Alert 10-108

Parbulk AS v. Kristen Marine SA and Aurele Trading Inco

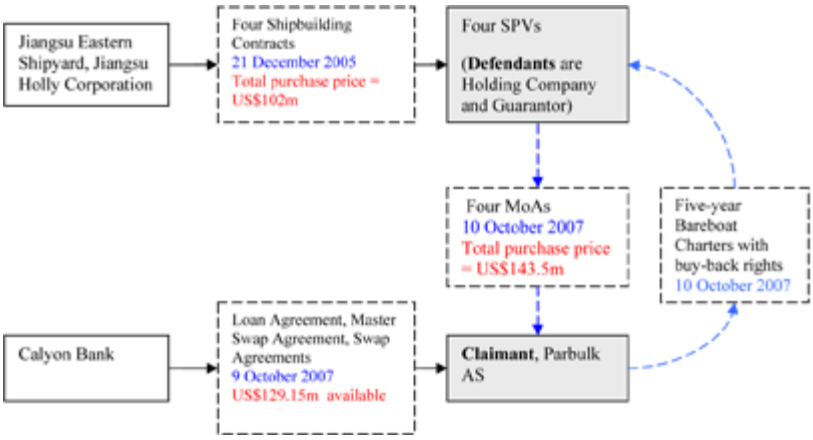
Ship sale and purchase – Clause 14 of Norwegian Saleform 1993

Introduction

This recent case gives guidance on the construction of Clause 14 of the Norwegian Saleform 1993 and also demonstrates how a simple amendment to the standard form can have far reaching consequences.

Background

The contractual matrix was as follows:



The Claimant had agreed to purchase four vessels "en bloc," from Special Purpose Vehicles ("SPVs") under four Memorandum of Agreements ("MoAs"), and then charter the vessels back to the SPVs. The finance for the purchase of the vessels by the Claimant came from Calyon Bank.

Construction of the vessels was delayed and the Claimant became entitled to, and did, cancel the MoAs. The subject of the dispute was the Claimant's entitlement to certain "expenses," which it argued fell within the scope of sentence (3) of Clause 14 of the MoAs. These "expenses" were significant:

(a) Sums flowing from the cancellation of the Loan Agreement and breaking of the Swap Agreements ("Swap Costs") with Calyon Bank. The Claimant calculated these sums to be US$15,185,647, the Defendants, US$14,335,647.

(b) "Out of Pocket Expenses" comprising a commitment fee of US$567,076 payable to Calyon, an arrangement fee payable to Calyon in the sum of US$774,900, and other expenses totalling US$521,105, making a total net claim of US$982,307.

Clause 14 of the MoAs was thus key to the dispute and is set out below. Amendments to the standard form Norwegian Saleform 93 are underlined. Mr Justice Burton numbered the sentences for ease of reference, and this is maintained below:

> *14. Sellers Default*

(1) Should the Sellers fail to give Notice of Readiness in accordance with Clause 5a) or fail to be ready to validly complete a legal transfer by [date for first vessel - 26 February 2009] the Buyers shall have the option of cancelling this Agreement provided always that the Sellers shall be granted a maximum of 3 banking days after Notice of Readiness has been given to make arrangements for the documentation set out in Clause 8. (2) If after Notice of Readiness has been given but before the Buyers have taken delivery, the Vessel ceases to be physically ready for delivery and is not made physically ready again in every respect by [26 February 2009] and new Notice of Readiness given, the Buyers shall retain their option to cancel subject to Clause 5c above. (3) In the event that the Buyers elect to cancel this Agreement the deposit together with interest earned shall be released to them immediately and Sellers shall pay the Buyer their proven expenses including, but not limited to, legal costs and breakage cost with the Buyer's lenders.

(4) Should the Sellers fail to give Notice of Readiness by [26 February 2009] or fail to be ready to validly complete a legal transfer as aforesaid they shall make due compensation to the Buyers for their loss and for all expenses together with interest 6 months Libor + 2% if their failure is due to proven negligence and whether or not the Buyers cancel this Agreement."

Mr Justice Burton resolved issues of liability in favour of the Claimant but left open the exact quantum of the Swap Costs and Out of Pocket Expenses. He ordered payment to the Claimant in the sums of US$14,335,647 and US$721,312.

Analysis

Several short points arise from the Judgment:

1. As a matter of construction, the remedies in sentence 3 of Clause 14 apply where the Buyer cancels on the basis of either of the first two sentences. That is a simple matter of construction.
2. The Defendants had pleaded a case that Clause 14 was an unenforceable penalty. This argument was not pursued at the hearing.
3. Sellers should be very careful in broadening the standard Clause 14 wording in relation to the Buyer's remedies if the MoA is cancelled. Here, the amendment had the consequence that the Defendant was liable for over US$15 million of "expenses," with Mr Justice Burton being satisfied that the Swap Costs were "breakage costs"; and even if he was wrong on that, then they were in any event "proven expenses," as were the Out of Pocket Expenses.

   Although holding the Defendants liable for more than US$15 million of expenses may, at first blush, appear unjust, there were good reasons on the facts as to why they should be so liable, relating to the overall scheme of the deal and the contemplation that such losses may arise. Whether the "expenses" were too remote and/or unreasonable fell to be considered against the overall factual matrix (Mr Justice Burton being unconvinced that this was a true indemnity and that all losses could be recovered).

   Sellers should be aware that a Buyer who has broadened the third sentence of Clause 14 to include "expenses" may use the Parbulk case to argue that it would be understood that this term would include, for example, Swap Costs, and claim accordingly.
4. The case can also be seen as illustrative of a growing trend to allow parties to recover hedging losses and costs (see further Reed Smith Alert 10-072).

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