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Defence Guides

Clause paramount in a nutshell

Introduction: what is a clause paramount?

A clause paramount incorporates the United States Carriage of Goods by Sea Act or the Hague/Hague Visby Rules ("the HV Rules") into a contract. Although the HV Rules were designed to regulate the legal relationship between carriers and shippers, and the same would usually be found in the reverse sides of bills of lading, the HV Rules can also be incorporated into charterparties.

For instance, a clause paramount can be found in the NYPE time charter form. As for voyage charterparties, such clauses are in the Asbatankvoy, Baltimore 1976, Amwelsh 1993 and Norgrain 1989 forms.

Provided that the charterparty (either voyage or time charterparty) makes it clear that the parties intended to incorporate a clause paramount into the charterparty, the English courts will give effect to that intention, even though this may involve manipulating the wording of the clause paramount and even though it may mean that some of the terms referred to in the clause paramount have to be ignored (see The Saxon Star [1959] AC 133).

Delivering the vessel to charterers at the beginning of the charterparty: how does the incorporation of a clause paramount affect owners' rights and obligations?

a. The condition of the vessel: an absolute obligation vs due diligence

Under English common law, the obligation on ship owners is to provide a seaworthy ship. This is unconditional and, on delivery of the vessel to charterers, owners will usually be liable, irrespective of fault, for any breach of the undertaking.

However, when a clause paramount incorporates the HV Rules into a charterparty, ship owners are only in breach of their duty if they fail, for example, to exercise due diligence to make the ship seaworthy before and at the beginning of the voyage. (see The Fjord Wind [2000] 2 Lloyd's Rep 191).

b. Under a clause paramount, how strict is owners' obligation of due diligence?

The notion of exercising due diligence entails two basic requirements. Firstly, ship owners must carry out any inspections, repairs or other preparations which, in the circumstances, a skilled and prudent ship owner would reasonably carry out to ensure that the ship is seaworthy. Secondly, any work in fact carried out must be done with reasonable skill, care and competence (see Union of India v Reederij Amsterdam [1963] 2 Lloyd's Rep 223).

Engaging competent contractors to perform the necessary work does not mean that ship owners' duty to exercise due diligence has been satisfied. The duty would only be satisfied if due diligence is shown by every person to whom any part of the work has been entrusted, whether employees, agents or independent contractors (see The Muncaster Castle [1961] 1 Lloyd's Rep 57).

The replacement of the absolute warranty of seaworthiness by an obligation to exercise due diligence relieves ship owners from responsibility for latent defects in the ship. For example, ship owners will be protected against defects which could not be discovered by the ship owner or by competent experts exercising due diligence. (See The Muncaster Castle [1961] 1 Lloyd's Rep 57). Under most charterparty forms, a ship has to be delivered, ready to receive cargo with clean swept holds which are "tight, staunch, strong, and in every way fitted for the service". This is a strict obligation. Thus, the ship owner is in breach if the vessel is not "in every way fitted for service", regardless of any fault on his part.

However, as mentioned above, with the incorporation of the clause paramount, the absolute duty is converted to one of merely exercising due diligence to make the ship seaworthy for loading and the cargo-carrying voyage.

For example, if the vessel's cranes break down on delivery and the charter does not include a clause paramount, the owner will be in breach, regardless of fault. If the charter contains a clause paramount, the owner may be able to defend a claim from the charterers if he can demonstrate that he exercised due diligence to comply with his obligation to make the vessel "in every way fitted for service".

c. Under a clause paramount, do owners have to exercise due diligence at the beginning of each voyage or just at the beginning of the charter?

Under time charters with consecutive voyages, there is no obligation of seaworthiness at the beginning of each voyage under the charter. The obligation of seaworthiness only exists at the beginning of the charter when the ship is delivered. However, if the clause paramount is incorporated in the time charterparty, the ship owner is bound to exercise due diligence at the beginning of every voyage.

Notwithstanding the above, the courts have yet to fully accept the above proposition that due diligence must be exercised at the outset of every voyage in the event the HV Rules are incorporated into a charterparty (The Hermosa [1980] 1 Lloyd's Rep 638). Consequently, ship owners should be cautious and ensure that due diligence is exercised at the beginning of every voyage if a clause paramount exists in the charterparty.

d. Does the clause paramount vary the ship owner's obligations when tendering an NOR?

Ship owners should note that the presence of a clause paramount in a charterparty does not affect the requirements for tendering a valid notice of readiness ("NOR") (For more on NOR, please refer to our Notice of readiness in a nutshell defence guide. Therefore, even if due diligence is exercised by ship owners but the vessel's holds are nonetheless unclean and not ready to receive cargo, the tendering of the NOR would not be effective to commence the running of laytime nor would charterers have to accept delivery of the vessel.

During the charterparty: how does the incorporation of a clause paramount affect owners' rights and obligations?

a. Obligation to maintain the ship

As noted in 2) a) and c) above, the incorporation of a clause paramount into a time charter converts owners' absolute obligation of seaworthiness when the ship is delivered to an obligation of due diligence at the beginning of each voyage under the charter.

This fresh obligation of due diligence is in addition to owners' pre-existing obligation under clause 1 of the NYPE form to maintain the ship's hull, machinery and equipment throughout the entire charter period. As such, members should note that the continuing duty to maintain the ship would still exist under the NYPE form notwithstanding the clause paramount.

b. Can ship owners use the exclusions of liability contained in the HV Rules to avoid liability?

i) Article IV rule 2 of the HV Rules: the HV Rules contain a list of exclusions of liability under Article IV rule 2. One of the most important of these states: "Neither the carrier nor the ship shall be responsible for loss or damage arising or resulting from… (a) act, neglect, or default of the master, mariner, pilot or the servants of the carrier in the navigation or in the management of the ship…".

Ship owners are entitled to rely on all further exceptions provided by the HV Rules so long as they are able to prove that they fall within such exceptions.

An interesting use of this exception is illustrated in a case where charterers had ordered the master to load as much cargo as possible so as to have sufficient draught to enable her to go through the Panama Canal. Upon arrival, the ship was refused entry into the Panama Canal because she had exceeded her permitted draught. The ship was not off hire and charterers therefore made a claim for damages. However, charterers' claim for damages was defeated because the loss was found to have arisen from the neglect of the master in the management of the ship (which is an exception under the HV Rules). The court found that the neglect of the master caused the vessel to exceed the permitted draught and excused the owners from liability (See The Aquacharm [1980] 2 Lloyd's Rep 237).

Further, in a case where ship owners were in breach of a speed warranty in a voyage charterparty due to an engine breakdown, the ship owners were allowed to rely on the exceptions under the HV Rules to avoid liability (The Leonidas [2001] 1 Lloyd's Rep 533).

Notwithstanding the above, members should note that the above cases are confined to their own facts and members should not assume a similar outcome would be found in a case with different facts.

ii) Deviation: certain standard form charter parties such as the NYPE only state that the vessel has the liberty to deviate in order to save life and property but does not specify that the ship owners' liability resulting from such deviation is excluded.

The HV Rules on the other hand specifically state that ship owners would not be liable for any losses or damages resulting from reasonable deviation. As such, a clause paramount which incorporates the HV Rules may be a useful means excluding liability for reasonable deviation.

iii) Limitation of liability (financial limit): ship owners may also benefit from the limitation regime afforded by the HV Rules. However, this is only confined to ship owners' liability in respect of loss of or damage to goods carried under the charter (The Kapitan Petko Voivoda [2003] 2 Lloyd's Rep 1).

iv) Limitation of liability (time limit): since the HV Rules originated within bills of lading, the one-year time bar under the HV Rules was specifically designed to operate in relation to cargo claims. Therefore, where the HV Rules have been incorporated into a charterparty, the one year time bar in the HV Rules would only apply to claims in relation to cargo that arise between owners (or disponent owners) and charterers under the charterparty (See The Agios Lazarus [1976] 2 Lloyd's Rep 47). In this regard, "claims in relation to cargo" does not just refer to cargo claims per se (i.e. claims for cargo damage and/or shortage) but also includes claims for financial losses due to delays in loading the cargo, as well as expenses for extra tank cleaning and pumping of the cargo which were held to be losses and damages related to goods and therefore time barred due to the incorporation of the HV Rules into the charterparty (See The Ot Sonja [1993] 2 Lloyd's Rep 435 and The Stolt Sydness [1997] 1 Lloyd's Rep 273).

Moreover, claims in respect of damaged or lost property belonging to charterers which are kept on board the vessel may be caught by the one-year time bar if they are regarded as "goods" which are due to be delivered at a later date. However, a claim for loss of charterers' bunkers on board the vessel would not be caught by the one-year time bar as such bunkers were meant to be consumed and not delivered (See The Seki Rolette [1998] 2 Lloyd's Rep 638). Equally, a claim by charterers for damages arising out of owners' delay in issuing bills of lading will not be time-barred after one year due to the incorporation of the HV Rules into the charterparty (see The Standard Ardour [1988] 2 Lloyd's Rep 159). Notwithstanding the above, as most charterparties incorporate the Inter-Club New York Produce Exchange Agreement ("ICA"), the ICA will prevail over the HV Rules in terms of liability and time bar.

It is also important to note that the one-year time bar only applies to claims by charterers against owners but does not cover proceedings by owners against charterers (see The Khian Zephry [1982] 1 Lloyd's Rep 73).

Conclusion

In light of the potentially far-reaching effects of a clause paramount outlined above, members are advised to carefully consider whether to include such clauses in their (time or voyage) charter parties. Generally, owners are advised to include clause paramount in their charterparties as (1) they may be entitled to rely on the exceptions under the HV Rules, (2) their absolute duty of seaworthiness is reduced to one to exercise due diligence and (3) they may be able to rely on the one year limitation period for cargo claims under the HV Rules. The only potential disadvantage to owners (and disponent owners) of incorporating a clause paramount into a charterparty is that owners' obligation to ensure the seaworthiness and cargoworthiness of the vessel will then arise at the start of each voyage under a time charter, not just on delivery of the vessel to charterers. However, even here, if the charter is on NYPE terms, owners/disponent owners will in any event be under a continuing warranty of seaworthiness/cargoworthiness (previous section, par a.).

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