marine and Energy Ltd v China National Chartering Co Ltd* [2017] UKSC 35 ('*The Ocean Victory*').
[24] *Kodros Shipping Corp of Monrovia v Empresa Cubana de Fletes* [1983] 1 AC 736 ('*The Evia [No 2]*').
[25] Supreme Court Decision (n 1) [37].
[26] Ibid [40].
[27] Ibid [41]–[42].

> First, clause 21 (A) gives the owners an unqualified right to refuse to accept orders for the ship to go or to continue to any place or on any voyage or to be used in any service which will subject her to any of the dangers to which this sub-clause refers. Secondly, under clause 21 (B) the owners can, in the circumstances there prescribed, insure the ship and charge the premiums to the time charterers. Thirdly, notwithstanding the off-hire clause (clause 11 (A)) the ship is to stay on-hire in the circumstances predicated in clause 21 (B) (2). Fourthly, whereas clause 2 bears the rubric 'trade', clause 21 bears the rubric 'war' and it is permissible to consider these rubrics when construing these various clauses.[28]

Lord Roskill also observed that the charterers paid the insurance premia and it would be a 'remarkable result' if they obtained no benefit from it.[29] But Lord Hamblen said that other cases 'make it very clear that the mere fact that charterers pay an extra insurance premium is not enough to create an insurance code or fund.'[30]

Lord Hamblen stated that several general considerations were relevant when considering whether there was an insurance fund in this case.

(1) General average is a common law right, albeit one regulated by the contract. For the shipowner to be held to have given up such a valuable right in relation to well-known kidnap and ransom risks requires a clear agreement to that effect.
(2) To establish that the parties have agreed an insurance code or fund it has to be shown that this is a necessary consequence of what has been agreed—that is a high threshold.
(3) This is not a case of joint names insurance.
(4) There is no principle exempting charterers from liability for their breaches of contract or in general average merely on the ground that they have directly or indirectly provided the funds whereby the owners insured themselves against the relevant loss or damage.[31]

The cargo interests submitted that the clause in this case was materially indistinguishable from that in *The Evia [No 2]*. They argued that the shipowner had sweeping rights to cancel or substantially vary the performance of the charter in the event of war risks,[32] but Lord Hamblen stated:

> [a]gainst the background of that specially agreed contractual regime for the known piracy risks of transiting the Gulf of Aden I do not consider that it would have been open to the shipowner to contend that such risks were 'war risks' for the purposes of clause 39. Having agreed the vessel's route and the terms upon which the Gulf of Aden would be transited neither the shipowner nor the master could then turn round and say that they had changed their mind and were no longer willing to take on the known piracy risk of transiting the Gulf of Aden on the terms agreed. If different war risks materialised in the Gulf of Aden or there was a change in the nature of the piracy risk, or a change in its degree sufficient to make it qualitatively different, then it may be that clause 39 could be relied upon, but not if there was no change in risk. In the present case there is no suggestion or finding that the piracy risk changed at any time from that known and contemplated at the time that the charter was agreed.[33]

As such, unlike in *The Evia [No 2]*, 'the shipowner did not have an "unqualified right" or "absolute veto" under clause 39 in relation to the transit of the Gulf of Aden'.[34]

Lord Hamblen thought that the charterers' obligations to pay an additional war risk premium was a less powerful factor in this case because it did not involve joint insurance.[35] In response to a submission based on Lord Roskill's 'remarkable result' language,[36] Lord Hamblen said

> this was premised upon [Lord Roskill's] conclusion that (1) the charterers would otherwise obtain no benefit from the payment of the additional premium and (2) they would do so in circumstances where

[28] *The Evia [No 2]* (n 24) 766B–C.
[29] Ibid 766D–E.
[30] Supreme Court Decision (n 1) [48], citing *St Vincent Shipping Co Ltd v Bock, Godeffroy & Co* [1980] 2 Lloyd's Rep 95 ('*The Helen Miller*'); *D/S Idaho v Colossus Maritime SA* [1984] 1 Lloyd's Rep 385 ('*The Concordia Fjord*'); *Pearl Carriers Inc v Japan Line Ltd* [1993] 1 Lloyd's Rep 508 ('*The Chemical Venture*').
[31] Supreme Court Decision (n 1) [57] (citations omitted).
[32] Ibid [59].
[33] Ibid [62].
[34] Ibid [68].
[35] Ibid [69].
[36] See *The Evia [No 2]* (n 24) 766D–F.

> they were undertaking a significant additional burden (in relation to the disapplication of the off-hire clause). For the reasons given above, neither consideration applies here. The charterer obtains the significant benefit of being entitled to transit the Gulf of Aden on the terms specially agreed notwithstanding the wide rights which would otherwise arise under clause 39. Further, there is no obligation assumed by the charterer equivalent to that in relation to hire under clause 21(B) of the Baltime form.[37]

His Lordship concluded that the terms of the charter were materially different from that in *The Evia [No 2]* and that case should be distinguished.[38] Lord Hamblen cautioned against following *The Evia [No 2]* in cases involving differently worded charters. His Lordship gave several reasons for this.

> (1) English commercial law in general and shipping law in particular recognises the importance of certainty and predictability and fosters it so far as it can.
> (2) Leaving aside cases of joint insurance such as *The Ocean Victory*, the search for an insurance code or fund in a charterparty necessarily introduces uncertainty. No express code or fund has been established and it is a question of seeking to infer it from a consideration of the charterparty terms as a whole. This is a difficult exercise which is likely to require the input of lawyers, if not arbitration or mediation.
> (3) If parties wish to provide that there be no right of recovery or subrogation in respect of loss or damage covered by insurance that can be easily stated—as clause 13 of the Barecon 89 form illustrates.
> (4) The practical difficulties which may arise are illustrated by a consideration of the position of insurers. Whether or not they are to have rights of subrogation is likely to be material to their rating of the risk as it increases the risk of loss borne by them. Disclosure may, however, give rise to difficult issues. For example, it may be very unclear whether the subrogation position is known to the insured in circumstances where it all depends upon implications to be drawn from the terms of the charter. Similarly, if disclosure is sought to be met by providing a copy of the charter, whether that is full and fair disclosure must be questionable in circumstances where it says nothing expressly about subrogation rights. If no effective insurance cover were provided then issues would arise as to whether in such a case there is any code, and difficult questions might also arise if the insurance did not fully cover the losses suffered by the shipowner.[39]

Incorporation into the Bills of Lading

While the resolution of the first issue meant that the cargo interests' appeal must fail, Lord Hamblen went on to consider further issues related to whether the insurance fund was incorporated into the bills of lading. He did so on the assumed basis that there was an insurance fund.[40] Lord Hamblen quoted with approval the summary of the law on the incorporation of charterparty terms into bills of lading contained in *Scrutton on Charterparties and Bills of Lading*:

> (1) The incorporating clause in the bill of lading must be construed in order to see whether it is wide enough to bring about a prima facie incorporation of the relevant term. General words of incorporation will be effective to incorporate only those terms of the charterparty which relate to the shipment, carriage or discharge of the cargo or the payment of freight. Which of those terms are incorporated into the bill depends on the width of the incorporating provision. Where specific words of incorporation are used, they are effective to bring about a prima facie incorporation even if the term in question does not relate to shipment, carriage or discharge, and even if some degree of manipulation is required. Further, on the modern approach, specific words of incorporation in the bill of lading may be sufficient to incorporate a term in the charterparty which it was clearly intended to incorporate, even if the term does not literally fall within the incorporating words, if it is clear that something has gone wrong with the language. Where the intention is doubtful, the court will not hold that the term is incorporated. If the incorporating clause in the bill of lading is not wide enough of its own to bring about a prima facie incorporation of the relevant term, then (semble) it will not be permissible to have regard to the terms of the charterparty in order to effect an incorporation which would otherwise fail.
> (2) If it is found that the incorporating clause is wide enough to effect a prima facie incorporation, the term which is sought to be incorporated must be examined to see whether it makes sense in the

[37] Supreme Court Decision (n 1) [72].
[38] Ibid [73].
[39] Ibid [74].
[40] Ibid [75].

context of the bill of lading; if it does not, it must be rejected. This process should be performed intelligently and not mechanically, and must not be allowed to produce a result which flouts common sense. Where the term relates to shipment, carriage or delivery, some degree of manipulation is permissible to make its words fit the bill of lading, but not where the term relates to other matters. Where the intention to incorporate a specific clause is particularly clear, a greater degree of manipulation will be permitted.

(3) Where there is an incorporation which is prima facie effective, the term in question must be examined to see whether it is consistent with the express terms of the bill. If it is not, it will be rejected, although terms of the charterparty which are not incorporated for this reason may nevertheless negate the implication of terms which might otherwise be implied into the bill of lading.[41]

His Lordship endorsed Males LJ's statement in the Court of Appeal judgment that these steps 'should not be too rigidly applied' and that conclusions reached at each stage of the process were provisional.[42]

Lord Hamblen made several general comments on incorporation of charterparty terms.

- '[W]hat matters are the incorporating words in the bill of lading, not provisions relating to incorporation which may be found in the charter. If the incorporating clause in the bill of lading is not sufficient to incorporate the provision in question, then that is the end of the inquiry.'[43]
- The rule 'that general words of incorporation only incorporate provisions of the charter which are "germane" to the shipment, carriage and delivery of the goods, or the payment of freight, under the bill of lading … excludes ancillary agreements such as an arbitration clause or a jurisdiction clause', as well as 'provisions which are inapplicable in the bill of lading context (such as provisions which relate to the approach voyage or to matters after the completion of discharge) and provisions which make no sense in the bill of lading context (such as provisions relating to hire if the relevant charterparty is a time charter)'.[44]
- '[W]here specific words of incorporation are used a degree of manipulation of the relevant clause in the charterparty will be appropriate so as to give effect to the parties' expressed intention'.[45]
- '[W]here general words of incorporation are used some degree of manipulation may be permissible of terms which directly relate to shipment, carriage and delivery of the cargo, or the payment of freight, in order to make the wording fit the bill of lading but there is no rule of construction to this effect'.[46]

Lord Hamblen also rejected the suggestion, which was not pressed in oral submissions, that the case law on this subject was 'dated' and should be updated in light of modern case law on contractual interpretation.[47]

His Lordship considered that the bill of lading did incorporate the parts of the war clauses relating to insurance, as they 'relate to the route to be taken by the vessel and therefore are directly relevant to the carriage'.[48] It could not be intended that the liberties given to the shipowner relating to war risks were incorporated, but not provisions that limited or qualified them: 'The intention must surely be to incorporate the entirety of the relevant contractual regime set out in the charter rather than to do so partially or incompletely.'[49] The whole of the Gulf of Aden clause and the War Risk clause, including the charterer's obligation to pay insurance, were therefore incorporated into the bills of lading.[50]

However, Lord Hamblen rejected the argument that, if an insurance fund existed, the shipowner would be precluded from claiming against the bill of lading holders for losses covered by the insurance fund. The obligation to pay the insurance premia was on the charterer, not the bill of lading holders. As they had not paid for the insurance, it would not be a 'remarkable result' for the shipowner to be able to claim against them.[51]

[41] Ibid [77], quoting David Foxton et al, *Scrutton on Charterparties and Bills of Lading* (Sweet & Maxwell, 24th ed, 2020) [6-016]–[6-018].
[42] Supreme Court Decision (n 1) [78], quoting Court of Appeal Decision (n 11) [34].
[43] Supreme Court Decision (n 1) [81].
[44] Ibid [82]–[84].
[45] Ibid [85].
[46] Ibid [86].
[47] Ibid [87].
[48] Ibid [89].
[49] Ibid.
[50] Ibid.
[51] Ibid [93].

His Lordship concluded that there was no basis to manipulate the wording of the bills of lading to make the holders of the bills lading liable for the insurance premia. It was not 'necessary to do so in order to make the wording fit the bill of lading'.[52] Indeed there were reasons against doing this.

> If the holders of the bills of lading are liable to pay the insurance premia the basis of that liability vis a vis the shipowner and each other is wholly unclear. Is each bill of lading holder liable for the full premia? If not, is its liability proportionate and, if so, is it proportionate to the quantity of the cargo covered by the bill of lading or its value? If a bill of lading holder pays the insurance premia what are its recourse rights against other bill of lading holders and how are they to be enforced? All of these issues arise in the context of putative bill of lading holders who might be a holder for different parcels of cargo for different lengths of time and only for a period if the cargo is traded afloat.[53]

Comment

The Supreme Court clearly wanted to confine the application of insurance fund doctrine in the interests of commercial certainty. Insurance funds seem unlikely to be found to exist, at least in the shipping context, outside cases of joint names' insurance. Lord Hamblen stressed the high threshold of an insurance fund being a necessary implication of the agreed terms of the charterparty.

His Lordship also stated that there needed to be 'clear agreement' that the shipowner was giving up the valuable right of general average.[54] Presumably he did not mean express agreement by this, as the insurance fund doctrine is one of necessary implication. Rather he was emphasising the degree of clarity required for a necessary implication.

While *The Evia [No 2]* was distinguished rather than overruled, Lord Hamblen was unmistakably sceptical of it. The caution against relying on it in cases of clauses with different wording effectively confines it to its facts. Unless a charterparty is truly indistinguishable in wording from that in *The Evia [No 2]*, an argument based on it is unlikely to succeed.

The Supreme Court's treatment of the war risk clause in relation to the risk of piracy in the Gulf of Aden is of particular interest given the volatile global situation. It seems reasonable to say that when a risk has been specifically contemplated and provided for in the charterparty, as the risk of piracy was in the Gulf of Aden clause, the shipowner cannot rely on a general war risk clause to refuse to undertake that risk. This is simply the result of reading the clauses together, so the one clause does not undermine the other and the intention of the parties is not frustrated.

However, the position is less clear when there is a change in the risk after the charterparty was entered into. Lord Hamblen acknowledged the possibility that the position might be different in this situation but appeared to envisage a high bar for this: 'a change in the nature of the piracy risk, or a change in its degree sufficient to make it qualitatively different'.[55]

It is not clear what a risk being 'qualitatively different' means or just how much it must increase in order to meet this threshold. It would seem simpler to say that, where there is a material increase in risk, the shipowner's rights under the war risk clause are applicable. This would be a principled approach where the war risk clause cannot be relied upon in relation to existing risks that have been specifically provided for but can be relied on if the risk becomes materially greater than when it was provided for in the charterparty.

What a change in the nature, as opposed to the degree, of the piracy risk means could also be open to argument. This might apply if, for instance, a risk to the life of the crew from piracy emerged that had not previous existed. Presumably a risk to life is of a different nature to a risk to property.

Lord Hamblen confirmed that, when considering whether charterparty terms are incorporated in the bill of lading, it is the wording of the bill of lading, not the charterparty, that is relevant. Generally speaking, this must be correct. Terms from one contractual document can only be incorporated in another contractual document if the latter document incorporates them, not because the former document envisages their interpretation. However, that the

[52] Ibid [97].
[53] Ibid [98].
[54] Ibid [57].
[55] Ibid [62].

charterparty envisages incorporation might be relevant if the words of the bill of lading are ambiguous, as it could be seen as part of the surrounding context.

Lord Hamblen's rejection of any suggestion of modernising the case law on incorporation of charterparty terms is consistent with his emphasis on certainty: he quoted Bingham LJ's dictum from *The Federal Bulker* that 'it is preferable that the law should be clear, certain and well understood than that it should be perfect.'[56] But his Lordship is also correct that the doctrine is not a technical or rigid one. Indeed, its acknowledgement of the permissibility of 'manipulation' of terms in the charterparty to fit the bill of lading is consistent with the modern contextual and purposive approach to contractual interpretation.

Overall, the Supreme Court's judgment prioritises commercial certainty and restricts the application of the insurance fund doctrine outside the context of joint names' insurance.

[56] Ibid [87], quoting *Federal Bulk Carriers Inc v C Itoh & Co Ltd* [1989] 1 Lloyd's Rep 103, 105 (Court of Appeal) ('*The Federal Bulker*').