Free of Encumbrances and Third Party Arrests

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It is common for shipowners and charterers to give warranties to each other, which specifically address the question of which party bears the risks for the arrest of the ship by third parties.

In a recent decision from the English High Court Rhine Shipping DMCC v Vitol SA, a warranty given by an owner that the ship was “free from encumbrances” has highlighted the extent to which the Courts will give support to the operation of the warranty.

In 2020, Rhine Shipping, as disponent owners, chartered the MT Dijilah to Vitol to carry crude oil between Djeno in the Congo to various ports in Asia. The charter contained a warranty from the owners which confirmed the ship was “free of any encumbrances and legal issues that might affect vessel approvals or performance of the charter.”

It also contained a standard third-party arrest clause, dividing responsibility for the arrest of the ship during the charter between owners and charterers – depending on what had caused the arrest.

Clause 13 stated:

“In the event of arrest/detention or other sanction levied against the vessel through no fault of Charterer, Owner shall indemnify Charterers for any damages, penalties, costs and consequences and any time vessel is under arrest/detained and/or limited in her performance is fully for Owners’ account and/or such time shall not count as laytime or if on demurrage as time on demurrage.

In the event of arrest/detention or other sanction levied against the vessel through no fault of Charterers, Charterers shall be entitled in Charterers option to terminate the Charter. Termination or failure to terminate shall be without prejudice to any claim for damages Charter may have against Owners.”

Before the MT Dijilah was fixed by Vitol SA on 27 March, after they had entered into a sale contract of the intended cargo with Vitol Asia. The purchase price payable by Vitol Asia was going to be the average of the settlement quotations at the date the oils arrived at the discharge port. The intended arrival period for the ship was between 20-31 May. Vitol S.A then purchased cargo from TOTSA; Vitol agreed that the ship would arrive at Djeno between 5-6 May. The purchase price for the oil was agreed to be the average of quotations – on the

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date of the bill of lading.

On delivery in the charter, Vitol ordered the ship to take on cargo at Offshore Cape Three Points and then load the Djeno cargo.

At Cape Three Points, the ship's bunkers were arrested to obtain security for the claim in London Arbitration. The disputes in London related to an issue between the registered owners of the ship and an associated company of Rhine and a charterer – Al-Iraqia.

The ship was allowed to load its cargo in Cape Three Points, but the departure was delayed from that place whilst the security for the arrest was put in place.

The ship arrived in Djeno on 10 May and loaded its cargo on 12 May, issued bills of lading and sailed to Qingdao. The ship arrived at Qingdao on 13 June but was unable to discharge all the cargo on board fully and had to be moved to Huangdo.

- Following the completion of the charter – the owners Rhine claimed demurrage, which was agreed upon.
- Vitol then presented a counterclaim for the delays caused by the arrest.
- That counterclaim was the difference between the amount Vitol had to pay for the cargo in Djeno – which was USD 24,562,783.57, rather than USD 20,887,349.35 they would have paid if the ship had arrived on time.

The Court had to consider whether the owners had breached the warranty on encumbrances. The answer to that was yes. Property on board the ship had been arrested, and the arrest was directed at the ship.

As far as the losses were concerned, the charterers had been able to show that, except for the arrest, the ship would have arrived at Djeno on time.

The Court only had to consider whether the arrest had caused the loss of the chance to purchase the TOTSA cargo – at the lower price.

The Judge took the view that there was clear and “undisputed” evidence as to how long the loading took place at Djeno – less than a week later after the events in question. On that basis, the timings of events were virtually certain, and that was good enough to show what impact the arrest had on events.

The dispute also looked at the way Vitol bought and sold cargo and the hedging system they used, as well as the internal swaps. As soon as the delays had occurred as a result of the arrest, Vitol had rolled over the swops internally and made some gains. The Court was asked to consider whether those internal gains should be

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brought into account when looking at a loss.

As the swops were related to “internal” rather than external hedging – the Court decided that they were purely internal arrangements within Vitol and did not affect Vitols’ external profit or loss.

Of particular importance, the Court decided that the losses were not too remote. Expert evidence was produced to show that the loss claimed by Vitol was of a usual type flowing from a breach of charterparty.

The Judges’ approach to the loss issue appears to have been based upon the third-party arrest clause. The view he took was that damages which flowed from the arrest should not be limited to non-remote consequences and that clause 13 – was not limited by the usual rules on remoteness.

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