WIKBORG | REIN

Update

December 2021

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Publisher: WIKBORG REIN
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Photos: GETTYIMAGES.COM
Layout: HELENE S. LILLEBYE
Print: BODONI / 1000 COPIES

Update December 2021 Shipping Offshore

Dear friends and readers,

It has been a turbulent year. After having experienced waves of Covid-19 mutation outbreaks, the increased vaccination levels over the summer gave us the feeling that the worst was behind us. However, uncertainty is once again prevailing with the Omicron mutation spreading around the world. In Europe alone cases have been reported in 19 countries. So far the cases reported suggest asymptomatic or mild reactions, but authorities minding previous experience are once again adopting different precautionary measures. Vulnerable sectors may once again face mounting problems, requiring additional government interventions. Hopefully, the current wave will be limited in severity, time and scope, enabling economic recovery sometime next year.

The shipping markets started 2021 on a bumpy ride, but high demand for goods combined with a lack of supply has driven freight rates causing a shipping boom on the Norwegian stock exchange (see article on p. 4). On the bright side, the energy transition has greatly increased investments in green initiatives, innovation of future fuels, electrification and renewable energy sources such as offshore wind. Technological innovations to exploit the oceans' renewable energy resources more safely and sustainably are in the forefront, and will continue to present significant commercial opportunities for ambitious stakeholders.

This Update contains articles on important developments in our industry, considering issues such as the EU's "Fit for 55" package with proposals for decarbonisation of shipping and the EEXI amendments to MARPOL Annex VI, as well as other issues such as tiered dispute resolution clauses, implied terms, demand guarantees, demurrage and limitation of liability.

I hope that you will find these articles interesting and informative. We welcome any feedback and would be particularly interested in receiving requests for topics that you would like us to address in future Updates.

Enjoyable reading!

Partner and Global Head of Shipping & Offshore

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SHIPPING BOOM
in the Norwegian stock market

After a period of strong headwinds, the shipping industry sets course for historic annual results. High demand for goods combined with a lack of supply and a lean world fleet has driven freight rates and shipping shares through the roof.

After last year's decline in the market, analysis now shows a historic growth in the maritime freight market. Last year's negative trend in demand for tonnage has been turned upside down but not everyone is on board - it is first and foremost the segment for container freight that has gained momentum, with the market for break-bulk following in its wake.

MPC-STOCK SURGE ON OSLO BØRS

The Oslo Stock Exchange, part of the Euronext Group, is world leading in the energy, shipping and seafood sectors. It operates the regulated markets for securities trading in Norway, the Oslo Børs main board and Oslo Expand, as well as the multilateral trading facility Euronext Growth. The marketplaces operated by the Oslo Stock Exchange are part of the Norwegian maritime cluster with access to domestic and international investors, investment banks with industry focus, seasoned legal advisors and a highly competent research community, as well as efficient settlement, listing and admission processes and trading systems.

Amongst the top 20 winners on the Norwegian stock market so far this year, we find the shipping companies MPC Container Ships, Jinhui Shipping and Transportation, Awilco LNG, Belships, Wilson, Golden Ocean Group and 2020 Bulkers.

The freight boom has led to soaring share prices in the Norwegian stock market for shipping companies in general and for the container freight industry especially. MPC Container Ships (MPC) is being referred to as the "stock rocket" of the year on the Oslo Stock Exchange. MPC has also strengthened its position in the market by the new NOK 1.8 billion acquisition of Songa Container, expanding its fleet from 64 to 75 feeder ships. Commenting on the market in an interview with the Norwegian financial website E24, MPC's Constantin Baack said he believed that they would see a quick return on their new acquisition and expressed strong optimism for the year to come.

MPC assumes a gross operating profit of over USD 350 million next year, equivalent to around NOK 3 billion, an increase from the approximate NOK 170 to 180 million this year.

Looking at recent listings, we find the listing of Western Bulk Chartering's shares on Euronext Growth, having its first day of trading on 20 September 2021. On completing the issue for new shares, Western Bulk Chartering experienced an overwhelming interest and felt it necessary to cut the subscription period. The investors at Arctic Securities and DNB Markets completed the issue of NOK 130 million in just a few hours.

A MARKET FOR ALL

Both professional and retail investors are loading up with container shares. MPC, the only pure container company on the Oslo Stock Exchange, also attracts many Norwegian retail investors.

For dry-bulk on the Oslo Stock Exchange, we saw companies like 2020 Bulkers Ltd. reaching its all-time high in mid-August 2021, nearly three times the market cap compared to the same time last year. Similarly, Golden Ocean Group reached an all-time high in the beginning of September of this year, well over three times the market cap of the same time last year.

MAIN REQUIREMENTS FOR PRIMARY LISTING AND KEY DIFFERENCES

	EURONEXT GROWTH	EURONEXT Expand	OSLO BØRS
Market capitalisation	EUR 2.5 million "available for trading"	NOK 8 million	NOK 300 million
Market value per share	NOK 1	NOK 10	NOK 10
Free float	**15%** public distribution	**25%** public distribution	**25%** public distribution
Number of shareholders	**30** (value of >NOK 5,000)	**100** (value of >NOK 10,000)	**500** (value of >NOK 10,000)
Existence and operational history	–	–	**3 years**
Historical financial information	• Annual reports for the last **2 years** • Interim report if >9 months since last balance sheet date	• At least **one annual or interim report (IFRS/IAS)** • Interim report if >9 months since last balance sheet date	• Annual reports for the last **3 years (IFRS)** • Interim report if >9 months since last balance sheet date
Liquidity	Sufficient liquidity for the last 12 months **or plan** to achieve sufficient liquidity	Sufficient liquidity for at least 12 months	Sufficient liquidity for at least 12 months
Main document to be prepared	**Information document**	Prospectus	Prospectus
Due dilligence	Independent DD advisors, with **some exemptions**	Independent DD advisors	Independent DD advisors

"Regulated markets"

NORWEGIAN OVER-THE-COUNTER MARKET (NOTC)

As an alternative to going through one of the centralised exchange markets, securities may be traded over the counter via a broker-dealer network. The NOTC can offer instant low threshold listings of shares with minimum reporting requirements.

SERVICE TAILORED TO FIT YOUR NEEDS

Wikborg Rein has assisted and is assisting numerous companies going public, both as legal advisors for the companies seeking to raise capital through the securities market and for the advisors managing the IPO/listing processes. Furthermore we have extensive experience on bond issues (and listings) and other financial instruments, giving companies access to capital from all over the world. We have a clear edge on shipping and offshore related IPOs and fundraising as well as international presence with our London, Shanghai and Singapore offices. •

After last year's decline in the market, analysis now shows a historic growth in the maritime freight market.

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Limitation of liability for collisions claims in respect of wreck removal expenses

A recent decision in the Norwegian proceedings relating to the collision between the Norwegian navy frigate "Helge Ingstad" and the oil tanker "Sola TS" saw Hordaland District Court weigh in on a question that has been the subject of international debate for some time. The court held that the Norwegian state's indemnity claim against the owners of the "TS Sola" in respect of the costs of the removal of the wreck of the "Helge Ingstad" is subject to the limitation amount for claims in respect of property damage and not the separate and higher limitation amount for claims in respect of clean-up and wreck removal.

As a result of the collision in the Hjeltefjorden on the West Coast of Norway on 8 November 2018, "Helge Ingstad" sank and was later deemed a total loss. Fortunately, there were no lives lost. The state commenced proceedings before Hordaland District Court, where it brought claims against the owners of the "Sola TS", Twitt Navigation Limited ("**Twitt**"), in the amount of about NOK 13 billion for the total loss of the frigate and about NOK 770 million for the costs of the wreck removal. Twitt established a limitation fund before the same court for claims in respect of property damage in accordance with the Norwegian Maritime Code ("**NMC**") section 172, ref. section 175 No. 3. Apportionment of liability for the collision is disputed and is not yet determined in the proceedings.

While the parties agreed that the total loss claim was subject to the limitation amount for property damage the issue in dispute between the parties was whether the state's claim for the wreck removal costs was also subject to the same limitation amount. Twitt argued that it was. The state however contended that the claim for the wreck removal costs was instead subject to the separate and higher limitation limit for claims in respect of clean-up and wreck removal under sections 172a and 175a of the NMC.

Based on the gross tonnage of the "Sola TS" the limitation amount for property claims was NOK 400 million, whereas the limitation amount for clean-up and wreck removal claims was significantly higher at NOK 1,150 million. It follows that, if the wreck removal claims were subject to the limitation amount for clean-up and wreck removal claims, such claims would not in fact be limited. On the other hand, if the same claims were subject to the limitation amount for property claims, they would be limited and compete with the total loss claim.

LLMC AND NORWEGIAN LAW

Norway is party to the Convention on Limitation of Liability for Maritime Claims 1976 ("**LLMC**") as amended by the 1996 Protocol. The LLMC Article 2 sets out which claims can be limited by the shipowner. Article 2(1) distinguishes on the one hand between "*claims in respect of* [...] *loss of or damage to property* [...] *in direct connexion with the operation of the ship* [...] *and*

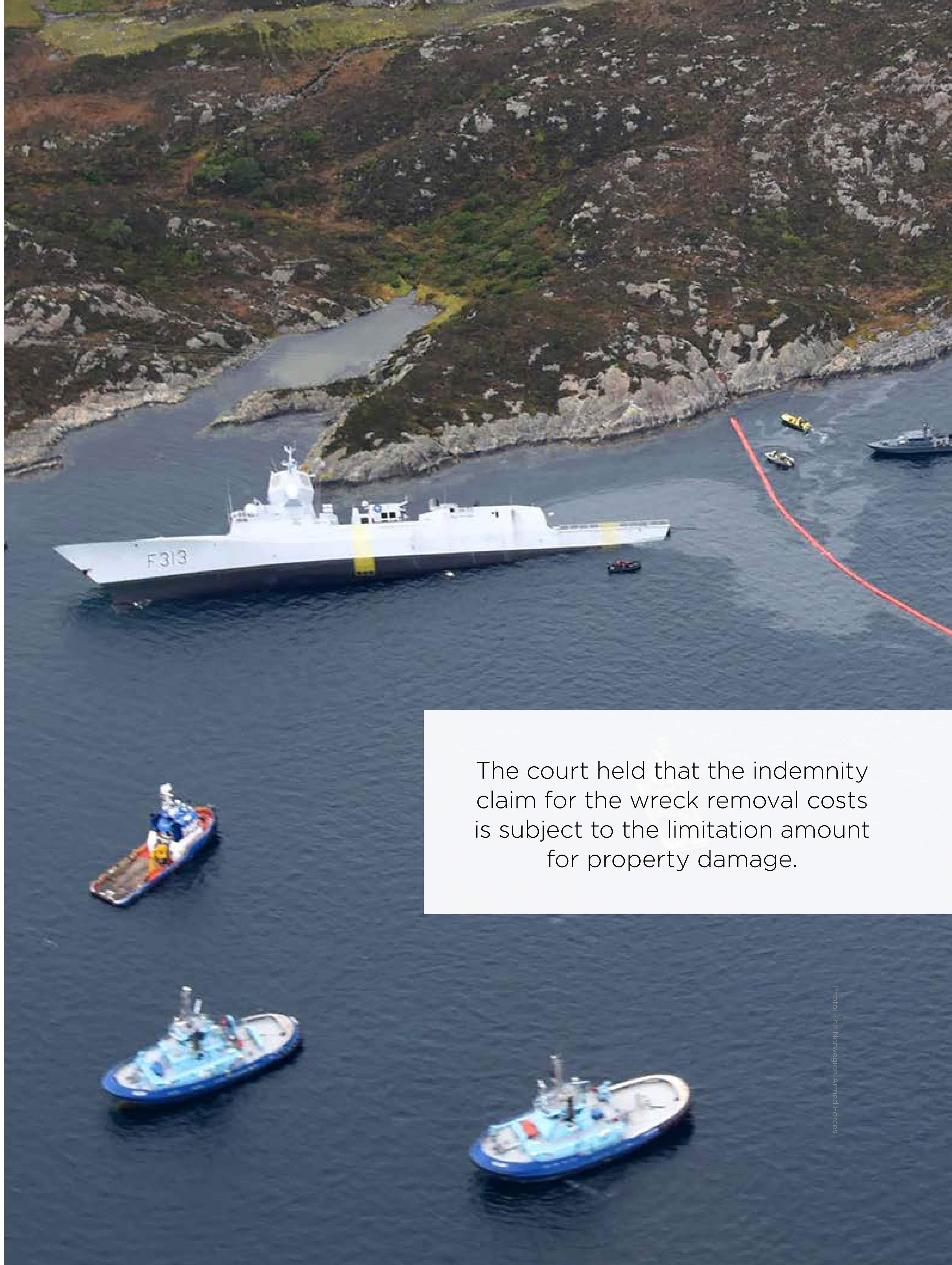
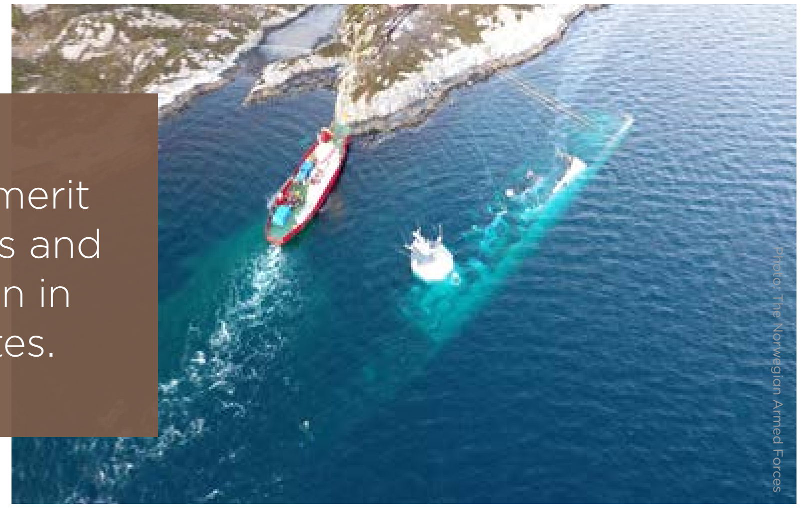


Photo: The Norwegian Armed Forces

The court held that the indemnity claim for the wreck removal costs is subject to the limitation amount for property damage.



There are arguments of merit in favour of both positions and no uniform interpretation in the LLMC member states.

consequential loss resulting therefrom" in paragraph (a) and on the other "*claims in respect of the raising, removal, [...] of a ship which is sunk, wrecked, stranded or abandoned, including anything that is or has been on board such ship*" in paragraph (d). Article 2 provides that this distinction applies even where the relevant claims are "*brought by way of recourse or for indemnity under a contract or otherwise*".

Norway, similarly to many other countries, has reserved the right under LLMC Article 18 to exclude claims in respect of clean-up and wreck removal in Article 2(1)(d) and (e) from the application of the LLMC. For such claims Norway has instead implemented a separate and higher limitation limit in NMC section 172a and 175a.

THE COURT'S DECISION

In its decision on 16 November 2021, Hordaland District Court recognised that there is a certain overlap between consequential loss arising from property damage in paragraph (a) and claims in respect of clean-up and wreck removal in paragraph (d) and that, when read in isolation, the wording allows for the state's claim in respect of the wreck removal to fall within both paragraphs (a) and (d).

However, there were three decisive factors which lead he Court to the conclusion that the state's claim in respect of the wreck removal fell within Article 2(1)(a), and was therefore subject to the limitation amount for property claims.

First, the Norwegian preparatory works prior to the decision of implementing the reservation against LLMC Article 2(1)(d) and (e) provide that a strong motive was to prevent the public authorities from footing the bill for the clean-up expenses, which suggests that the reservation was not intended to apply to collision claims between two ships.

Secondly, the intention behind the reservation against Article 2(1) (d) and (e) was not to confine the application of Article 2(1)(a).

Thirdly, the court emphasised that the NMC sections 172 and 172a should not be construed in a way that is contrary to Norway's international obligations as a member of the LLMC.

CONCLUDING REMARKS

The question as to whether collision claims against another ship for wreck removal costs shall be construed as either being claims for consequential losses arising from property damage and thus subject to the LLMC Article 2(1)(a) or claims in respect of wreck removal subject to the LLMC Article 2(1)(d) is a difficult one. There are arguments of merit in favour of both positions and no uniform interpretation across the LLMC member states. It is anticipated that the Hordaland District Court will not have the last say on this issue. •

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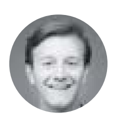

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Are lawyers' notes from crew interviews legally privileged?

In another recent decision in the Norwegian proceedings relating to the collision between the Norwegian navy frigate "Helge Ingstad" and the oil tanker "Sola TS", the Gulating Court of Appeal has held (LG-2021-115658) that notes taken by lawyers from crew interviews were legally privileged and such privilege had not been waived by disclosure in the proceedings of a report referencing content from those notes.

Following the collision, lawyers acting for the owners of the "Sola TS", Twitt Navigation Limited ("**Twitt**"), and their insurers conducted interviews of the crew on the oil tanker.

In the proceedings that ensued, the state requested that Twitt disclose those notes. Twitt argued that they were not obliged to do so, claiming legal privilege over the notes.

In the first instance, Hordaland District Court found that Twitt had consented to disclosing the notes, thereby waiving privilege, by disclosing a report which referred to the contents of the notes. Twitt appealed the District Court's decision and, on 13 September 2021, the Gulating Court of Appeal overturned the District Court's decision holding that privilege had not been waived.

WERE THE NOTES PRIVILEGED?

The universal principle of attorney-client privilege is reflected in section 22-5 (1) of the Norwegian Dispute Act, which prevents the courts from receiving evidence from lawyers about "*something that was confided to them in their professional capacity*".

Reiterating the case law, the Court of Appeal held it is a requirement for legal privilege to attach that the information was confided to the lawyer whilst performing "*work as a lawyer in the true sense*" ("*egentlig advokatvirksomhet*"). This has to be considered on a case-by-case basis.

As a starting point, the Court of Appeal found that the information obtained by the lawyers during interviews with the crew onboard "Sola TS" had been provided to them "*in their professional capacity*", acting as the legal representatives of Twitt.

The Court of Appeal then considered whether the interviews were conducted "*exclusively to survey factual circumstances which could not have legal consequences*", and as such would not be considered "*work as a lawyer in the true sense*", see HR-2014-1775-A. The Court of Appeal found that this was not the case as the information "*could have legal consequences*" and, moreover, could provide the basis for legal advice from the lawyers in connection with claims arising from the collision and the ensuing legal proceedings.

The Court of Appeal also considered the Supreme Court's decision in HR-2019-2168-U *Cheshire*, where it was held that ordinary written and signed statements

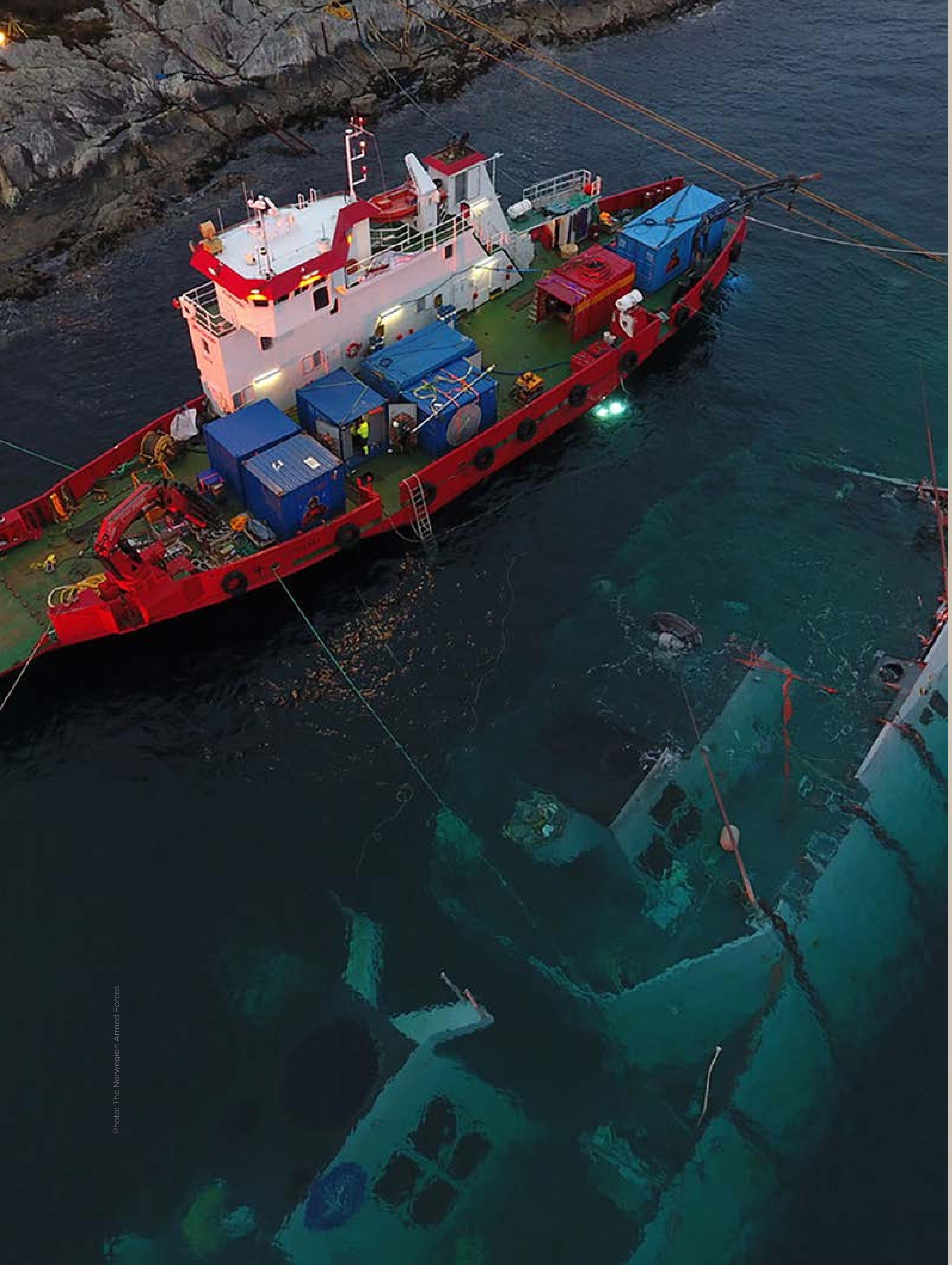

Photo: The Norwegian Armed Forces

created with the intention of being disclosed were not covered by legal privilege, even if lawyers had been instrumental in creating them. However, on the facts of this case, the Court of Appeal found that the notes prepared by the lawyers were not intended to be disclosed, and therefore remained privileged.

HAD TWITT CONSENTED TO DISCLOSE THE NOTES?

The Court of Appeal then considered whether Twitt had consented to disclose the notes, thereby waiving privilege, since they had produced a report in the proceedings which had referenced the notes, cf. section 22-5 (3) of the Dispute Act.

Whether consent was given had to be considered according to general principles of contract law. Although there are no requirements as to form, the consent must be "*fairly clear, decisive and exhaustive*", and appear as a renunciation of legal privilege.

The Court of Appeal held that sharing of privileged information in itself was not sufficient to establish consent to waive legal privilege, cf. *inter alia* HR-2013-2652-U.

Whilst the District Court had found that consent to waive legal privilege could be inferred, citing *inter alia* Rt-2009-1204, the Court of Appeal distinguished the cases on the facts and found that the decision provided little guidance for the question under consideration.

The Court of Appeal then held that a report could only be seen as giving consent to disclose privileged information if the contents in the report itself were privileged, citing the aforementioned HR-2019-2168-U *Cheshire*.

The Court of Appeal did not decide on whether the report itself was privileged, as the disclosure of the report in any event – in the Court of Appeal's opinion – did not fulfil the criteria of a valid consent to waive legal privilege. In reaching this conclusion, the Court of Appeal emphasised that the 17-page long report only contained two references to the interviews, and as such could not be regarded as a sufficiently clear consent to waive legal privilege for the more extensive interview notes. That the report itself was marked as privileged and confidential, could not be decisive for the question of consent to disclose other privileged documents.

Finally, the Court of Appeal held that any departure from the protection afforded under attorney-client privileged information under *inter alia* the Norwegian Criminal Code section 211, the Norwegian Constitution section 95 and the European Convention on Human Rights Article 6, required a clear basis.

COMMENT

This decision provides guidance as to the application of legal privilege in connection with marine casualties. It follows from the decision that lawyers' notes from crew interviews are privileged unless they are intended to be disclosed, as was the case in the Supreme Court decision in HR-2019-2168-U *Cheshire* where formal statements had been signed by the individual crew member. Furthermore, the decision suggests that the courts will take a relatively restrictive approach to establishing consent by a party to disclose otherwise privileged information.

The decision has been appealed to the Supreme Court. •

> Lawyers' notes from crew interviews are privileged unless they are intended to be disclosed.

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The right to claim deprivation interest in pollution incidents in Norway

Norwegian authorities normally respond to an oil spill or other type of pollution along the Norwegian coast by initiating a state-led operation, often involving significant costs. A recent amendment to the Norwegian Pollution Act has created a statutory legal basis for the authorities, when claiming reimbursement from the owners, to include a claim for so-called deprivation interest as from the time the relevant costs were incurred.

In a white paper published in December 2019, the Ministry of Transport proposed that a statutory deprivation interest rate of NIBOR + 4% per annum should be applied to all clean-up response costs as from the time relevant costs were incurred until the time when the usual interest on late payment (so-called "penalty interest") started accruing. The latter is normally 30 days after a written demand for payment.

The proposal for an unqualified right for the authorities to claim deprivation interest on reimbursement claims under section 76 of the Norwegian Pollution Act ("NPA"), would – compared to judicial precedent as developed by the courts – have represented a significant expansion of the authorities' rights to claim deprivation interest in these types of cases. Whilst the Ministry's proposal was adopted, it contained one significant amendment:, namely that the right to claim deprivation interest is not wholly unqualified as originally proposed by the Ministry.

THE "INCENTIVE PROBLEM" WITH THE ORIGINAL PROPOSAL

Unfortunately, there have been several accidents along the Norwegian coast in recent years involving significant oil spills and other types of pollution from vessels, resulting in expensive state-led clean-up operations. Well known examples are "Server" off Fedje in 2007 and "Full City" off Såstein in 2009, both involving significant bunker oil spills and expensive clean-up operations. A main concern with the white paper proposal was the experience from these and other cases that the public authorities were very slow in presenting proper quantified claims to owners, often having to request time-extensions to avoid time-bar. The authorities could arguably be blamed for such delay. However, under the original proposal which contained an unqualified right to claim deprivation interest of NIBOR + 4 % rate, the authorities would have no economic incentives to alter practice by presenting their reimbursement claims in a more expedient fashion.

QUALIFICATION OF THE RIGHT TO DEPRIVATION INTEREST

On 21 May 2021 an amended proposal was therefore enacted by the Norwegian Parliament which entered into force on the same day. The interest rate suggested by the Ministry was enacted unamended in the second paragraph of the NPA section 76. However, instead of giving the authorities an unqualified right to claim deprivation interest in all circumstances, an amended wording was adopted stating that deprivation interest "may" be calculated as from the time the expenses were incurred. This is an important qualification compared to the Ministry's original proposal as the door is left open for owners to argue that no deprivation interest shall apply if public authorities can be blamed for delaying the reimbursement claim.

The preparatory works address the point that public authorities often may be blamed for the prolonged time period before a reimbursement claim is presented, but emphasise that these types of cases are complicated and therefore deprivation interest should normally be allowed, cf. Prop. 87 L (2020–2021) p. 10. However, as also noted, if the time period is short, there is limited need to calculate deprivation interest.

In summary, although owners may still argue that public authorities are not entitled to claim deprivation interest due to prolonged delay in claiming reimbursement, the adoption of the revisions in section 76 and the background explained in the preparatory works indicate that succeeding with such an argument is not straight-forward •

> The door is left open for owners to argue that no deprivation interest shall apply if the authorities can be blamed for delaying the reimbursement claim.

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Apache UK Investment Limited v Esso Exploration and Production UK Limited (2021) EWHC 128

WHOSE LIABILITY IS IT ANYWAY?

On the 17 May 2021, the Commercial Court clarified the proper interpretation of the Petroleum Act 1998, dealing specifically with the extent of previous licensees' liability in decommissioning programmes.

In 2011, Apache UK Investment Limited ("**Apache**") entered into a sale and purchase agreement with Esso Exploration and Production UK Limited ("**Esso**"), by which Apache acquired several oil and gas assets in the North Sea.

Before this, the newly acquired licensee company had been served several section 29 notices under the Petroleum Act, requiring submission to decommissioning programmes.

The parties entered into a series of Bilateral Decommissioning Security Agreements ("**BDSAs**"), under which Apache agreed to indemnify Esso for any decommissioning obligations arising out of the transferred assets. A dispute arose over four subsea wells which were drilled after the sale to Apache.

ISSUES

Two key issues arose under the BDSA regarding proposed decommissioning plans for 2021.

The first issue, which this article does not discuss, was the choice of which proposed decommissioning plan was to apply, which required contractual interpretation of the BDSA's specific terms.

The second issue was contingent upon key analysis of the Petroleum Act's decommissioning regime, requiring judicial interpretation of the statutory scheme.

THE ARGUMENTS

Esso objected to Apache's proposed plan for 2021, arguing that the cost estimate should have included the four additional wells that were drilled after they sold the assets to Apache, on the basis that they could become liable for the decommissioning costs (if the section 29 notices originally served on Esso were wide enough to extend to these additional wells).

Apache contended that for the additional wells neither Esso nor their predecessors fell within section 30(1) of the Petroleum Act, as the additional wells were drilled after Esso divested itself of the relevant licences on the sale to Apache and so section 34 of the Petroleum Act, which concerns revision of programs, was not engaged.

In turn, Esso (that had discussed their concerns with the Offshore Petroleum Regulator for Environment and Decommissioning), contended that they could be liable for the decommissioning costs of the additional wells under section 34 of the Petroleum Act, and, therefore, Esso were entitled to additional security from Apache in respect of the potential costs of decommissioning the additional wells.

DECISION

The judge held that Esso could not be liable for the decommissioning costs of the additional wells under the section 29 notices, because the wells did not exist, nor were they "intended to be established", when Esso owned the assets and carried out exploration and production activities, or when the original section 29 notices were served.

Referring to the objectives of the Petroleum Act's regime, the court noted that such an interpretation aligns with the objective of ensuring that those who have "*derived a financial benefit from an offshore installation should also be responsible for its decommissioning*".

When interpreting the definition of "offshore installation" under sections 44(1) and 44(5) of the Petroleum Act, the court suggested a narrower approach, dismissing the argument that the phrase could refer to whole fields or sub-fields as opposed to equipment or structures within a field. The court highlighted the Act's reference to "*any floating structure or device*", holding that this could not be interpreted as describing an entire field. This is important guidance for future decommissioning projects.

However, Esso could still be liable for decommissioning costs under section 34 of the Act in due course.

COMMENT

Now that decommissioning programmes are being put into practice, the court's interpretation of the Petroleum Act's statutory regime is a valuable insight into what to expect. The broad terms of section 29 notices are now more refined in practice, limiting the liability of former licensees in respect of new asset installations that they did not intend during their ownership.

Wells drilled by new owners will not lead to liability for previous owners in respect of decommissioning costs. This clarification will assist those involved in decommissioning security agreements when drafting proposed plans, as new wells will not need to be included, nor will security be required in relation to such wells. Additionally, former licensees can take solace in the court's interpretation, as they will not be liable for decommissioning costs for wells that they did not drill or intend to drill.

However, sellers should still be cautious, as they may still be liable for any installations that they **intended to establish at the time when section 29 notices were served**. The OPRED guidance suggests that a former licensee could be liable for the decommissioning of new equipment added to platforms that existed during their ownership, but the court has not yet clarified this point. Until the English courts take a view on this, companies involved in decommissioning security agreements should be mindful of the possibility of being liable for equipment that they did not install. •

Referring to the objectives of the Petroleum Act's regime, the court noted that such an interpretation aligns with the objective of ensuring that those who have "derived a financial benefit from an offshore installation should also be responsible for its decommissioning".

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Eternal Bliss did not last forever for shipowners

Court of Appeal overturns decision narrowing scope of demurrage

The High Court decision last year in *The Eternal Bliss* changed the landscape for owners and voyage charterers by establishing that damages in excess of demurrage can be claimed by owners, even where the only breach was the failure to load and discharge within the laytime. Demurrage had previously been thought to be a complete code for damages caused by that breach. Judgment has now been handed down in the Court of Appeal overturning that decision.

In voyage charterparties, it is trite law that demurrage represents liquidated damages for the failure of the vessel to load and discharge within the agreed period, i.e. the laytime. However, this is where consensus ends.

By failing to give clarity on the issue, the venerable authority of *Reidar v Arcos* [1927] 1 K.B. 352 set the stage for arguments as to whether a separate breach of charterparty as well as damage of a different kind from delay was required in order to obtain damages in excess of demurrage. The members of the Court of Appeal in that case came to their decisions on varying grounds, leaving this question open.

Charterers invariably argued that demurrage is a complete code of damages for delay, and that in order to claim damages over and above the demurrage rate, it is necessary to show both a breach of a separate obligation (distinct from the obligation to load and discharge within the agreed laytime) ***and*** a different type of loss. This is the view set out in *Voyage Charters*, one of the leading texts on this subject.

However, that view had always been open to criticism. Owners would counter that demurrage is compensation for lost employment only, and therefore that damages in respect of a different type of loss can be recovered even where there is no separate breach of charterparty. Owners' view has been supported by other leading academic texts, including *Scrutton on Charterparties*, and by the lack of clear authority making demurrage a complete and exclusionary code.

This has remained a hot button issue in circumstances where rapidly changing market rates can leave owners, and disponent owners, with a demurrage rate that does not adequately compensate them for delay.

HIGH COURT

The High Court decision of Mr Justice Andrew Baker in The Eternal Bliss ([2020] EWHC 2373 (Comm)) came down on owners' side.

In doing so, the Judge rejected *The "Bonde"* [1991] 1 Lloyd's Rep 136, a High Court case of 30 years' standing, in which it had been held that it would be necessary to show not only damage of a different kind from delay but also breach of a separate obligation to the obligation to load and discharge within the agreed laytime.

In doing so, the Judge held that demurrage *"gives an agreed quantification of the owner's loss of use of the ship to earn freight by further employment in respect of delay to the ship after the expiry of the laytime, nothing more"*.

It followed that owners could claim damages in addition to demurrage arising out of a single breach if they had suffered losses other than delay. In coming to this decision, the Judge relied on the reasoning of Lord Justice Bankes in Reidar v Arcos – a minority judgment which has come in for some criticism (particularly in an article by one of the authors of Voyage Charters, Michael Ashcroft QC).

Permission was granted to appeal to the Court of Appeal.

COURT OF APPEAL

The Court of Appeal heard charterers' appeal of the first instance decision at the end of October 2021, just over a year after judgment had been first handed down by the High Court. The Court of Appeal was made up of the Master of the Rolls, Geoffrey Vos, Lord Justice Newey and Lord Justice Males, and the hearing was live-streamed on various channels (including YouTube).

The Court of Appeal's judgment was handed down less than a month later, on 18 November 2021, with Lord Justice Males delivering the judgment ([2021] EWCA Civ 1712).

The state of the law on demurrage now is that if a shipowner seeks to recover damages in addition to demurrage arising from delay, it must prove a breach of a separate obligation.

The Court of Appeal held that demurrage liquidates all damages arising from a charterer's failure to complete cargo operations within the laytime, in breach of charter, for the following reasons:

- It would be *"unusual and surprising"* to liquidate only some of the damages arising from a particular breach (paragraph 53 of the judgment). Such an arrangement would need to be clearly stated.
- Demurrage is intended to compensate owners for the loss of prospective freight, *"but that does not mean that this is all demurrage is intended to do (...) it is more accurate to say that the demurrage rate is the result of a negotiation between the parties where the loss of freight is likely to be one factor, but is by no means the only factor (...)"* (paragraph 54).
- The alternative would *"inevitably be disputes as to whether particular losses are of the 'type' or 'kind' covered by the demurrage clause"* which would lead to further litigation (paragraph 55).
- *The Bonde*, overturned by the first instance decision in *The Eternal Bliss*, had stood almost unchallenged for over 30 years, and hence could be seen as settled law – itself a *"powerful reason"* not to overturn that decision (paragraph 57). The Court of Appeal further held that (unsurprisingly in light of the above) they did not accept the criticisms of *The Bonde* made by the High Court (paragraph 58).
- The Court of Appeal therefore thought that allowing owners to claim damages in addition to demurrage would disturb *"the risk inherent in the parties' contract"* which was already balanced between commonly insured losses on the one hand and demurrage on the other. In particular: *"a charterer will not typically have insurance against liability for unliquidated damages resulting solely from a failure to complete cargo operations within the laytime. Rather, the charterer has protected itself from liability for failing to complete cargo operations within the laytime by stipulating for liquidated damages in the form of demurrage. Accordingly the consequence of the shipowner's construction is to transfer the risk of unliquidated liability for cargo claims from the shipowner who has insured against it to the charterer who has not."*
- *"Finally, to allow the appeal will produce clarity and certainty, while leaving it open to individual parties or to industry bodies to stipulate for a different result if they wish to do so. If our judgment does not meet with approval in the market, it should not be difficult for clauses to be drafted stating expressly that demurrage only covers certain stated categories of loss"* (paragraph 59).

The Court of Appeal did not grant permission to appeal to the Supreme Court, but it is expected that the claimant owners will petition the Supreme Court directly.

COMMENT

In the months since the first instance decision in *The Eternal Bliss*, we have seen a sharp increase in claims from owners for sums in addition to demurrage. These often relate to attempts to pass on liability for cargo claims, which are usually brought against owners as carriers under the bill of lading contract in the first instance, and which often run into the millions of dollars. These claims previously struggled to find a separate breach (other than delay) to link the damages suffered. However, following the rejection of *The Bonde*, this obstacle had been cleared.

Now, however, the floodgates have firmly closed on those claims (at least until the Supreme Court weighs in). It follows that, per the Court of Appeal, the state of the law on demurrage now is that *"if a shipowner seeks to recover damages in addition to demurrage arising from delay, it must prove a breach of a separate obligation"* (paragraph 52). •

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TIERED DISPUTE RESOLUTION CLAUSES

– problems in drafting

There are various forms of tiered dispute resolution clauses requiring negotiation and/or mediation before arbitration, and difficulties may arise when the procedure is not followed. A recent English case, *NWA and Other v NVF and Others [2021] EWHC 2666*, has added further insight to the interpretation of these clauses and the need for clarity in their drafting.

NWA and Other v NVF and Others involved a tiered dispute resolution clause that required disputes to be referred (a) to LCIA mediation in London and (b) if not settled by mediation within 30 days of commencement of the mediation, the dispute was to be referred to LCIA arbitration. In this instance, NVF had first made a request for LCIA arbitration, asking that it be immediately stayed in favour of LCIA mediation. Presumably, there was a time bar that required arbitration to be commenced before any mediation could be carried out. NWA, as respondent in the arbitration, ignored the request for mediation, the notice of arbitration and the LCIA's own invitation to respond. Some 55 days after the notice of arbitration was filed, the LCIA appointed an arbitrator and notified this to the parties. NVF followed up, again offering to stay the arbitration 30 days for a mediation. At this point, NWA replied that a time bar had passed, and refused to participate in the proposed mediation. NVF made two further offers to mediate that were ignored, and then proceeded with the arbitration.

THE ARBITRATION DECISION

A replacement arbitrator decided that the requirement to refer disputes to LCIA mediation was not sufficiently clear and certain to be enforceable, with the effect that it posed no bar to starting arbitration without mediating, and that in any event the ability to start arbitration before any mediation had run 30 days was not expressly injuncted, so even a clear mediation term would not prevent NVF arbitrating without mediating. NWA then appealed to the High Court, on the basis that the arbitrator had no jurisdiction due to the lack of a mediation before the arbitration had commenced. In effect, NWA denied the arbitrator's finding that a mediation was not a condition precedent to commencing arbitration.

THE APPEAL DECISION

The High Court first addressed the issue of whether non-compliance with the mediation term was a matter merely affecting the admissibility of the particular claim being brought in arbitration or one that stopped any arbitration commencing and therefore removing the arbitrator's substantive jurisdiction to determine the claim. In the former case, it would be for the arbitrator to decide if any non-compliance prevented the claim from being pursued, whereas in the latter, the arbitrator had no jurisdiction to consider the question, leaving it for the courts to handle.

The High Court construed the dispute resolution clause as showing the parties had intended all disputes to be arbitrated swiftly, rather than litigated in court. While there was also a 30 day window to mediate a dispute, where one party refused to mediate, the High Court did not regard this as removing the arbitrator's jurisdiction to resolve the dispute. Instead, it was a matter of admissibility for the arbitrator to determine the consequences of any alleged breach of that procedural condition. This followed *Sierra Leone v SL Mining Limited* ([2021] EWHC 286 (Comm)) and joined with it in distinguishing two earlier High Court decisions (*Emirates Trading Agency LLC v Prime Mineral Exports Pte Ltd [2015] 1 WLR 1145 and Tang v Grant Thornton International Limited [2013] 1 All ER (Comm) 1226*) which considered the issue a jurisdictional one, repeating that those decisions had not had the benefit of full argument on the issue.

As such, English law has settled into accepting that the effect of non-compliance of a tiered dispute resolution procedure is for the arbitrator to decide, unless there are very clear words indicating that non-compliance excludes the claim in question from the arbitration agreement.

The High Court also indicated that if the mediation term was worded sufficiently clearly to constitute a condition precedent to being able to arbitrate a dispute, NWA's refusal to mediate would be a breach of such a condition precedent and they could not rely upon their own breach to contend that NVF had failed to comply with the condition precedent; alternatively, compliance with the alleged condition precedent was waived by the parties.

COMMENTARY

Compliance with a tiered dispute resolution clause only tends to become sensi ive when there is a potential time bar involved. Otherwise, the process can simply be repeated properly and the claim arbitrated if negotiation/mediation does not produce an agreement. What this case highlights is that the respondent will not be allowed to ignore or delay a mediation request as a way to create the time bar defence.

The case also underlines how difficult it is to make prior negotiation/mediation steps conditions precedent to arbitration, such as by mentioning the need for clear terms on how the mediation can be started (and if necessary continued) by one party if the other is not co-operating, on the time allowed for mediation, on an injunction against arbitration during the negotiation/mediation or even on an exclusion of claims that have not been mediated from the arbitration agreement. Moreover, if the condition precedent works and the claim cannot be arbitrated, it can still be brought in a court with jurisdiction to hear it, unless time barred.

As such, if parties intend that a dispute must be negotiated and/or mediated before any arbitration can start, they will need to be very careful in drafting their dispute resolution clause. They will also need to consider if such prescriptive drafting is going to help: These clauses are usually drafted on the basis that the parties will remain reasonable and co-operate in negotiations or mediation to try to find an amicable settlement, but drafting it to cover the possibility that the other party does not co-operate may not be appreciated by that party, and if the parties do subsequently stop co-operating, then firm drafting forcing them to mediate may not improve matters. So there remains a good case for the tiered dispute resolution agreement that is not a condition precedent to arbitration. •

> If parties intend that a dispute must be negotiated and/or mediated before any arbitration can start, they will need to be very careful in drafting their dispute resolution clause.

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High Court provides further guidance on implied terms under English law

In the shipping and offshore industry, guarantees are frequently given as security for a legal promise for performance of a separate or primary contract. However, as guarantees are themselves a form of security, do they also contain an implied term that security cannot be sought for breaches of their provisions? That question was recently answered by the High Court in *CVLC Three Carrier Corp v Arab Maritime Petroleum Transport Company* [2021] EWHC 551 (Comm).

Within the shipping and offshore industry, a guarantee may serve several different purposes, for example they are:

- given by parent companies in support of charterparties entered into by their subsidiaries;
- an essential documentary component of the shipbuilding process; and/or
- often a condition precedent to contracts awarded for the construction of large offshore energy projects.

The rationale for this arrangement is simple – if a party to a primary contract defaults on its obligations, the guarantee provides an additional and, in theory, less costly and complex avenue for recovering any amounts owed to a beneficiary.

THE FACTS

CVLC Three Carrier Crop and CVLC Four Carrier Corp (the owners) each chartered one of their vessels to Al-Iraqia Shipping Services and Oil Trading (the charterer) on materially identical bareboat charterparties. The performance of the charterer's obligations under these charterparties was guaranteed by the defendant, Arab Maritime Petroleum Transport Company (AMPTC), pursuant to two materially identical guarantees. These guarantees had been given as consideration by AMPTC to the owners for entering into the charterparties. Whilst not written using the standard forms, the guarantees were "*largely composed of boilerplate text*" which "*would be familiar to anyone with a working knowledge of guarantees*".

Approximately nine months after entering into the charterparties, the owners terminated them for alleged breaches by the charterer. The owners then served notices of arbitration on AMPTC, contending that AMPTC was liable under the guarantees for the losses and damage caused by the charterer's breaches of the charterparties. To secure their claims against AMPTC, the owners proceeded to apply for an arrest of one of AMPTC's vessels in Angola. However, in the period between filing the arrest application and the Angolan court judgment ordering the vessel's arrest, AMPTC applied to the sole arbitrator in London for a declaration that it was an implied term of the guarantees that the owners would not seek additional security in respect of the matters covered by the guarantees.

The guarantees created a separate contractual relationship to that between the owners and the charterers, and a right to seek security against AMPTC would only arise if they did not respond under the guarantees.

The application was made on a documents-only basis, so the arbitrator declined to make any findings on the facts (as these were contentious). The arbitrator first issued an award making the requested declaration, i.e. that such a term was implied. In a second award, the arbitrator then declared that the owners were in breach of that implied term and were therefore liable to AMPTC for damages. The arbitrator's conclusion, if upheld, would have had far-reaching consequences both for security already provided and for future security, which was being negotiated.

English law is reluctant to imply terms into commercial contracts unless such a term is so obvious that it goes without saying or it is necessary to give the contract business efficacy.

THE HIGH COURT'S DECISION

The owners subsequently appealed the tribunal's decision to the English High Court and the Court was asked whether there is an implied term in contracts of guarantee which:

- guarantee the performance of another contract; and
- are expressly given in consideration of entering into another contract, so that creditors would not seek security over and above that which is provided by a guarantee where the guarantor is, or is alleged to be, in breach of the guarantee.

The Court disagreed with the arbitrator and held that there was no implied term preventing the owners from securing their claim against AMPTC.

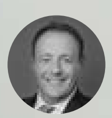
Mrs Justice Cockerell noted that "*the legal hurdle for the implication of a term is a high one*" and as this guarantee was "*couched in boilerplate terms*", if such a term was to be implied, it would in effect mean that a term of this kind would be implied in most guarantees. The judge also commented that the proposed implied term was essentially an exclusion clause, and, therefore, clear wording would generally be required before the Court circumscribed or took away common law rights and remedies from the owners.

Having noted the above, Mrs Justice Cockerell took little time in rejecting AMPTC's arguments that a term preventing the owners from seeking further security needed to be implied for "*business efficacy/necessity*" and that it would make no sense for the owners to be entitled to two sets of security that would be activated if the charterer was in breach of its obligations. The judge noted that the guarantees created a separate contractual relationship to that between the owners and the charterers, and that a right to seek security against AMPTC would only arise if they did not respond under the guarantees. Further, the security sought by the owners was security for the breach of AMPTC's obligation under the guarantee and not for a breach of the charterers' obligations under the charterparties.

Therefore, Mrs Justice Cockerell answered the question of law in the negative, overruling the arbitrator's conclusion with her own. Her ruling meant that the owners were entitled to seek additional security for breaches of the guarantees.

The case serves, along with *Alpha Marine Corp v Minmetals Logistics Zhejiang Co Ltd* (MV Smart) [2021] EWHC 1157 (Comm)], as another recent reminder that English law is reluctant to imply terms into commercial contracts unless such a term is so obvious that it goes without saying or it is necessary to give the contract business efficacy. •

CONTACTS



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Shanghai Shipyard Co Ltd v
Reignwood International Investment (Group) Company Limited:

Always on demand?

On 23 July 2021, in a decision with potentially far-reaching implications for the shipbuilding industry and for guarantees generally, the Court of Appeal issued a judgment addressing what makes a guarantee issued by an entity other than a financial institution a "demand guarantee" rather than a "see to it guarantee".

The Court of Appeal rejected the presumption that a guarantee issued by any entity other than a financial institution should be considered a "see to it guarantee" just because of the guarantor's status. According to the Court, what matters are the terms of the guarantee, not the guarantor's characteristics.

DEMAND AND SEE TO IT GUARANTEES

A "demand guarantee" is an absolute undertaking to pay a sum of money without reference to the details of any underlying dispute, i.e. a guarantor is obliged to pay upon receipt of a demand regardless of whether there is a dispute under the underlying contract.

In contrast, a "see to it guarantee" is a secondary obligation whereby the guarantor is liable only to the extent that the guaranteed party is liable, i.e. a guarantor can normally wait for any liability dispute arising under the underlying contract to be resolved before becoming obliged to make a payment under the guarantee.

In practice, many guarantees issued in a shipbuilding context, particularly by parent companies, contain terms that are traditionally found in both demand and see to it guarantees. In *Shanghai Shipyard Co Ltd v Reignwood International Investment (Group) Company Limited*, the Commercial Court, and subsequently the Court of Appeal, looked at the guarantee issued by Reignwood to determine how it should be characterised.

THE FACTS

Shanghai Shipyard Co Ltd (the builder) and Reignwood International Investment (Group) Limited (the original buyer and guarantor) were parties to a shipbuilding contract dated 21 September 2011 for the construction of a drillship for a total price of $200 million. The contract was subsequently novated to bring in a new buyer, Opus Tiger 1 Pte Ltd (the novated buyer), which was an indirect subsidiary of the guarantor, and a guarantee was provided by the guarantor to secure payment by the novated buyer of the final instalment of the purchase price of $170 million (the guarantee).

The novated buyer did not accept delivery of the drillship and so the builder made a demand on the guarantee. The demand was refused by the guarantor, pending resolution of the dispute as to whether the novated buyer was obliged to take delivery. After the demand had already been made, the dispute was submitted to arbitration.

THE DECISION IN THE COMMERCIAL COURT

The Commercial Court was asked to determine two issues – namely:

- whether the guarantee issued in this instance was a see to it or demand guarantee; and
- whether the guarantor was entitled to refuse payment under clause 4, pending the outcome of an arbitration between the parties in respect to a dispute regarding the novated buyer's liability to pay the final instalment:

English law will look to the language used, without the nature of the entity issuing the guarantee tainting the interpretation.

- only if the arbitration had been commenced between those parties by the date the demand was made; or
- regardless of when such arbitration was commenced.

In arriving at its decision, the Commercial Court focused on the fact that the guarantee had not been issued by a bank and, in line with case law, concluded that where an instrument is not provided by a bank or other financial institution, there needs to be cogent indications that the instrument is intended to operate as a demand guarantee. Based on the language of the guarantee and consideration of the factual background, the Court held that the guarantee was a see to it guarantee.

In respect of the second issue, the builder argued that even if the guarantee was a see to it guarantee, the proviso in clause 4 of the guarantee operated as a defence to a claim under the guarantee only if the arbitration was commenced before the demand was made, which was not true in this case. Therefore, in the absence of an arbitration, the guarantor was obliged to make payment.

The Court was not persuaded that the benefits of clause 4 would arise only when the dispute had been submitted to arbitration before the demand under the guarantee was made, and so it held that the true construction of the clause entitled the guarantor to refuse to make the payment pending the arbitration outcome, notwithstanding when the arbitration was commenced.

OVERTURN OF THE COMMERCIAL COURT'S DECISION

On 23 July 2021 the Court of Appeal unanimously overturned the Commercial Court's decision on both issues.

In respect of the first issue, the Court of Appeal emphasised the following:

"*What matters for the purposes of counterparty risk is not the nature of the business carried on by the guarantor as such, whether banking, other financial business or commercial trading activity. It is simply the commercial and financial strength and probity of the guarantor. […] [The Guarantor] clearly exercised a financing function beyond that which might arise between parent and subsidiary in an established group of companies in relation to the group's business.*

Thirdly, in the shipbuilding context it has long been established that payment and refund guarantees may be demand guarantees."

The Court of Appeal was keen to emphasise that wording took precedence over any assumptions as to the nature of the guarantee based on the guarantor or otherwise.

The Court then considered the language of the guarantee and identified the following as indicators that the guarantee was a demand guarantee as opposed to a see to it guarantee:

- the words "*ABSOLUTELY*" and "*UNCONDITIONALLY*" in clauses 1 and 3 of the guarantee, which conveyed no conditionality on the buyer's liability;
- the words in clause 1 "*[as primary obligor] and not merely as the surety*", which clearly indicated that the document was not a surety, i.e. a see to it guarantee;
- the words "*upon receipt by us of your first written demand*" in clause 4, which "*is the hallmark of a demand guarantee*";
- the words "*we shall immediately pay to you*" in clause 4, which would be inappropriate in a surety guarantee, given the time needed to investigate the underlying liability; and
- clause 7(a), which provided that obligations on the guarantor were to be unaffected by any dispute under the building contract.

The proviso in clause 4 was held merely to be a carve out of what was otherwise a demand guarantee; when triggered, "*it involves an obligation to pay against a document, namely the arbitration award. It does not involve an obligation to pay in respect of an underlying liability*".

In respect of the second issue, the builder submitted that in order for the proviso in clause 4 to be triggered and prevent a payment obligation from arising, there had to be "*both a dispute and the commencement of arbitration prior to a valid demand being made*". The buyer argued that a dispute only needed to exist. The Court disagreed with the buyer's argument on the basis that if the buyer was right, "*the on demand obligation would be suspended indefinitely by the existence of a dispute and that would occur in every case of non-payment of the delivery instalment*".

KEY TAKEAWAYS FROM THE COURT OF APPEAL'S JUDGMENT

The Court of Appeal's judgment provides guidance as to the factors that will determine whether a guarantee should be construed as a demand or a see to it guarantee. Any presumption arising solely from whether the guarantor is a financial institution, parent company or other type of entity has seemingly fallen away. English law will look to the language used, without the nature of the entity issuing the guarantee tainting the interpretation. Wording such as "unconditionally" and "immediately" and differentiation from traditional see to it guarantee obligations is likely to mean, regardless of the nature of the entity issuing the guarantee, that a guarantee is a demand guarantee.

Where a guarantee has a proviso, such as that in clause 4, that excuses payment where a dispute has arisen and arbitration has been commenced, strict compliance with both aspects must be satisfied before any demand on the guarantee is made for the payment obligation to be suspended. As such, where similarly worded guarantees are in place and it becomes apparent that a beneficiary may soon have a right to make a claim on the guarantee, this judgment is likely to lead to arbitrations being urgently commenced before any demand is made in order to provide guarantors with a basis for suspending payment.

This judgment serves as reminder of the need to be careful when drafting guarantees and to strictly adhere to their terms •

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Equipment leasing in the maritime industry

– protection of legal title

Companies leasing out equipment for use on board vessels need to be mindful of the legal risks and challenges in protecting legal title to their equipment. In this article we have highlighted potential threats and possible measures of mitigation.

Leasing equipment for use in the maritime industry may be a practical means for shipowners (the "**lessee**") to cover a short term need or avoid having to invest in expensive equipment. Typical examples of equipment being offered for lease include streamers for seismic operations, ROV's, offshore cranes and gangways. Traditionally, leasing has been offered by specialized companies that have leasing as their main business. However, more recently we are seeing a trend towards a broader use of leasing as a business model, where the possibility of leasing equipment is also being offered by equipment manufacturers and others. When entering into this market it is particularly important for the equipment owner (the "**lessor**") to be mindful of how to protect its legal title to the equipment.

A common feature of leasing is that whilst legal title in the equipment is retained by the lessor, physical possession of the equipment is handed over to and will be in the full care and custody of the lessee. In shipping this typically involves the equipment being installed on board a vessel and becoming an integrated part of the vessel's operations and unless mitigating measures are taken, there are certain situations where the lessor risks losing legal title in the equipment.

Some typical examples as seen from a Norwegian law perspective are highlighted below. The same situations will also typically represent a risk for the lessor in other jurisdictions, including under English law.

VOLUNTARY SALE OF THE VESSEL TO A BONA FIDE BUYER

In a situation where the shipowner voluntarily sells the vessel to a third party buyer with the equipment still on board, the question arises as to whether the lessor can enforce its ownership rights and demand that the equipment is returned to it by the third party buyer. In such a situation the third party buyer may argue that the vessel was purchased under the assumption that the equipment was part of the vessel and the property of the seller, and thus included in the sale.

According to the Norwegian Good Faith Acquisition Act section 1, if an object in the possession of the seller is sold to a bona fide buyer (*i.e.* a buyer "in good faith"), then the lawful owner's legal title is extinguished and the bona fide buyer assumes legal title. Whilst the lawful owner will likely have a claim for damages against the seller, if the seller is insolvent such a claim may be close to worthless. Thus, an equipment lessor may lose legal title to the equipment if the vessel buyer in good faith assumes that the seller was entitled to sell the vessel *including* the equipment.

This risk of extinction in this situation may be mitigated by the lessor by clearly marking the equipment as the property of the lessor. Furthermore, the leasing contract should include specific obligations on the lessee to make such markings clear.

CREDITORS' RIGHTS – ENFORCEMENT OF MORTGAGES

The lessor's legal title may also be threatened where a creditor with a lien against the vessel enforces its claim, *e.g.* where a bank enforces its mortgage due to default under the loan agreement. This will typically lead to a forced sale of the vessel. According to the Norwegian

Unless mitigating measures are taken, there are certain situations where the lessor risks losing legal title in the equipment.

Maritime Code section 45, (the "**NMC**") the ship mortgage comprises not only the vessel itself, but will also include the vessel's "appurtenances". In this case, the question would arise as to whether the equipment on lease would be considered as an "appurtenance" and thus encompassed by the mortgage, or not. If it is, then the mortgagee may include the equipment as part of the forced sale and the lessor's legal title may be extinguished.

Whether the lessor's equipment is or would be considered as an appurtenance turns on the facts and would of course need to be assessed on a case by case basis. A general guideline however is that all equipment intended for long-term use on board the vessel will likely be deemed to be an "appurtenance" and thus included as part of the mortgage/lien. There is no requirement for the equipment to be permanently mounted on board the vessel to be considered an appurtenance, nor does it need to be strictly necessary for the operation of the vessel.

A possible measure of mitigation is found in the act itself. According to the NMC section 45 second paragraph, if the lessee has a right to cancel the lease contract with no more than six months' notice, then the equipment will not be deemed part of the mortgage/lien. Consequently, when leasing out equipment at risk of being deemed an appurtenance under section 45 of the NMC, it may be sensible to incorporate into the relevant lease contract a right of termination for the lessee with six months' notice or less. Other possible alternatives of mitigation would require agreement with the mortgagee/creditors.

BANKRUPTCY

Finally, a situation may arise where the lessee becomes insolvent and enters into bankruptcy proceedings. The bankruptcy estate may claim that the equipment is part of the estate and that the value of the equipment is to be divided among the creditors of the lessee.

In this situation, the lessor may rely on the Norwegian Satisfaction of Claims Act section 2-2. According to this provision, the bankruptcy estate can only seek satisfaction in the property of the debtor at the time of attachment, *i.e.* when bankruptcy is declared. Since the lessor's equipment has never belonged to the lessee – the lessee has only leased the equipment – the bankruptcy estate cannot dispose of the lessor's equipment.

As the examples demonstrate, equipment owners should carefully consider the risks before entering into leasing arrangements in the maritime industry and retention and protection of legal title should be at the forefront of potential lessors' minds. To achieve this objective, equipment owners should be aware of the need for careful and tailored drafting of the leasing contracts, including, where necessary taking local law advice. •

Retention and protection of legal title should be at the forefront of potential lessors' minds.

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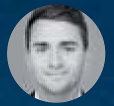
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MARPOL Annex VI – EEXI AND CII

CAN YOUR CONTRACTS COPE?

The IMO recently introduced amendments to MARPOL Annex VI aimed at improving the technical and operational efficiencies of all types of ships. These amendments are expected to enter into force as soon as 1 January 2023. The amendments introduce the Energy Efficiency Existing Ship Index (EEXI), a technical measure concerned with ship design, and the Carbon Intensity Indicator (CII), an operational measure concerned with a ship's trading and operation.

The EEXI is a one-time requirement to improve the energy efficiency of a ship's design. The regime applies to all existing ships above 400 GT falling under MARPOL Annex VI. The relevant ship will be ascribed an "attained EEXI" which will demonstrate the ship's energy efficiency compared to a baseline. The attained EEXI will then be compared to a "required EEXI" for that particular ship type. If the attained EEXI is less efficient than the required EEXI, owners will need to take steps to ensure compliance.

IMPLEMENTATION AND COMPLIANCE WITH THE EEXI

To comply with the EEXI, a Technical File will need to be prepared for most ships (excluding those already built in accordance with Energy Efficiency Design Index (EEDI) Phase 2 or 3 requirements). The Technical File will record the calculation of the attained EEXI, which must be below the required threshold.

Once completed, owners or managers of a ship must submit the File to its classification society for approval and also carry it on board. A verification process for the attained EEXI as recorded in the Technical File will then take place during the first annual survey in 2023, and, if verified, a new International Energy Efficiency Certificate (IEEC) will be issued by the classification society on behalf of the relevant flag state. The IEEC will need to be presented to port authorities, though the consequences of failing to do so are not yet clear.

Whilst there are no formal requirements for owners to make technical modifications to the ship (e.g. by installing energy saving devices or making propeller improvements), it may be the most realistic way to achieve compliance. Owners may also wish to limit engine power.

ENSURING CONTINUOUS IMPROVEMENTS TO SHIP'S ENERGY EFFICIENCY

Where the EEXI is a one-time certification, the CII regime will ensure continuous improvements to ships' energy efficiency by enforcing increasingly stricter emission targets for existing ships year on year. This will apply to all ships above 5,000 GT.

The actual CII attained will be documented (in most cases measured in grams of CO2 emitted per cargo-carrying capacity and nautical mile) and verified against the required CII. This gives a rating on a scale from A to E.

The attained CII should improve annually. Ships rated E, or ships

The new regulations will have a profound impact across all sectors of shipping, and owners in particular will need to act early in order to understand what measures are required to comply.

which for three consecutive years are rated D, will have to submit a corrective action plan showing how the required index will be achieved. To promote continuous improvement of attained CII for all ships, it is expected that incentives will be provided by administrations, port authorities and other stakeholders to ships rated A or B.

IMPLEMENTATION AND COMPLIANCE WITH THE CII

Before the CII enters into force, all ships above 5,000 GT will need to have an approved Ship Energy Efficiency Management Plan (SEEMP) in place. The SEEMP will include a plan showing how the CII targets will be achieved.

Significant reductions in a ship's CO2 emissions can be achieved in various ways, including by slow steaming, installing and implementing new energy efficiency technologies, using alternative fuels and by operational changes (e.g. rerouting or limiting cargo intake).

IMPACT OF THE NEW REGULATIONS

The new regulations will have a profound impact across all sectors of shipping, and owners in particular will need to act early in order to understand what measures are required to comply. This will involve reviewing existing charters and drafting future charters with the requirements acutely in mind.

There will be a heightened need to cooperate between owners and charterers to strike a balance between the owners' interests in adjusting to the CII regime and charterers' interests in the vessel's employment and their obligations towards third parties.

IMPACT ON EXISTING CHARTERS

In relation to the EEXI framework, owners and charterers should begin negotiating their existing charters as early as possible in order to address the various challenges. If Owners intend to conform by modifying the ship, the costs of modification will most likely be for owners' account. owners may however wish to seek an agreement from charterers that charterers contribute not only with their expertise but also by covering the direct costs of modification or by accepting increased hire. The parties will also need to discuss when and how the ship should deviate to dry dock for the modification. If owners intend to limit the engine power, they may wish to amend the vessel description and/or the speed and consumption warranties.

WHAT TO TAKE INTO ACCOUNT WHEN DRAFTING NEW TIME CHARTERS

The EEXI is not expected to cause any difficult challenges for owners once the ship has received the certificate of compliance. The CII, however, will have a serious impact on commercial contracts because it affects fundamental rights of owners and charterers in traditional charters. Key areas of impact on future charters which will need to be considered are:

- **Utmost despatch**: Most charters require the ship to proceed using "utmost despatch" or similar. Because owners may be required to slow steam or sail longer routes in order to meet the CII targets, owners should have the right to proceed with the most fuel-efficient route. The charter should also ensure that, by doing so, owners are not in breach of their utmost despatch obligation nor their obligation to meet charterers' orders.
- **Wrongful deviation and off-hire**: Sailing longer routes may constitute a wrongful deviation and accordingly put the ship off-hire. Owners should negotiate appropriate language to allow for sailing longer routes where doing so is necessary in order to comply with the CII.
- **Speed adjustments**: Most charters allow charterers to slow steam. If owners intend to reduce the ship's speed in order to meet the CII, owners should ensure that new charters also give them the right to do so.
- **Speed and performance warranties**: Owners usually warrant a certain fuel consumption at certain speeds. Owners should ensure that such warranties cover the potential need to deviate from this in order to meet the CII requirements. •

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DECARBONISATION IN SHIPPING – THE EU PROPOSALS

On 14 July 2021 the European Commission published its "Fit for 55" package setting out various legislative proposals to enable the EU to reach its objective to reduce emissions by at least 55% by 2030 (as compared to 1990 levels).

The package includes proposals for a revised Emissions Trading System (ETS) directive (which until now has excluded the shipping industry) and a new FuelEU Maritime initiative, both of which will directly impact the shipping industry.

INCLUSION OF SHIPPING – WHY NOW?

In 2018, the International Maritime Organization (IMO) adopted an initial greenhouse gas emissions strategy for international shipping, which, amongst other things, sought to reduce average carbon intensity (CO2 per tonne mile) by at least 40% by 2030 and by 70% by 2050, as well as cutting total greenhouse gas emissions from international shipping by at least 50% by 2050 (as compared to 2008).

Whilst the IMO's emissions strategy represents real progress, it has nevertheless been criticised for not going far enough. Indeed in the "Fit for 55" proposal, the European Commission has said that "*While the recent progress achieved in IMO is welcome, these measures are insufficient to decarbonise international shipping in line with international climate objectives*".

Accordingly, the EU has decided to take matters into their own hands and to expedite applying its own shipping standards as part of the European Green Deal.

THE PUBLIC LAW ASPECT

As currently drafted, the EU ETS and the FuelEU Maritime proposals hold shipping companies responsible for actions which take place both inside and outside of EU territory, including in international waters.

Applying such extraterritorial jurisdiction clearly requires a legal basis in international public law and even though the EU will argue that they have the required basis, either through port state jurisdiction or under customary principles of international law (e.g. the so-called "effects doctrine" which allows a state to exercise extraterritorial jurisdiction over matters that have a substantial impact on the state's territory), it will not be surprising if certain members of the international community seek to challenge the proposals arguing that the EU is acting ultra vires i.e. outside of its powers.

Another possible critique the EU initiative may be subject to is that it challenges the established order – namely the generally held understanding that international shipping in international waters is regulated by the IMO and the United Nations Convention on the Law of the Sea (UNCLOS), which seek global cooperation and global rule development in order to secure uniformity and avoid unilateral approaches to regulate an international and global industry. Although the EU's proposals note that the regulations will be "reviewed" if global resolutions on relevant matters are reached, the international legal aspects do not seem to have been considered, in detail, by the European Commission.

> The EU has decided to take matters into their own hands and to expedite applying its own shipping standards as part of the European Green Deal.

THE EFFECT OF THE "FIT FOR 55" PACKAGE AND THE WAY FORWARD

When viewed through a global lens, there are obvious disadvantages in introducing a scheme that places obligations on ships in the EU only. Having different burdens placed on shipowners and operators in different parts of the world may create uncertainty and lead to shipowners and operators seeking to avoid the EU scheme.

Given the pressing need for a global response to curbing greenhouse gas emissions however, it is to be hoped that the EU's approach will be seen as a trailblazer that can provide an example for the rest of the world.

The "Fit for 55" package is at this point still only at the proposals stage and will have to be negotiated with the European Parliament and EU member states before it can be adopted and take effect. Although the proposed measures are subject to criticism and no doubt have room for improvement, it is safe to say that emissions from shipping will be subject to stricter and more comprehensive legal obligations going forward. •

EU COMMISSION'S PROPOSAL AS PART OF THE "FIT FOR 55 PACKAGE"

	EU ETS	FuelEU Maritime
What types of ships are affected?	• Commercial ships over 5,000 GT • Ships that call at EU ports regardless of whether they fly an EU flag and where the ship owner is incorporated	• Commercial ships over 5,000 GT • Ships that call at EU ports regardless of whether they fly an EU flag and where the ship owner is incorporated
What is the scope?	• 100% of emissions from intra-EU voyages • 50% of emissions from voyages which start or end at an EU port	• 100% of greenhouse has emissions intensity of onboard energy used during all voyages between ports in the EU and at berth in the EU • 50% of GHG intensity of onboard energy used during voyages which start or end at an EU port
When and what quantity?	• To ensure a smooth transition, the proposal suggests a phase-in period where shipping companies only have to surrender allowances for a portion of their verified emissions and gradually rising as follows: – 20% of emissions in 2023 – 45% of emissions in 2024 – 70% of emissions in 2025 – 100% of emissions in 2026	• The cap on greenhouse gas intensity in shipping fuels is suggested to be reduced as follows: – 2% from 1 January 2025 – 6% from 1 January 2030 – 13% from 1 January 2035 – 26% from 1 January 2040 – 59% from 1 January 2045 – 75% from 1 January 2050
Who is responsible	• Ship owners or charterers – "the entity that is responsible for the choice of fuel, route and speed of the ship."	• Ship owners or charterers – "the entity that is responsible for the choice of fuel, route and speed of the ship."

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THE EU ETS EXPANDS TO SHIPPING

One of the most talked about and controversial aspects of the EU's proposed "Fit for 55" package is the European Commission's proposal for a revised Emissions Trading System (EU ETS). This article examines the proposal and details its potential impact on the shipping industry.

The EU ETS was launched in 2005 and is in essence a trading system for emissions allowances. Under the "cap and trade" principle, a maximum (cap) is set on the total amount of greenhouse gases that can be emitted by participating installations and sectors. The scheme includes energy-intensive installations and sectors such as oil refineries and steel works, as well as commercial aviation within the EEA. Included sectors account for about 45% of EU greenhouse gas emissions. Allowances are allocated for free or auctioned off and can subsequently be traded. Installations must monitor and report their greenhouse gas emissions ensuring that they have sufficient allowances in hand to cover their emissions. If emissions exceed that permitted by its allowances, then the relevant installation must purchase more allowances. Conversely, if an installation has allowances remaining at the end of the relevant trading period, it may auction off its leftover credits. The included installations and sectors therefore have a financial incentive – as well as a duty – to reduce their emissions.

As well as all EU countries, Norway, Iceland and Lichtenstein have been a part of the EU ETS through the EEA-agreement since 2008.

THE INCLUSION OF SHIPPING IN THE EU ETS

As part of its "Fit for 55" package, the European Commission has proposed extending the EU ETS to also cover emissions from shipping starting from 2023. The proposal entails that shipping companies have to surrender allowances for all emissions that occur on voyages between ports within the EU, as well as emissions that occur whilst the ships are at berth at EU ports. Moreover, the Commission's proposal also requires shipping companies to surrender allowances for 50% of all emissions stemming from international voyages to or from ports within the EU. To ensure the effectiveness of the regulation and to avoid shipowners seeking to avoid the scheme by flagging outside the EU, the EU ETS will apply to emissions from all ships calling at EU ports, regardless of whether the ships fly an EU flag or whether the shipowner is incorporated in the EU.

To ensure a smooth transition, the proposal suggests a phase-in period where shipping companies only have to surrender allowances for a portion of their verified emissions increasing on a sliding scale as follows:

- 20% of emissions in 2023
- 45% of emissions in 2024
- 70% of emissions in 2025
- 100% of emissions in 2026

RESPONSIBILITIES AND PENALTIES

The proposal sets out requirements on shipping companies, defined as the shipowner or any other entity such as the manager or bareboat charterer that has "*assumed the responsibility for the operation of the ship from the shipowner*". This definition is in line with similar definitions used by the IMO, for example, in its 1994 international safety management code for the safe operation of ships and pollution prevention (the ISM Code). Shipowners that wish to hold other entities responsible for penalties and other losses which may occur in connection with the EU ETS proposal will therefore need to ensure that this is clearly specified in their contracts. The relevant responsible company must then surrender enough allowances at the end of each year to cover their ships' emissions for the preceding year.

Member States will be responsible for administering the scheme for shipping companies incorporated in their jurisdiction. For shipping companies incorporated outside the EU, the responsibility will lie with the Member States that the non-EU shipping company had the greatest estimated number of port calls at in the last two years. If the shipping company did not carry out any voyage to the EU in the last two years, the Member State from which the ship first departs will be responsible.

If a company does not surrender enough allowances for the preceding year by 30 April in the following year, it will be held liable for the payment of an excess emissions penalty. The excess emissions penalty is currently proposed at 100 euros per tonne of CO_2 equivalent emissions the company did not surrender allowances for.

On average, a container ship falling within the scope of the proposed EU ETS emits 24 400 tonnes of CO_2 annually (based on data from 2019). Assuming a calculation year of 2026, if a shipping company fails to surrender allowances for 2500 tonnes of CO_2, approximately 10% of a container ship's average annual emissions, the excess emissions penalty would amount to 250 000 euros. Even minor deviations from the proposed directive could thus result in the responsible company incurring significant financial penalties.

If a company does not comply with the EU ETS for two or more consecutive years, Member States may issue expulsion orders against the company's ships. The ships can consequently be detained in the Member State in which they are registered or denied entry into a port of another Member State.

LOOKING AHEAD

Several aspects of the EU's proposal to include maritime emissions in the EU ETS remain unclear. For instance, the proposal does not detail how free allowances will be allocated to shipping companies. Moreover, it is still not clear how the revenues from the expanded EU ETS will be utilised and to what extent this will benefit the individual shipping companies or the shipping industry at large.

Although the EU Parliament and the EU Council are yet to consider the proposal, it is assumed that it will not be heavily amended. It is therefore likely that shipping will be included in the EU ETS by 2023. Shipping companies and others affected should therefore start planning ahead and ensure they have processes in place to ensure compliance with the EU ETS. •

> To ensure the effectiveness of the regulation and to avoid shipowners seeking to avoid the scheme by flagging outside the EU, the EU ETS will apply to emissions from all ships calling at EU ports, regardless of whether the ships fly an EU flag or whether the shipowner is incorporated in the EU.

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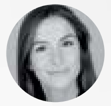
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NEWS & VIEWS

• PERSONELL NEWS • SHORT TOPICS • SECTOR NEWS •

"Yara Birkeland" shipboard visit

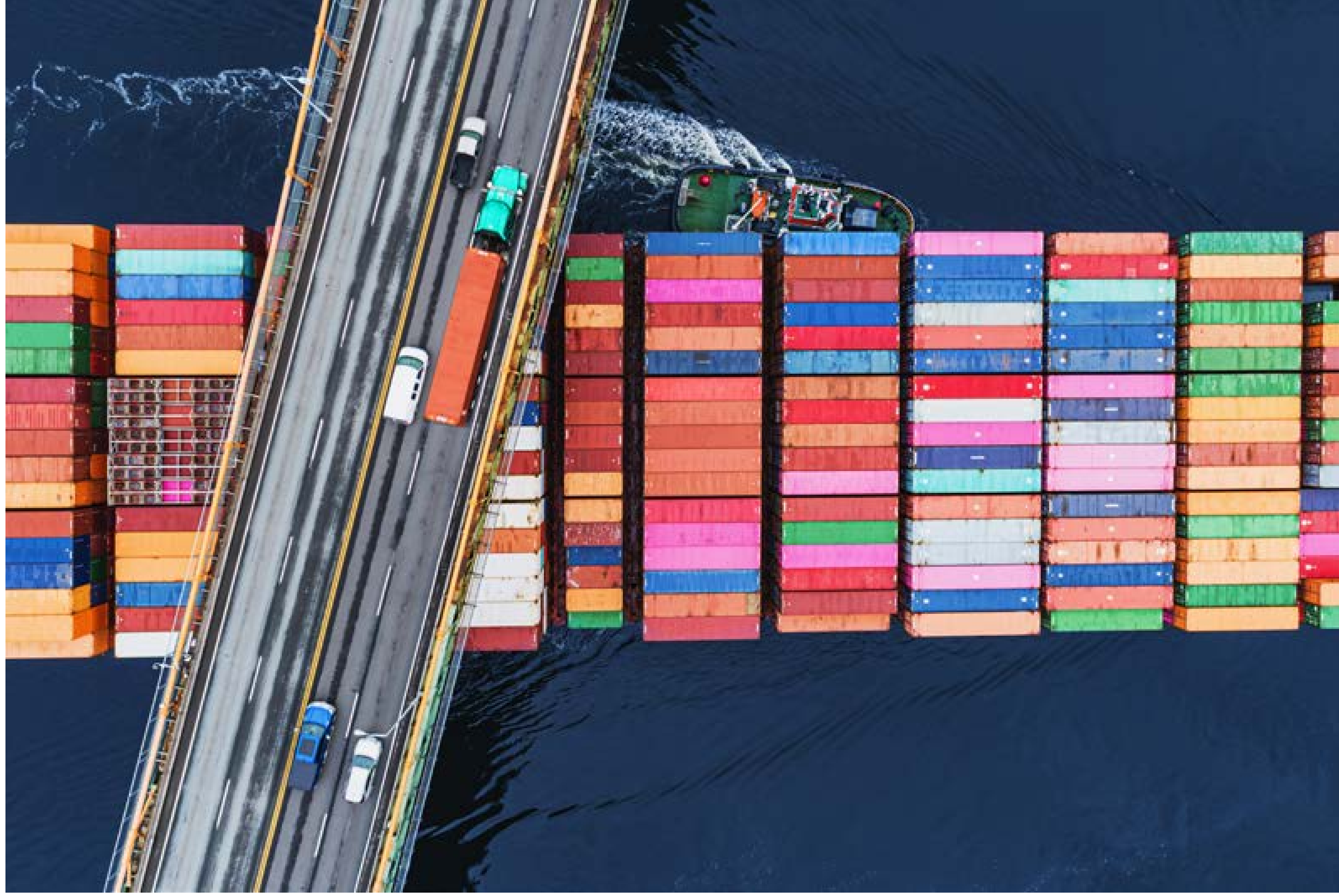
Yara recently invited Wikborg Rein's Herman Steen and Sindre Slettevold on board the world's first electric and (soon-to-be) fully autonomous container vessel, "Yara Birkeland", for a tour during her first and only voyage to Oslo. This truly fascinating, futuristic and inspiring project is a collaboration between several different stakeholders in the Norwegian maritime cluster.

Norwegian Maritime Law Day 2021

The Norwegian Maritime Law Day was held for the first time this November. The fully booked event had participants from nsurance companies, brokers, law firms and academics. Wikborg Rein partner Herman Steen contributed to the conference with a talk by on limitation of liability and choice of law. Steen's presentation was part of a series of talks on different issues in relation to fires on board container vessels together with Are Solum (Gard), Fredrik Doksrød-Olsen (Gard) and Helle Hammer (Cefor). The event was hosted by the Norwegian Maritime Law Association in co-operation with the Scandinavian Institute of Maritime Law.

Key aspects of

FuelEU Maritime proposal



On 14 June 2021, the European Commission presented a package of proposals aimed at ensuring that the European Union achieves its goal of cutting greenhouse gas emissions by at least 55% by 2030. The proposals include, amongst other things, the new FuelEU Maritime initiative, specifically aimed at the shipping industry.

The FuelEU Maritime proposal, together with the proposed implementation of the EU Emissions Trading System (the ETS) (on which we comment in a separate article) and the EU Energy Taxation Directive (the ETD), forms part of a basket of measures designed to, amongst other things, ensure emission reductions in the shipping sector by increasing demand for renewable and low carbon fuels.

The FuelEU Maritime proposal is of course highly technical in nature, however, at its core, the proposal aims to implement two specific measures, namely:

- an obligation for certain types of vessel to use an onshore power supply or zero-emission technology in ports; and
- the introduction of increasingly stringent limitations on the carbon intensity of fuels/energy used on board vessels.

The obligation to use an onshore power supply or zero-emission technology in ports is so far only proposed to apply to containerships and passenger vessels, and is not set to kick in until 1 January 2030. The reason for limiting its application only to the container and passenger vessels is that these are the vessels which, according to data collected by the European Union, produce the highest amount of emissions at berth. Although this part of the regulation currently only has a limited scope, there is a relatively high likelihood that the scope may be expanded to include other vessel types in time.

Due to this measure's limited application however, this article focuses on the second measure, namely the requirement to reduce the greenhouse gas intensity of fuel/energy used on board vessels.

LIMITING GREENHOUSE GAS INTENSITY OF ENERGY USED ON BOARD VESSELS

As drafted, the proposed limitation on greenhouse gas intensity will apply only to vessels with a gross tonnage of over 5,000 GT, regardless of the vessel's flag. Various types of vessel will however be exempted, such as fishing vessels, naval vessels and government vessels used for non-commercial purposes.

For those vessels to which the proposal will apply, the required reductions in the carbon intensity of fuels/energy used on board will be applied on a sliding scale based on the following timeline:

- a reduction of -2% from 1 January 2025;
- a reduction of -6% from 1 January 2030;
- a reduction of -13% from 1 January 2035;
- a reduction of -26% from 1 January 2040;
- a reduction of -59% from 1 January 2045; and
- a reduction of -75% from 1 January 2050.

How these reductions are to be achieved is not specified however. As a result, there has been some criticism that many shipowners will, at least initially, simply look to switch from more carbon heavy bunker fuels to lower emission fuels such as liquefied natural gas (from fossil fuel sources) and biofuels rather than seeking to switch to the use of zero-emission fuels such as electricity, hydrogen and ammonia. Whilst the European Commission has responded to such criticism by including specific provisions aimed at reducing the use of biofuels, biogas, renewable fuels of non-biological origin and recycled carbon fuels in its proposal, there will no doubt be continued criticism that the proposals does not go far enough, at least in the early phase of its application.

In terms of its scope, the regulation is intended to apply to all fuel/energy used by vessels on voyages between EEA member states' ports of call. To disincentivise shipowners from seeking to avoid their responsibilities by evasive port calls, it will also apply for voyages departing from or arriving to a member state port of call but where the last or the next port of call is in a third country outside the EEA, albeit to only 50% of the energy consumed.

To reward good practice, in the event that a vessel has a compliance surplus for a particular reporting period, it is proposed that shipowners may bank that surplus to the same vessel's compliance balance for a subsequent period and if a vessel has a compliance deficit for a reporting period, shipowners may, within certain limits, borrow from a projected future compliance surplus. Shipowners will also be allowed to pool

> Where a vessel has failed to present a valid FuelEU certificate of compliance for two or more consecutive reporting periods and where other enforcement measures have failed to ensure compliance, the competent authority of the member state of the port of call may issue an expulsion order.

the performances of different vessels within a fleet and use the possible overperformance of one vessel to compensate for the underperformance of another vessel.

The person or organisation responsible for compliance with the regulation is intended to be the shipowner or any other organisation or person, such as the manager or the bareboat charterer, who has assumed the responsibility for the operation of the vessel from the shipowner. This definition is in line with similar definitions used by the IMO, for example, in its 1994 international safety management code for the safe operation of ships and pollution prevention (the ISM Code). Shipowners that wish to hold other entities responsible for penalties and other losses which may occur in connection with the FuelEU proposal will therefore need to ensure that this is clearly specified in their contracts.

The relevant responsible entity will also be responsible for monitoring and reporting relevant data for each of its vessels. Monitoring and reporting must be complete and cover the fuel/energy used on board vessels whilst they are at sea as well as at berth and the data provided will be required to be verified by accredited, independent and competent verifiers. Based on the data, the verifiers will then calculate and establish the annual average greenhouse gas intensity of fuel/energy used and the vessel's balance with respect to the applicable limit. Provided that there is no deficit, the verifier will issue a FuelEU certificate of compliance.

For any vessel that does not meet the annual limits, a penalty system will be established, with the penalties being calculated on the basis of specific rules set out in an annex to the regulation. Generally speaking however, the penalties will be based on the amount and cost of renewable and low-carbon fuel that the vessel would have needed to use in order to meet the relevant requirements and the FuelEU certificate of compliance will not be issued until all penalties have been paid. Within the European Union, penalty payments received will be allocated to support projects aimed at the rapid deployment of renewable and low-carbon fuels in the shipping sector.

In addition, where a vessel has failed to present a valid FuelEU certificate of compliance for two or more consecutive reporting periods and where other enforcement measures have failed to ensure compliance, the competent authority of the member state of the port of call may issue an expulsion order. Upon the issuance of such an expulsion order, all other member states shall refuse entry of the vessel to their ports. Where the vessel flies the flag of a member state, the member state concerned may also order a flag detention until the relevant company fulfils its obligations.

COMMENT

The feedback period for the proposed new FuelEU regulations ended only on 8 November 2021, the results of which will now be summarised by the European Commission and presented to the European Parliament and Council for subsequent discussion and negotiation. It therefore remains to be seen whether the FuelEU Maritime proposal will be adopted, either in its current or in a modified form. However, with the increased focus on decarbonisation and transition to alternative low and zero-emission fuels, it seems clear that the shipping sector needs to be prepared for significant additional regulations in the months and years to come. •

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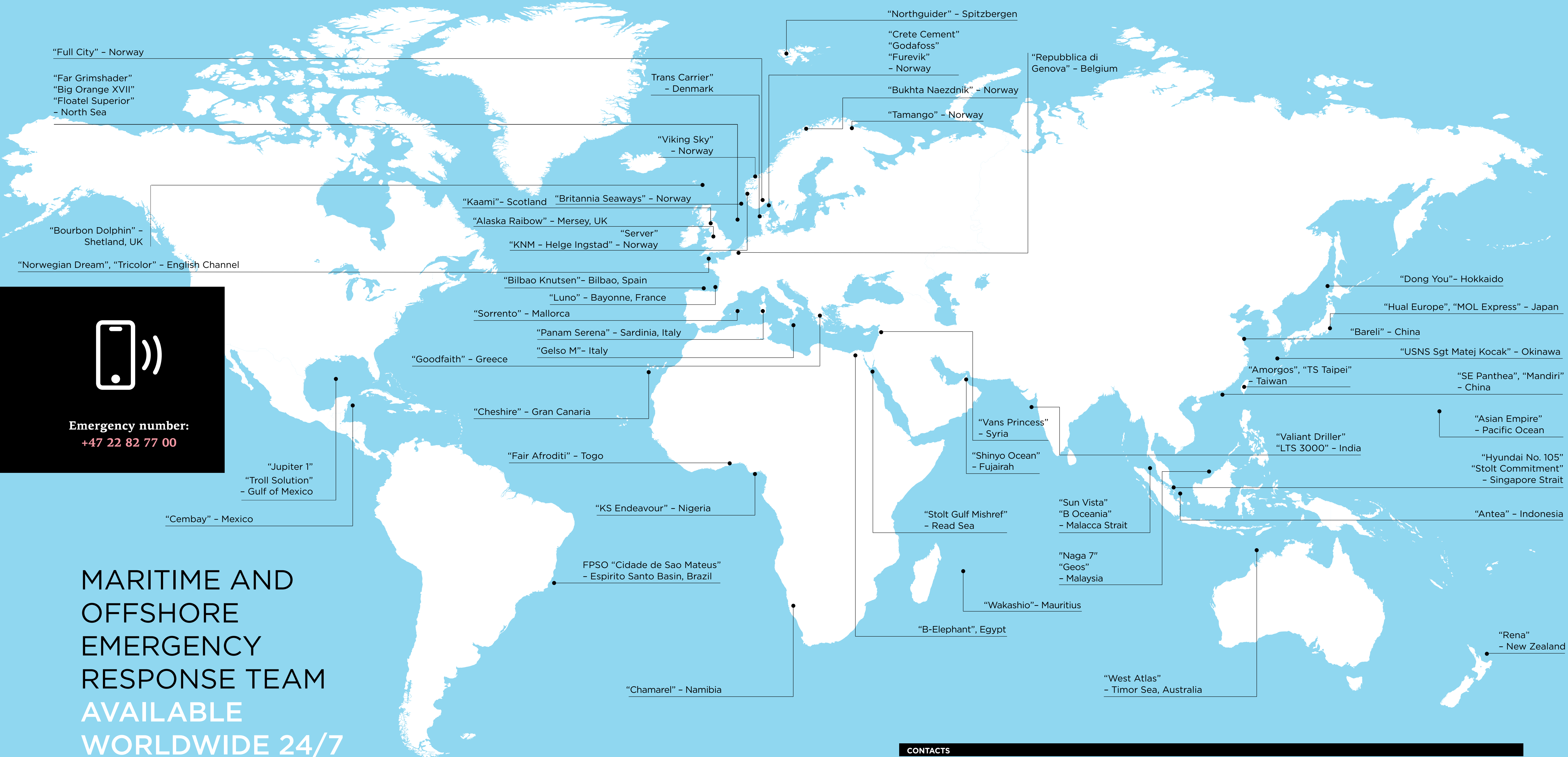

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MARITIME AND OFFSHORE EMERGENCY RESPONSE TEAM AVAILABLE WORLDWIDE 24/7

Members of our Maritime and Offshore Emergency Response Team have extensive experience in handling the practical and legal issues associated with casualties and maritime emergencies. Our team, led by Morten Lund Mathisen, assists insurers and owners in connection with a wide range of incidents.

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