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Laytime and demurrage clauses in contracts of sale – how to make it work

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Definitions and abbreviations

B/L	Bills of Lading
CIF	Costs, insurance, freight
C/P	Charterparty
Demurrage	Liquidated damages. Been defined as "an agreed amount payable to the owner in respect of delay to the Vessel once the Laytime has expired, for which the owner is not responsible. Demurrage shall not be subject to exceptions which apply to Laytime unless specifically stated in the Charter Party.[1]
FOB	Free on board
JBL	Journal of Business Law
L&D	Laytime and demurrage
LMCLQ	Lloyd's Maritime & Commercial Law Quarterly

[1] BIMCO: Laytime Definitions for Charter Parties (2013) clause 30, as published 10th September 2013. Earlier VOYLAYRULES 93.

Laytime	Amount of time allowed in a voyage charter for loading and/or discharging operation
S/C	Sale contract

1. Introduction

In every commercial sale the contracting parties will seek certainty[2] when it comes to their rights and obligations under the contract. This is especially true for provisions concerning time and money, as these elements are generally considered to be of immense importance to commercial parties.[3]

One of such obligations is the agreed laytime used for loading and discharge operations of the chartered vessel and the following liquidated damages[4] in the form of demurrage if the laytime is exceeded. Such clauses are usually found in voyage charterparties, but a CIF seller or FOB buyer acting as charterer would be eager to pass on the risk of this cost to the other party under the contract of sale concluded on shipment terms. The reason being that they generally have no control over the discharge or loading process, respectively. It is important to emphasise that the risk here mentioned is in terms of carriage under the charterparty and not as the concept is perceived in international trade relating to the goods.

The understanding on how to draft such clauses in order to make them work has immense financial importance for the parties involved because money turns on the wording of the clause if laytime is exceeded. The fine differences in wording have

[2] See here Lord Bingham in *The Starsin* [2004] 1 AC 715 [13], quoting Lord Mansfield. Also Thomas D.R, *The evolving law and practice of voyage charterparties* (Informa Law, 2009) p. 175.
[3] See here also Sale of Goods Act 1979, S. 62 (2) which refers to the common law.
[4] Lord Dunedin held "the essence of liquidated damages is a genuine covenanted pre-estimate of damage" in *Dunlop Pneumatic Tyre Co. Ltd v. New Garage & Motor Co. Ltd* [1915] AC 79.

implications on the construction and the very understanding of laytime and demurrage clauses in sale contracts.

If the laytime and demurrage clause in the contract of sale is seen as an independent obligation regardless of the charterparty, the consequence is that demurrage might be payable under the sale contract but not under the charterparty itself, giving the other party a benefit, which might be regarded as unjustifiable.

In addition, the two different provisions might provide terms that does not reconcile as to the period of laytime and amount payable as demurrage. There is also several issues relating to the commencement of laytime and the exceptions found in the charterparty. These problems are especially relevant when the clause makes a reference to or incorporates a rate from the charterparty, thereby strengthening the relevance of the charterparty in the construction.

The aim of this dissertation is to examine how the authorities have construed laytime and demurrage clauses in the contract of sale and how one should draft such clauses in order to avoid making them payable when they are not under the charterparty. In addition, the dissertation will undertake to answer what nature and effect these clauses have and if the law of penalties can avoid making these clauses independent under the sale contract. The dissertation will use authorities from case law in order to determine where the law stands on these issues. The dissertation restricts itself to deal with laytime and demurrage clauses in contracts of sale under English Law and will therefore not deal with incorporation issues related to bills of lading or the many problems related to the calculation of laytime in charterparties.

1.2 Legal and commercial background: 'Your delay is my cost'

Voyage charterparties or contracts of affreightment, are considered to be the governing contract between the shipowner and the charterer. The party that has undertaken to load and discharge the cargo may vary depending on the shipment terms used and obligations the parties have agreed, but the single most important factor for the shipowner under a voyage charterparty is the usage of time since other fixtures might be waiting. Time is therefore money and the shipowner or carrier is therefore eager to regulate this variable.

The amount of time allowed in a voyage charter for the loading and discharge operation is therefore usually set out as laytime in the charterparty. If the time is exceeded, the vessel will then be on demurrage, which are liquidated damages for exceeding the agreed time at disposal. The demurrage provision therefore shifts the risk of delay onto the charterer, which is the closest party to regulate the loading and discharging process.

This is the basis for the expression 'your delay is my cost' where the shipowner has no interest in covering expenses arising from delays he is not responsible for, nor has any control over. The shipowner therefore shifts the risk of delay onto the charterer, who in turn tries so shift it over to the CIF buyer or FOB seller under the sale contract. The charterparty usually exist because either party has to fulfill his obligation to transport the goods under the sale contract. The charterparty is therefore entered into by the charterer which can be either the CIF seller or the FOB buyer.[5]

[5] There are several variation to this and the parties have the freedom to make any arrangements they may please.

Consequently, these laytime and demurrage clauses are found in charterparties between the shipowner and the charterer and traditionally not in contracts of sale between the seller and the buyer. Their natural habitat is therefore not within contracts of sale at all. This causes problems with their interpretation, construction and how they are to be regarded next to their counterparts in charterparties if there are any inconsistencies and especially if there is a reference to the charterparty itself.

Firstly, what is the relationship between the two sets of clauses? Is the default position that they are free and independent or can they act as an indemnifying provision? This is especially relevant if the clause in the sale contract refers to the charterparty terms or incorporates a rate and there is an inconsistency between the clauses.

Secondly, if they are regarded as free and independent, what does the usage of general words of incorporation or reference to the charterparty terms in the sale contract do towards their construction and interpretation? How is the exceptions under the charterparty to be understood and when does the laytime commence?

And thirdly, if a cesser clause in the charterparty protects the charterer against demurrage costs under the charterparty, would it not be considered unfair that the seller can claim demurrage under the contract of sale even though no such costs have been incurred under the charterparty?[6] And if not, would not the law of penalty strike

[6] This was the case of *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.) where it was held to be an indemnity clause. The idea that a CIF seller could take such a benefit of a cesser clause has later been described as 'unappealing' in *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [32].

down any possibility of claiming liquidated damages when no demurrage has actually occurred under the charterparty?

2. Laytime and demurrage clauses in sale contracts

2.1 Is the law on charterparties and bills of lading relevant for interpretation and construction?

One of the most obvious answers to this is that charterparties and bills of lading quite simply operate under a different contractual regime than the sale contract, giving limited amount of relevance to sale contracts. It would therefore seem that the only possibility would be by way of analogy. The understanding of the laytime and demurrage provision as an incorporation clause will depend on the drafting of the clause itself and how many elements it relies on from the charterparty.

The understanding will depend on the wording of the clause itself as a mere reference to the laytime an demurrage clause in the charterparty must be seen as a certain type of incorporation, at least of a rate if not more. If the view is taken that the laytime and demurrage clause is free and independent, it would also seem to be counter-productive to regard the clause as a type of incorporation because one would then strengthen the linkage towards the charterparty to such a degree that it would seem natural to regard the clause as operating by way of indemnity. If the parties have agreed on a laytime and demurrage clause referring to the charterparty, the exact scope and wording of the clause must be assessed.

One of the reasons for not applying the same principles is that the law of charterparties is highly developed, but its primary focus is on the ship, and not the

goods being carried.[7] Consequently, the law of charterparties would, *prima facie*, not be able to aid the construction and incorporation of laytime an demurrage clauses since they deal with a different subject-matter entirely and therefore would seem not to relevant to the right and obligations of the parties under a sale contract which deals with the goods or commodity.

However, there are cases where charterparty law has been used for the construction of laytime and demurrage clauses in contracts of sale. The restrictions from the charterparty regime applied *mutatis mutandis* to the laytime and loading rate under the sale contract in *The Bonde.*[8] If the parties' intentions is the ultimate aim of construction based on the language used,[9] it could be asked if similar situations could aid such a construction.

In general, incorporation from the charterparty by general wording into the bill of lading is effective as a general principle from the law of contract.[10] There are however challenges with the identification of the charterparty,[11] which terms that are incorporated[12] and if the wording can be manipulated. The purpose is to make the receiver or bill of lading holder liable for freight, demurrage or other obligations.

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[7] Chuah J, *Laytime and Demurrage Clauses in Contracts of Sale – A Survey of the New York Society of Maritime Arbitrators' Awards (1978 – 2008) and English Case Law* (Informa Law, 2009) at page 178.
[8] *The Bonde* [1991] 1 Lloyd's Rep 135.
[9] *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50 [14].
[10] Treitel G, et al, *Carver on Bills of Lading* (3rd edn, Sweet & Maxwell, 2011) 3-014.
[11] See *Pacific Molasses Co v Entre Rios CN. ("The San Nicholas")* [1976] 1 Lloyd's Rep. 8 and *Partenreederei MS "Heidberg" and another v Grovenor Grain and Feed Co. Ltd ("The Heidberg")* [1994] 2 Lloyd's Rep. 287.
[12] *TW, Thomas & Co. Ltd v Portsea SS Co Ltd. ("The Portsmouth")* [1912] AC 1, where an arbitration clause was not found to be germane by The House of Lords.

In *The Miramar*[13] the House of Lords answered the question of manipulating the charterparty terms so that consignee became liable for demurrage negatively. The reasoning given was partly due to the fact that the consignee is "accepting blindfold a potential liability to pay an unknown and wholly unpredictable sum for demurrage".[14] This point is also mentioned in other authorities.[15] There is a similarity here towards the CIF buyer or FOB seller, which rarely will have any access to the charterparty terms as they are not charters and therefore an argument could be put forward that the same considerations and restrictive approach should be applied.

The reasoning for applying charterparty law in *The Bonde*[16] has been said to prevent the potential far-reaching implications the buyers argument had.[17] It would seem far-fetched that this argument itself would limit the precedence of the case. The case has been seen as "the most explicit example of a judicial tendency to apply to sale clauses the rules developed by the courts for the construction and application of laytime an demurrage clauses in charterparties".[18] The tendency can be explained by the close similarity towards charterparties and the problems that there arise. When a type of clause is taken out of its natural habitat and the law on this area is scarce, the understanding of the clause can be helped by looking at how it is perceived under the charterparty.

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[13] *Miramar Maritime Corp v Holborn Oil Trading Ltd ("The Miramar")* [1984] AC 676 [685].
[14] Ibid.
[15] A point made in *Jindal Iron & Steel Co Ltd. V Islamic Solidarity Shipping Co. ("The Jordan II")* [2005] 1 WLR 1363 [25] by Lord Steyn.
[16] *The Bonde* [1991] 1 Lloyd's Rep 135.
[17] Chuah J, *Laytime and Demurrage Clauses in Contracts of Sale – A Survey of the New York Society of Maritime Arbitrators' Awards (1978 – 2008) and English Case Law* (Informa Law, 2009) at page 176.
[18] Debattista C, Laytime and demurrage clauses in contracts of sale – links and connections 2003 LMCLQ 508 at 523.

There are also several other examples from the authorities. The tendency to borrow from the law of bills of ladings has also shown itself when it comes to the incorporation of arbitration clauses into a retrocession contract.[19] And "some assistance is to be derived from the general approach of the Courts" from cases concerning the incorporation from charterparties into bills of lading when it comes to the incorporation of a time bar clause into a sale contract.[20] This has been followed up where the question was if the incorporation of charterparty terms into the sale contract was valid.[21]

Thereby it could be argued that the law of charterparties concerning the incorporation into bills of lading can apply *mutatis mutandis* to incorporation of laytime and demurrage in contracts of sale. The situation can be said to be analogous to the incorporation of charterparty terms into bills of lading.

However, this provides uncertainty for the parties to the sale contract because any exceptions might not be a part of the sale contract at all. The better view seems to be that it would be difficult to understand the nature of a laytime and demurrage clause in the sale contract as independent if exceptions under the charterparty apply to the contract of sale without being mentioned in the clause under the sale contract.

[19] *Excess Insurance Co Ltd v Mander* [1997] 2 Lloyds Rep. 119.
[20] Judge Rix, as he then was, in *OK Petroleum A.B. v. Vitol Energy S.A.* [1995] 2 Lloyd's Rep. 160 [165].
[21] *Ceval Alimentos S.A. v Agrimpex Trading Co. Ltd (The "Northern Progress" No. 2)* [1996] 2 Lloyd's Rep. 319 [330].

It is also tempting to draw a line towards general incorporation issues under contracts of sale regarding time bar provisions, arbitration clauses and jurisdiction clauses incorporated from charterparties. These situations can also be said to be analogous towards incorporation of demurrage clauses because the same issues of construction arise.

There are several cases bearing resemblance to the incorporation issue. For instance the incorporation of a time bar relating to demurrage was answered negatively in *OK Petroleum v Vitol Energy*.[22] The main reasoning being that the incorporation cannot be construed wide enough if the provision was not a part of the subject-matter of the contract and merely ancillary to it, and therefore not germane to the right and obligations of the parties.[23] And the general incorporation of the whole of a charterparty was also answered negatively in *The Northern Progress No.2*.[24]

Furthermore, if there is a cesser clause in the charterparty, one could argue that the liability for demurrage under the sale contract "flies in the face of commercial reality"[25] so that it is unreasonable, the parties must make such an intention clear and if not it cannot be incorporated. It can therefore be suggested that there is some legal basis for applying the principles of construction as set out by the law of charterparties to sale contracts and that the benefits of doing so are several. Another question is how much commercial sense and certainty such a use of analogy would provide for the parties.

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[22] *OK Petroleum A.B. v. Vitol Energy S.A.* [1995] 2 Lloyd's Rep. 160.
[23] *OK Petroleum A.B. v. Vitol Energy S.A.* [1995] 2 Lloyd's Rep. 160 [168].
[24] *Ceval Alimentos S.A. v Agrimpex Trading Co. Ltd (The "Northern Progress" No. 2)* [1996] 2 Lloyd's Rep. 319.
[25] *Ceval Alimentos S.A. v Agrimpex Trading Co. Ltd (The "Northern Progress" No. 2)* [1996] 2 Lloyd's Rep. 319 [330].

On the other side, there are some considerable differences between these two types of contract. This is shown by the fact that the courts have been described as having a restrictive approach to the construction of general words incorporating charterparty terms into the bills of lading,[26] partly due to the fact that charterparty terms contain elements not relevant between carrier and B/L holder and that it is not plausible that the parties intended such incorporation.[27] The same reasoning applies to charterparty terms and the buyer and seller under a contract of sale, since these are also two different contractual environments. The terms of the charterparty are not material relevant towards a CIF buyer or FOB seller and it would therefore seem too remote to use these cases by way of analogy and a restrictive approach should in the view of the author be used. In addition to the fact that the subject matter is different, it would seem difficult to the parties under a sale contract to be certain of their rights and obligations if the exceptions under the charterparty might apply to the sale contract.

Furthermore, several authors have expressed the view that the "stricter rule" which governs incorporation of charterparty terms into bills of lading does not apply to contracts generally.[28] It has also been pointed out that a laytime and demurrage provision might refer to or incorporate from a charterparty, but that the provision itself is in an otherwise independent sale contract regime.[29] It is therefore submitted that since these are two different contractual regimes, which deals with different subject-matters, the better view seems to be that one cannot in general rely on

[26] Treitel G, et al, *Carver on Bills of Lading* (3rd edn, Sweet & Maxwell, 2011) 3-014.
[27] Ibid.
[28] See Treitel G, et al, *Carver on Bills of Lading* (3rd edn, Sweet & Maxwell, 2011) 3-015.
[29] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [42, vi].

charterparty law to solve issues on laytime and demurrage clauses in sale contracts. The most important difference being the disparity in the function and materiality of the two different contracts.

2.2 Construction: indemnity or individual clauses?

A good starting point as to interpretation of contractual terms is found in *The Rainy Sky,*[30] where the Supreme Court held that the ultimate aim is to determine what the parties meant by the language used by ascertaining what a reasonable person would have understood the parties to have meant. Furthermore, a "relevant reasonable person is one who has all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract".[31]

There should be no apparent reason why the same principles of interpretation should not be applied to laytime and demurrage provisions in contracts of sale, as these are in fact provision found in the same type of contract. Since the charterparty terms often are drawn up after the sale contract is concluded, it must be kept in mind when construing a sale contract term, that the background knowledge of the parties might be limited.

In *The Suzuki*[32] the Court of Appeal held that a CIF contract stating "demurrage as per charter-party or freight agreement" should be construed as a contract of indemnity based on the language used and consequently the appeal was dismissed. The judge also pointed out that an obligation to pay demurrage irrespective of the sellers obligations was an addition to the price paid and "one does not quite see why the

[30] *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50.
[31] *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50 [14].
[32] *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.).

parties should enter into such a contract".[33] The point made is a valid one as one of the physical duties of a CIF seller is to ship or procure a shipment of goods in accordance with the contract and thereby procure the proper shipping documents to the buyer.[34] In other words the buyer pays for, among other things, to avoid the undertaking and risks of being held accountable for demurrage to the shipowner. It would seem not to make any commercial sense that a CIF buyer would enter into a sale contract undertaking responsibility for liquidated damages without, most likely, knowing the rate. And in addition, to be accountable for demurrage under the contract of sale even though no demurrage has incurred under the charterparty. This paradox is even more visible when the incorporation is seen from the view of the FOB seller since he does not have anything do to with the goods as soon as they are shipped at the port of loading.

If the development is a tendency that the CIF seller (charterer) discharges liability under the charterparty and shifts the risk towards the CIF buyer, the buyer might be better off concluding the sale contract on FOB shipment terms so that he is in full control of the charterparty terms himself and able to make the now FOB seller liable for demurrage at the loading port.

Taking these observations into account, the better view would seem to be that the words "Demurrage as per charter-party" should be construed as being an indemnity, making it payable at the respective rate only if it is actually payable under the relevant charterparty. However, the developments from the authorities suggest otherwise.

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[33] Lord Justice Bankes in *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.) [171].
[34] Bridge M, et al, *Benjamin's Sale of Goods* (8th edn, Sweet & Maxwell, 2010) at 19-010.

A fair question to ask is what benefit there is to regard the laytime and demurrage provision as one of indemnity rather than free and independent. It is necessary to point out that regardless of what one find to be most beneficial, it is the parties intentions which are predominant in the construction, save that it would provide more commercial common sense to follow the position which provides equal benefits for both parties if possible.

Firstly, one would avoid the situation where a CIF buyer or FOB seller would be liable for demurrage under the sale contract and the counterparty is not liable due to a cesser clause, making no demurrage payable under the charterparty itself. The courts have described such a benefit or windfall as 'unappealing'.[35] The question if the law of penalty would aid the other party is further discussed in chapter 3.

Secondly, it is not uncommon for the parties under a CIF contract to incorporate terms, which at the contracting time is unknown to one contracting party.[36] If the precise rate of demurrage is unknown because the charterparty has not yet been drawn up, the situation would not be any different from the view of regarding the clause free and independent if it also incorporates a rate from the charterparty.

Thirdly, the wording "As per charterparty" can be construed as not only referring to the rate but also to the amount actually payable under the charterparty, meaning antithetic that if no demurrage is payable under the charterparty, neither should any be payable under the sale contract. Even if the laytime and demurrage clause is seen as free and independent, one does not escape the fact that was admitted in *The Devon*,

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[35] Lord Justice Mance in *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [32].
[36] Point made by Judge Rix in *Ceval Alimentos S.A. v Agrimpex Trading Co. Ltd (The "Northern Progress" No. 2)* [1996] 2 Lloyd's Rep. 319 [327].

that the function of the liquidated damages is "a genuine pre-estimate of the recovering party's exposure".[37] It would therefore seem that an isolated view of the laytime and demurrage clause would not easily be reconciled with the intentions of commercial parties so that one of the parties should cover the others expenses if they have not incurred any.

This last remark goes to the very root of any reservation against regarding theses clauses as free and independent. The terminology demurrage is found in charterparties as liquidating damages due to exceeding the laytime agreed. If the same type of clauses operates in a different contractual environment, the same justifications for their existence is no longer valid, especially when no demurrage is payable under the charterparty. It can then be argued that these clauses have a different nature than their counterparts in charterparties, because they no longer relate to the liability for exceeding laytime at all.

Nevertheless, the rationale in *The Suzuki*[38] has not been greatly followed and the opposite conclusion has been drawn in several cases. The reasons for doing so has been that the relevant laytime an demurrage clause is followed by detailed provisions about notice of readiness and calculation of laytime[39] or that a free standing provision provides certainty so that the parties will know where they stand.[40] Another reason is the difficulties one has where there are several charterparties to choose a rate from.

The case law does not provide consistency when it comes to the construction. This is

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[37] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [35].
[38] *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.).
[39] *Gill & Duffus S.A. v Rionda Futures Ltd.* [1994] 2 Lloyd's Law Rep. 67 [77].
[40] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [33-34].

shown by the case of *Gill & Duffus,*[41] where the same wording as used in *The Suzuki*[42] gave a different result. The laytime and demurrage clause was in *Gill & Duffus* not construed to be an indemnifying provision. This could stand for the proposition that the wording itself is not predominant as to the nature or that there has been a development in the authorities so that this wording itself is not enough to regard the provision as indemnifying. Following later authorities it seems evident that it is not possible to conclude on the nature of the clause merely by looking at the wording itself but that the context and references made to the charterparty[43] must also be considered.

One natural consequence of shifting the risk so that the laytime and demurrage clause is free and independent would be that the CIF buyer or FOB seller would be entitled to any despatch money if the clause so provides and the cargo has been loaded or discharged quicker than anticipated. The author has however not found any authority for this, but it would follow as a natural consequence of agreeing that the risk is on the other party, and thereby also the benefits should be attributable to the party.

These justifications can be questioned as it has later been held that certainty in itself is not a principle, but "a desideratum and a very important one, particularly in commercial contracts. But it is not a principle and must give way to principle. Otherwise incoherence of principle is the likely result".[44]

One of the principles of construction which goes against construing the laytime and

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[41] *Gill & Duffus S.A. v Rionda Futures Ltd.* [1994] 2 Lloyd's Law Rep. 67.
[42] *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.).
[43] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [42, iv].
[44] *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha* [2007] 2 WLR 691 [38] by Lord Scott of Foscote.

demurrage clause as free and independent is the fact that the wording of the clause often directly refers to the charterparty or incorporates the clause by the wording "Demurrage as per charterparty".

In the general law of contract, if a clause is ambiguous the wording will normally be construed against the party relying on it following the rule of *contra proferentem*.[45] The rule has seemingly not been applied to cases where one sets out to determine the nature of a laytime and demurrage clause in a sale contract. The reason for this might be that the clause itself is not perceived as ambiguous by the courts by construing the clause according to the intention of the parties.

Another possibility is that the rule is less favourable following *The Rainy Sky*, where it was pointed out that if there is a possibility of more than two possible constructions "the court is entitled to prefer the construction which is consistent with business common sense and to reject the other".[46] If the laytime and demurrage clause in sale contracts can be construed both as a free and independent clause and as indemnifying, one could ask which approach is most consistent with business common sense.

Following the authorities cited above and the better view seems to be that it would make more business common sense to perceive the nature of a laytime and demurrage clause as free standing and independent because one then avoids the issues of discrepancies between the two sets of contracts and identifications issues. However, the freedom of contract principle still applies and "the weight to be given to the commercial consequences must depend on the degree of ambiguity of the language

[45] See for instance *Glynn v Margetson* 1893 AC 351 where the principle was used in relation to a deviation clause in a charterparty.
[46] Lord Clarke of Stone-cum-Ebony JSC in *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50 [21].

concerned".[47] The construction of the laytime and demurrage clause will therefore depend on the context and wording used.

2.3 The 'default position'

Some authors have taken the view that the default position is that laytime and demurrage clauses in contracts of sale stand free and independent of their counterparts in the relevant charterparty.[48] This can be supported by one of the highest authorities on the interpretation and construction of theses clauses in contracts of sale, which suggests that they are independent. In *The Devon,*[49] the laytime and demurrage provisions in the contract of sale provided demurrage payable "As per charterparty per day pro-rata".

The dissenting Lord Justice Buxton favoured the position that their nature was one of indemnity. The reasoning adopted is based on the notion that the seller might incur expenses in performing the contract of carriage and they are therefore included in the sale contract, which "is the very essence of an indemnity".[50]

The majority of the Court of Appeal held that the clause was an independent obligation and that only the rate was incorporated.[51] It would therefore seem that the default position should be that these clauses are regarded as independent even if they refer to the charterparty as done in *The Suzuki.*[52] Furthermore, the fact that there is

[47] Judge Briggs in *LB Re Financing No 3 Ltd v Excalibur Funding No 1 plc* [2011] EWHC 2111 [46].
[48] Debattista C, Laytime and demurrage clauses in contracts of sale – links and connections 2003 LMCLQ 508 [508].
[49] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822.
[50] [2004] EWCA Civ 822 [61].
[51] [2004] EWCA Civ 822 [43].
[52] *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.).

only one reported case[53] where the laytime and demurrage clause was held to act as an indemnity, strongly suggests that these clauses are to be regarded as free and independent from the outset, since there has been a shift from the authorities.

However, this is only the conclusion of the case and the reasoning given by Lord Justice Mance shows that the process is not as straightforward as one might think. It would also seem that an argument based on scarce case law cannot evidence their nature in general as the clauses are drafted differently and the context varies in almost every case. There are several points, which must be made, as to the very nature of the laytime and demurrage clause in a sale contract.

Firstly, it has been held that there is no presumption as to whether laytime and demurrage provisions are to be regarded as independent obligations in contracts of sale, but this is a question of construction itself[54] which must be done against the factual matrix in each case.[55] The better view seems therefore to be that the only meaning of "default position" is that the laytime and demurrage clause in the sale contract is, *de facto*, different from their counterparts in charterparties, being under a different contractual regime. One should therefore not approach the question of the nature of the laytime and demurrage clause by starting with any default position giving any presumption as to their nature. Their position and legal nature must be the product of their construction based on the principles set out in the authorities.

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[53] *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.).
[54] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [42] where Lord Justice Mance refers to this as a "general principle" and the case of *Houlder Bros. v The Commissioners of Public Works* [1908] A.C. 276.
[55] *Glencore Energy (UK) Ltd v Sonol Israel Ltd* [2011] EWHC 2756 (Comm) [13] and also pointed out in *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 WLR 896 as "the matrix of fact".

It is therefore submitted that the starting point should be "neutral and free of pre-conceptions or presumptions"[56] and that the default position should take its basis in the principles of interpretation as set out in the *Rainy Sky*.[57] This enables a skilled draftsman to provide a laytime and demurrage clause to act as a way of indemnity by the wording used, thereby showing the parties intentions.[58] This can be clearly stated in the clause itself.

Secondly, laytime and demurrage clauses nature and effect "depends upon the context and wording of the particular provisions, including the scope of any reference to or incorporation of the demurrage provisions of a charter-party".[59] In *The Devon*[60] the reference "as per charterparty" did nothing more than to incorporate a rate, somewhat different from the earlier mentioned decision in *The Suzuki.*[61] It would therefore seem that the wording does not itself provide the entire picture when it comes to the construction, and the context surrounding the charterparty and sale contract therefore becomes crucial.

Summarised, the better view seems to be that the starting point is that laytime and demurrage clauses in contracts of sale are regarded as different clauses on the basis that they are under different contractual regimes. Their nature and effect must

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[56] *Glencore Energy (UK) Ltd v Sonol Israel Ltd (The Team Anmaj)* [2011] EWHC 2756 (Comm) [18].
[57] *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50.
[58] Debattista C, Laytime and demurrage clauses in contracts of sale – links and connections 2003 LMCLQ 508 at 510.
[59] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [42, iv].
[60] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822.
[61] *Suzuki & Co. v Companhia Mercantile Internacional* (1921) 9 LI.L.Rep 171 (C.A.).

however be determined individually in each case based on the principles set out above. It is therefore submitted that there is no default position, albeit that laytime and demurrage provisions in a contract of sale are separate provisions from their counterparts in charterparties, being under a different contractual regime.

2.4 Freedom and privity of contract principles

The privity of contract principle is not only found when it comes to laytime and demurrage clauses, but it is a principle found in the general law of contract.[62] The rights and obligations found within the four corners of the agreement are only between the parties to that specific contract and no one else. The implication being that an agreement between two parties can never regulate the right and obligations of a third party.

One of the exceptions to this privity is the Contracts (Rights of Third Parties) Act 1999, but often this is exempted from applying to sale contracts.[63] It would however seem difficult that a CIF buyer can rely on S. 6 (5) in the Contracts (Rights of Third Parties) Act 1999 as to "avail himself of an exclusion or limitation of liability" in the carriage contract if the obligation to pay demurrage is regarded as free and independent under the sale contract.

The next relevant principle is the freedom of contract principle. The principle stems from general law of contract and it can be seen as one of the reasons why English Law is favourable as governing law in commercial sales. The rights and obligations of

[62] *Dunlop Pneumatic Tyre Co. Ltd v Selfridge & Co. Ltd* [1915] AC 847.
[63] See here e.g. GAFTA 119, line 268-269.

the parties are found within the four corners of the contract and nowhere else. In *The Rainy Sky* it was pointed out "Where the parties have used unambiguous language, the court must apply it".[64] In other words, the parties are free to agree to any terms as they may please, however as previously mentioned,[65] if there are two possible constructions available the "the court is entitled to prefer the construction which is consistent with business common sense and to reject the other".[66] The freedom of contract principle can here be in conflict with construing the clause according to business common sense.

In *The Devon*[67] Lord Justice Mance found it useful to refer to authority for the notion that "there is no rule of law… preventing the parties making any bargains they may please".[68] This is one of the bases on which the judge concludes that the clauses are independent since the parties "may construct an independent scheme regarding demurrage".[69] The freedom of contract principle seem here to be favoured in contrast to the commercial sense argument which underlines the possibility of the seller to make a windfall profit if demurrage does not incur under the charterparty.[70] It must be pointed out, that even if the freedom of contract principle exists, the principle itself

[64] Lord Clarke of Stone-cum-Ebony JSC in *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50 [23].
[65] See discussion above p. 16.
[66] Lord Clarke of Stone-cum-Ebony JSC in *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50 [21] and *Antaios Compania Naviera S.A. v Salen Rederierna A.B. ("The Antaios No. 2")* [1984] 2 Lloyd's Rep. 235 [238].
[67] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [27].
[68] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [28], referring to *Houlder Bros. v The Commissioners of Public Works* [1908] A.C. 276.
[69] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [33].
[70] Dissent of Lord Justice Buxton in *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [61].

cannot infer or to go against the notion that "the ultimate aim is to determine what the parties meant by the language used by ascertaining what a reasonable person would have understood the parties to have meant".[71] A construction of the laytime and demurrage clause based on the freedom of contract principle would therefore take a more literal interpretation than finding the intention of the parties through the factual matrix supported by business common sense.

The better view seems to be that even if the parties enjoy freedom of contract, the proper construction of the agreement shall be based on a more holistic view, considering the language used as a reasonable person who has all the background knowledge would ascertain it and not use the principle as an argument for clauses if they do not make any commercial sense.

Furthermore, if there is a cesser clause in the charterparty, one could argue that the liability for demurrage under the sale contract "flies in the face of commercial reality" so that it is unreasonable, the parties must make such an intention clear.[72]

Another point must be made, which is that even though the parties enjoy freedom of contract, once one of the parties is obliged to pay liquidated damages even though there is no demurrage payable under the charterparty, it seem construed and without basis in reality to call such clauses for a demurrage clause when they in fact belong to the charterparty regime.

[71] *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50 [14].
[72] See discussion above p. 13.

3. Can the law of penalties prevent laytime and demurrage clauses to be independent?

The law of penalties prohibits the use of pre-estimated anticipated loss, which is stipulated as *in terrorem*[73] to the offending party and extravagant in comparison to the greatest loss that could follow from the breach.[74] In other words, if the contract consists of a provision giving the other party a benefit, which is in great excess of the pre-estimated loss, the courts will strike out a clause that is based on deterring the other party from breaching the contract.

In order to determine if the law of penalties has any effect on laytime and demurrage clauses in sale contracts, it is necessary to examine the very nature of these clauses and their purpose. The general purpose of a demurrage clause can be seen in two ways. It is both a pre-estimate of the loss that will occur if the vessel uses more time than prescribed and it gives the charterer a strong incentive not to exceed the stipulated laytime. This last observation fits strongly with the characterisation of being *in terrorem* as it is one of the main functions of a penalty clause. Whether the clause will be determined to be one or the other depends on the difference between the amount payable for the breach and the loss that might be sustained.[75]

It would therefore seem that the law of penalties does little in terms of demurrage provisions in excess when it comes to charterparties since exceeding the laytime may result in loss of the next fixture, and therefore be of a considerable amount.

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[73] *Dunlop Pneumatic Tyre Co. Ltd v. New Garage & Motor Co. Ltd* [1915] AC 79 [86].
[74] Ibid. [87].
[75] *Lordsvale Finance plc v Bank of Zamibia* [1996] Q.B. 752 [762].

One of the arguments put forward by Lord Justice Mance in *The Devon*[76] for the clauses to be regarded as independent is that the general law of penalties "offers potential protection" for provisions without "a reasonable basis as a genuine pre-estimate of the recovering party's exposure".[77] It has been said that the CIF buyer continues to enjoy the protection the law affords against penalty clauses.[78]

The argument itself seems to be based on the acceptance that the demurrage clause in the contract of sale is in fact used as a way of recovering costs under the charterparty. This leads somewhat reluctantly to the implication that it is an indemnifying provision, even though the judge concluded that it was indeed free and independent.

The dissenting Lord Justice Buxton point out that it would seem a "sparse comfort" that the law of penalties would strike down such a clause as it being characterized as oppressive.[79] Taking into account the nature of a demurrage clause, the question is if the law of penalty is able to strike down a demurrage clause at all.

The market fluctuations relating to the pre-estimate of loss occurred and the calculation of demurrage is not relevant after the contract is concluded, as the clause is judged as of the making of the contract and not as the time of the breach.[80] This

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[76] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd [*2004] EWCA Civ 822.
[77] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [35].
[78] Todd P, *Laytime and demurrage provisions in sale contracts* 2013 LMCLQ 150 [154].
[79] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [63].
[80] *Dunlop Pneumatic Tyre Co. Ltd v. New Garage & Motor Co. Ltd* [1915] AC 79 [87].

provides difficulty in our case as the sale contract may be concluded long before the terms of the charterparty. If the relevant time of assessing the clause is when the sale contract was entered into it might prove difficult to assess if the estimate of liquidated damages in the sale contract "is a genuine covenanted pre-estimate of damage" when one does not know the actual demurrage payable under the charterparty.

Consequently, the demurrage rate agreed at the time of entering the sale contract might seem to be a genuine pre-estimate at that time, but if there is a falling market, the difference between the loss and the rate might be significant. In other words, the law of penalties will not be able to assist a CIF buyer or FOB seller under a falling market because the assessment is made when the contract of sale is made and not later.

Firstly, it would therefore appear that it is uncertain that the law of penalties can apply to a charterparty all the time it is fixed after the contract. Secondly, the safety net would seem inadequate as protection, when the threshold for applying the law of penalties to strike down a clause is high and narrow.[81] It is therefore submitted that the CIF buyer or FOB seller would at best enjoy an uncertain and narrow protection from the law of penalties when it comes to laytime and demurrage clauses.

The question arises if the law of penalties would give any protection if there was a cesser clause in the charterparty. Again, the time of assessing the clause is when the

[81] Thomas D.R, Chuah J, *The evolving law and practice of voyage charterparties; Laytime and Demurrage Clauses in Contracts of Sale – A Survey of the New York Society of Maritime Arbitrators' Awards (1978 – 2008) and English Case Law* (Informa Law, 2009) at page 174.

contract of sale was entered into. If the charterparty terms were not yet fixed, the parties would not have any knowledge about the charterparty at all and the cesser clause seems to fall outside the scope of the law of penalties since it is not a part of the factual matrix at the time of entering the contract. Consequently, the law of penalties gives the CIF buyer or FOB seller little to none comfort.

It would therefore seem that if one is to regard a clause as independent of the charterparty it would seem difficult to hold the liquidated damages to be oppressive when one has nothing to compare with and the parties enjoy the freedom of contract. The better view seems therefore to be that the law of penalties argument in favour of the laytime and demurrage clause to be free and independent is of little value.

3.1 The mirroring problem

The purpose of this chapter is to highlight the difficulties that arise when one has a free-standing laytime and demurrage clause in the sale contract making cross-reference to or incorporation from the charterparty. What implications do such references or incorporations have on their construction?

In general a back-to-back drafting of an laytime and demurrage clause in the sale contract should encourage a construction, which is highly influenced by the charterparty terms since they are alike. The problems with generalization is that the laytime and demurrage clauses might be drafted slightly differently, both in the contract of sale and in the charterparty. It therefore makes more sense to set out general principles of interpretation of these clauses than to give any definite answer to their nature.

In *The Team Anmaj*[82] the demurrage clause in the contract of sale set out that demurrage was payable "As per charterparty rate, terms and conditions" only incorporated a rate and did not provide an indemnifying provision when the sale contract contained also laytime provisions. Consequently, the demurrage claim from the seller was struck out as time-barred following S. 5 of the Limitation Act 1980 because the cause of action accrued when discharge was completed and not when the invoice was given later on. The case thereby followed the ratio given in *The Devon*[83] and *Gill & Duffus*[84], that when a laytime provision also is included, the laytime and demurrage clause is not indemnifying.

Mr Justice Beatson held that it clearly followed from authority that "where a sale contract incorporates the terms of a charterparty relating to demurrage in an otherwise independent sale contract containing, for example, provisions about laytime the obligation is generally to be construed as an independent demurrage obligation and not as an indemnity".[85] It therefore seems that the judge makes a general remark about these clauses when there is a laytime provision coupled with the demurrage clause in the sale contract. It seems therefore to be correct to call a laytime and demurrage clause free and independent when one also has a laytime provision in the sale contract.

[82] *Glencore Energy (UK) Ltd v Sonol Israel Ltd* [2011] EWHC 2756 (Comm).
[83] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822.
[84] *Gill & Duffus S.A. v Rionda Futures Ltd.* [1994] 2 Lloyd's Law Rep. 67.
[85] *Glencore Energy (UK) Ltd v Sonol Israel Ltd* [2011] EWHC 2756 (Comm) [21].

However, it might be the parties' intention to only provide the same laytime here as in the charterparty. How such a back-to-back arrangement can be seen as a sign of it being free and independent and not merely an indemnifying incorporation is more difficult to understand. The ratio can be followed from a viewpoint that if the demurrage clause also provides a laytime, it is more free and independent than if it merely provided for demurrage.

A further point made by Mr Justice Beatson was that the commercial background or "factual matrix" has implications on the construction of the laytime and demurrage clauses as they must be interpreted against their commercial background.[86] Thereby bearing in mind their function and purpose under the sale contract. This is also evident from the fact that it has been held that without any reference to the charterparty terms, the commencement of laytime under a sale contract is to count from the moment the goods are at the disposal of the buyer and thereby not reliant on the law of charterparties.[87] The laytime is therefore seen as independent of the charterparty when no reference is made.[88]

As the above authorities show, there are difficulties in construing laytime and demurrage clause even though they have a separate laytime provision when they refer to the charterparty and therefore should be regarded as free and independent. The CIF seller therefore has he following choices;

[86] *Glencore Energy (UK) Ltd v Sonol Israel Ltd* [2011] EWHC 2756 (Comm) [13.].
[87] *Etablissements Soules et Cie v Intertradex S.A.* [1991] 1 Lloyd's Rep. 378 (C.A.).
[88] The position is different if there is an explicit reference to the charterparty terms, e.g. about notice of readiness as shown by *Gill & Duffus S.A. v Rionda Futures Ltd.* [1994] 2 Lloyd's Rep. 67 where the law on charterparties applied.

i) incorporate or make reference to the charterparty rate of demurrage in the contract of sale, or ii) mirror the laytime and demurrage clause from the charterparty into the sale contract, if known (back-to-back) or iii) provide a cesser clause in the charterparty and a laytime and demurrage clause in the sale contract making the CIF buyer liable for demurrage, thereby making a potential profit.

There are however a further possibility for the parties to make their intentions as clear as possible as to making the clause independently, a method which is shown in *The Profindo*.[89]

4. A profound problem: The Profindo case

A recent case demonstrating the difficulties and a possible solution with the drafting and understanding of these clauses is seen in *The Profindo*.[90] The case concerned a sale contract concluded on CFR (Cost, freight) shipment terms. The port authorities obstructed the usage of laytime at the discharge port without any fault by the seller or the buyer.

The main question before the High Court of Singapore was who was to bear the costs of such obstructions when the relevant laytime and demurrage clause in the sale contract did not regulate if the laytime was to be suspended or not. The case is of importance because the reasoning given can lead to CIF and CFR buyers always being liable for demurrage, the risk of delay being upon them.[91]

[89] *Profindo Pte Ltd v Abani Trading Pte Ltd* [2013] SGHC 10.
[90] *Profindo Pte Ltd v Abani Trading Pte Ltd* [2013] SGHC 10.
[91] Todd P, *Laytime and demurrage provisions in sale contracts,* 2013 LMCLQ 150 at p. 153

In concluding that the buyer was to bear the risk and costs of such an interruption after laytime had commenced, the reasoning given by Judge Prakash was that if the physical duties for a CIF or CFR seller were not even "under any duty to ensure the actual physical delivery of the goods (…) it would be quite remarkable to hold that the *risk of delay in unloading the goods* at the port of discharge after laytime has commenced has to be borne by him".[92]

It appears that the reasoning is based on the general definition given for the duties of a CIF seller.[93] However, the better view seems to be that the lack of a physical duty on one party cannot imply a duty on the other without having any contractual or legal foundation. A much stronger argument would be that the CIF buyer had undertaken to carry out the discharge operation[94] and that any risk of delay in unloading the goods at port of discharge has to be borne by him and that the burden of persuasion as to show any agreed suspension is on him.

It also follows from the author that Judge Prakash is citing, that the contract "*may impose* on him [CIF buyer] a duty to discharge the cargo at a specified rate; and failure to perform this duty will make him liable to the seller for any demurrage which the latter has to pay in consequence for the delay",[95] but this obligation must follow from contract.

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[92] *Profindo Pte Ltd v Abani Trading Pte Ltd* [2013] SGHC 10 [25].
[93] Bridge M, et al, *Benjamin's Sale of Goods* (8th edn, Sweet & Maxwell, 2010) para 19-010.
[94] *Profindo Pte Ltd v Abani Trading Pte Ltd* [2013] SGHC 10 [4].
[95] Bridge M, et al, *Benjamin's Sale of Goods* (8th edn, Sweet & Maxwell, 2010) para 19-090 and *Acada Chemicals Ltd v Empresa Nacional Pesquera SA* [1994] 1 Lloyd's Rep. 428.

The case has been said to be a "landmark case" which will be highly persuasive for the UK courts[96] on the issue of obstructions after laytime has commenced when this is not regulated in the contract.

However, not all authors are of the opinion that the rationale of the case is to be followed as it has been criticised that Judge Prakash "is confusing entirely different types of risk (..) and it is not permissible to reason from CIF and CFR contracts generally".[97] The better view seems therefore to be that in case obstruction of laytime is not regulated by the sale contract itself by any exception clause, it should not be inferred that it always is the buyer who should bear the costs of any obstructions, but that the contractual terms must imply such a duty. The parties can therefore, similar to charterparties, provide an exception clause as to laytime.

The basis taken in the physical duties of the seller, or rather the lack of such, in order to justify that the obligations of the buyer to bear the costs, seems to stretch the duties of a CIF buyer too far. The better view seems to be that such obligations must be expressed in the contract and that the parties should not rely upon any implied obligations through the courts' interpretation, as this involves uncertainty. Another point is that the parties may have agreed different arrangements concerning the discharge process and that the obligation to discharge cannot be considered to be a general obligation for the CIF buyer.[98]

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[96] Awofeso A, *New laytime and demurrage considerations under sale contracts* Shipping & Trade Law, 28 January 2013.
[97] Todd P, *Laytime and demurrage provisions in sale contracts* 2013 LMCLQ 150 at p. 153, however the author suggests that the court was correct in its interpretation "but not in its reasoning from risk transfer in CIF contracts".
[98] *Congimex Companhia Geral de Commercio Importadora e Exportadora S.A.R.L. v. Tradax Export S.A.* [1981] 2 Lloyd's Rep. 687.

Furthermore, the case supports and follows the rationale of *The Devon*[99] by suggesting that the seller could have succeeded with a higher demurrage claim following the actual costs from the contract of sale rather than the amount actual payable to the shipowner.[100]

In *The Profindo,* the judge concludes that "as a matter of law, it could have been argued" that the laytime and demurrage clause is free-standing and uses *The Devon* as authority.[101] It must however be pointed out that the case makes the general notion that the question is one of construction[102] and that there are several principles one must apply in order to determine that the "provision constitute an independent code".[103]

4.1 The Profindo method

The method used in *The Profindo* for construing an independent laytime and demurrage clause in the contract of sale without incorporation from a charterparty has the advantage that the buyer knows where he stands.[104]

However, one of the disadvantages is that the terms of the contract of sale might be concluded long before any charterparty is fixed. In a fluctuating market, the

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[99] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822.
[100] *Profindo Pte Ltd v Abani Trading Pte Ltd* [2013] SGHC 10 [31].
[101] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822 [31].
[102] [2004] EWCA Civ 822 [42].
[103] [2004] EWCA Civ 822 [43].
[104] Todd P, *Laytime and demurrage provisions in sale contracts* 2013 LMCLQ 150 [152].

consequence is that the CIF seller cannot be certain of the exact demurrage rate the shipowner under the charterparty will demand. The rate agreed can therefore be an overestimate, which gives the CIF seller a benefit or it might be an underestimate, which leaves the rest of the cost to be borne by the CIF seller since it is free standing.

From the viewpoint of commercial common sense it would therefore seem to be more fair for both parties to follow the market fluctuations as they are at the time when the charterparty is entered into, and follow this rate rather than an hypothetical estimate of what the rate will be. The downside of this approach is that one faces the same problems as before and is back to square one when it comes to the construction and incorporation issues.

The better view would therefore for the parties to develop and draft clauses similar to the one used in the *Profindo* case in order to make sure that the clause operate independently. One would then also be in need of providing a separate laytime provision in the sale contract, combined with an exception clause as to obstructions after laytime has commenced. Following the rationale given in *The Handy Mariner*[105] the law on charterparties should not apply if no reference is made to the charterparty. Consequently, the laytime and demurrage provision in the sale contract will be long and complex. However, the better view seems to be that the complexity is necessary to ensure that the clause is free and independent and to avoid the problems with their construction as shown in the above.

[105] *Etablissements Soules et Cie v Intertradex S.A.* [1991] 1 Lloyd's Rep. 378 (C.A.).

5. Laytime and demurrage in standard form sale contracts: FOSFA and GAFTA

The commercial point of using a standard form contract is that it is efficient, provides certainty and often gives rules for how disputes are to be resolved under arbitration, often under its own trade tribunals. Several of these sale contracts have however no demurrage provisions at all, leaving the drafting of such clauses to the parties themselves. If the parties do not agree any laytime and demurrage provision, the situation would be as discussed below.[106] Furthermore, the ones that does mention demurrage or discharge costs are often "surprisingly laconic about laytime and demurrage".[107]

Under FOSFA 54, the demurrage provision provides that the oil shall be discharged and the CIF buyer "shall take delivery with customary quick despatch after notice of readiness has been given by the shipowner".[108] If the buyer does not comply with this, they are "to be liable to pay demurrage at the rate stipulated in the Charter Party or Contract of Affreightment". There are several issues that arise.

Firstly, the parties have provided for a customary and not fixed provision regulating the discharge process. What implications does it have that a reasonable period is allowed for discharge under the sale contract if the charterparty provides a fixed laytime provision?

[106] See Chapter 6.
[107] Debattista C, *Laytime and demurrage clauses in contracts of sale – links and connections* 2003 LMCLQ 508 [509].
[108] Federation of Oils, Seeds and Fats Association Limited (FOSFA) 54, line 153.

In an *obiter dictum* in *The Happy Day,*[109] the view was expressed that under a FOSFA 54 form "the liability of the buyer for demurrage is of course to the seller who may or may not be the charterer, and will usually be dependent upon whether or not the seller is himself liable".[110] Thereby it seems that the demurrage payable by the CIF buyer will actually depend if it is payable under the charterparty, making it resemble an indemnifying provision. It is however suggested that this *obiter dictum* should be read with some caution and that the general provision of FOSFA 54 provides only that the rate of demurrage should be the same as in the charterparty, therefore making it an independent and free-standing obligation.

The most difficult assessment is however the wording "customary quick despatch" which regulates the discharging process. It has been suggested by some that the reason for this short approach is because the parties may agree more specific laytime and demurrage provisions in an exchange of letters or faxes.[111] Even if the parties agree on specific terms outside the standard form, it can be questioned how effective this really is if the parties have to regulate the provision on every occasion of sale and the law on this issue is highly complex.

The situation is somewhat different under FOSFA 53 which is concluded on FOB shipment terms. If the FOB seller fails to comply with the loading rate stipulated in the preamble or the average rate and "demurrage is thereby incurred he shall be liable to pay demurrage" at the rate in the preamble or "US $18,000 per day/pro rata, or as

[109] Lord Justice Potter in *Glencore Grain Ltd. V Flacker Shipping Ltd. ("The Happy Day")* [2002] EWCHA Civ 1068 [505].
[110] Ibid. [59].
[111] Debattista C, *Laytime and demurrage clauses in contracts of sale – links and connections* 2003 LMCLQ 508 [510].

per Charter Party whichever is the lower".[112] The wording "thereby incurred" suggests that there actually has to be demurrage incurred under the charterparty, again the resemblance towards an indemnifying provision is present. This view will be strengthened if no demurrage is set out in the sale contract and the rate which is lower is found under the charterparty, thereby making the sale contract more dependent on the charterparty terms. There is however a qualification to the responsibility for the FOB seller if there is a delay over 72 hours and the delay is caused by "any other reason for which the Sellers are not contractually responsible, any extra costs for Sellers shall be for Buyers' account".[113] This exception must be seen as very widely drafted, meaning that the FOB seller is not responsible for costs due to obstructions resulting in delay, which are outside the control sphere of the FOB seller.

In GAFTA 122[114] and GAFTA 100 concluded on CIF shipment terms, the discharge provision[115] provides that the discharge shall be "as fast as the vessel can deliver" and that "the costs of discharge from hold to ship's rail shall be for Sellers' account, from ship's rail overboard for Buyers' account. If documents are tendered which do not provide for discharging as above (…) Sellers shall be responsible to Buyers for all extra expenses incurred thereby". It here seems that there is no demurrage agreed at all for the CIF buyer, following the last sentence providing that the CIF seller shall cover costs that the CIF buyer incurs if the discharge is not done correctly. It seems therefore that there is no obligation on the CIF buyer to be responsible for demurrage.

[112] FOSFA 53, lines 42-44.
[113] FOSFA 53, lines 45-46.
[114] Grain And Feed Trade Association (GAFTA) No. 122.
[115] GAFTA 122 cl. 13 and GAFTA 100 cl. 14.

This is in contrast to GAFTA 112 which provided the other extreme when it comes to length and precision.[116] This standard form does not only provide specifics about the commencement of laytime, but also exceptions. However, the demurrage provision is quite short only referring to "Rate of demurrage as per Charter Party/Booking Note/Despatch half demurrage".[117] This must be taken as only incorporating the rate, as seen in the earlier mentioned cases, making it free and independent from the charterparty terms.

In GAFTA 64 which is concluded on FOB shipment terms, simply states that the vessel is "to load in accordance with the custom of the port of loading unless otherwise stipulated",[118] thereby not giving any further guidance on any demurrage payable.

Summarised, it seems evident that these standard forms vary in their length and complexity, some provide extensive laytime and demurrage provisions, while others provide close to none. The ones which lack to mention laytime and demurrage place a responsibility on the parties themselves to develop and incorporate a demurrage and laytime provision.

[116] Debattista C, *Laytime and demurrage clauses in contracts of sale – links and connections* 2003 LMCLQ 508 [509].
[117] GAFTA 112, lines 174-175.
[118] GAFTA 64 lines 49-50.

6. No express laytime and demurrage clause in the sale contract: can implied obligations help the cost bearer?

It has been pointed out that that it is difficult to see how a CIF seller can recover against the buyer for delay, due to the basis that the buyer owed him a duty to discharge with reasonable despatch or at a rate as specified in the charterparty.[119] This follows from the notion that under a CIF contract there is no implied duty on the buyer to discharge the goods at all.[120] It would therefore seem that the CIF seller cannot rely on any implied terms and is therefore forced to provide a separate laytime and demurrage clause in the sale contract, unless it is specified in the contract that the buyer must discharge at a given rate.

The situation must be explained somewhat differently when it comes to the duties of a FOB seller as one of the duties is to deliver the goods free on board.[121] The obligation has however not been suggested to extend so that the FOB seller must deliver within any specified laytime as to avoid the buyer's potential liability for demurrage.[122] In general, it would seem that a CIF seller or FOB buyer cannot rely on implied obligations for the other party in order to get any demurrage reimbursed without having an explicit provision in the sale contract to that effect.

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[119] Debattista C, *Laytime and demurrage clauses in contracts of sale – links and connections* 2003 LMCLQ 508 [511].
[120] *Congimex v Tradax* [1983] 1 Lloyd's Rep 250 (C.A) and Lorenzon F, Baatz Y, *C.I.F. and F.O.B. Contracts* (5th edn, Sweet & Maxwell, 2012) [8-043].
[121] *Wimble v Rosenberg* [1913] 3 K.B. 743 and Debattista C, *Laytime and demurrage clauses in contracts of sale – links and connections* 2003 LMCLQ 508 [512].
[122] Ibid. [513].

This question must be seen differently when the parties have incorporated the Incoterms 2010 Rules since they provide more specifically the parties' obligations.

6.1 CIF Incoterms® 2010 Rules

There are several issues which arise if the parties have agreed to incorporate the Incoterms® Rules into the sale contract, here we are concerned on the implications in relation to making demurrage payable under the sale contract.

If the contract is concluded on CIF Incoterms® 2010 shipment terms, the terms themselves do not specify which kind of contract of affreightment the seller must procure or on which terms specifically. It is however provided that "The contract of carriage must be made on usual terms at the seller's expense (…)".[123] It is therefore suggested that these terms are not implied anymore, but are in effect a part of the contract between the parties, setting out their rights and obligations.

There are two issues that arise. The first one is if the requirement of the contract of carriage to be "usual" has any restrictions on which kind of terms the charterparty is concluded upon. If the charterparty contains a cesser clause or a very high demurrage rate, would the charterparty then be concluded on "usual" terms? Or is the term only relevant towards elements in the charterparty, which directly affect the CIF buyer?

If the charterparty contains a demurrage rate, which must be considered high compared to the market rate, it would seem that the only party suffering from such is the CIF seller himself under the charterparty. The situation is different if the sale contract incorporates the demurrage rate into the sale contract making it payable to

[123] Incoterms® 2010 CIF A3 a).

the CIF buyer as the charterparty then becomes a relevant component to the sale contract and the requirement of the charterparty to be usual also becomes relevant.

The reference to usual terms in the Rules can be seen in a much wider scope as S. 32 (2) of the Sale of Goods Act 1979 provides that the seller must make a contract with the carrier which is "reasonable". If he fails to do so, the seller will be at risk for the goods and responsible for any damages. The view has been put forward that Incoterms® 2010 Rules negates the effect of any reasonableness test provide by the Act because it favours what is "usual in the trade".[124] It is however submitted that these two provisions do not necessarily need to be in conflict, as what is common in the trade in most cases also would be reasonable and there is no known case law stating that these are to be understood as negating each others effect. It is submitted that the standard term in the Incoterms 2010 merely adopt and use the understanding of usual, which is found under the reasonableness test after S. 32 (2).[125]

However, it must be clear that the Sale of Goods Act 1979 S. 32(2) deals with the carriage contract itself. It does not deal with the demurrage clause under the contracts of sale. The only imaginable implication of the section would therefore be if the sale contract contains an incorporation of the charterparty terms, and these terms are outside what can be defined as usual in the trade when it comes to laytime and demurrage clauses in sale contracts. One possible alternative would be the

[124] *Geofizika DD v MMB Int Ltd* [2010] EWCA Civ 459 and Lorenzon F, Baatz Y, *C.I.F. and F.O.B. Contracts* (5th edn, Sweet & Maxwell, 2012) [2-031]. See however Lorenzon F, *When is a CIF seller's carriage contract unreasonable? – section 32(2) of the Sales of Goods Act 1979* 2007 13 JIML 241 [250 - 251] where the opposite view seems to be taken.
[125] Lorenzon F, *When is a CIF seller's carriage contract unreasonable? – section 32(2) of the Sales of Goods Act 1979* 2007 13 JIML 241 [244].

incorporation of demurrage terms making the CIF buyer liable also for exceeding the laytime in the loading operation. Another possibility is found if the provision refers to demurrage payable "as per charterparty" and the relevant charterparty contains a cesser clause, protecting the CIF seller as charterer. It would seem that in such a case the relevant provision would not pass the reasonable test under S. 32(2).
Firstly, it is the CIF seller that traditionally must procure a contract of affreightment,[126] thereby also bearing the risks and costs in relation to the charterparty. Secondly, there is no implied obligation of the CIF buyer to discharge the goods if not set out in the contract of sale itself.[127]

The second question is the meaning of the standard terms which provide that the carriage contract is for the "seller's expense". Taking into consideration that it is the carriage contract the terms have in mind it would seem that all the costs under the carriage contract is to be borne by the CIF seller. If this is true, it is able to be in conflict with any demurrage provision provided by the parties in the sale contract. This point is also supported by the view put forward in *The Devon* that even if the provision is not regarded as indemnifying, the "underlying rationale of the inclusion of any laytime and demurrage provision (…) is that the seller will have to arrange carriage on terms which may expose the seller to liability for demurrage to a shipowner or other third party".[128] Consequently, it would seem that even if the demurrage scheme is regarded as independently it is able to be in conflict with the charterparty because of this underlying rationale.

[126] *Johnson v Taylor Bros* [1920] A.C. 144.
[127] *Congimex Companhia Geral de Comercia Importadora e Exportadora Sárl v Tradax Export SA* [1983] 1 Lloyd's Rep. 250 C.A.
[128] [2004] EWCA Civ 822 [33].

Furthermore, it follows from the shipment terms that the CIF buyer must pay "all costs and charges relating to the goods while in transit until their arrival at the port of destination, unless such costs and charges were for the seller's account under the contract of carriage"[129]. It would therefore seem that the parties, according to the standard terms, have agreed that any costs arising from the charterparty are for the CIF seller to bear, such as demurrage.

One must however bear in mind that if the parties have agreed that demurrage is to be borne by the CIF buyer at the port of discharge under the sale contract, the provision must be regarded as special terms which must prevail if no hierarchy clause is provided for.[130] The parties have in other words agreed to amend the Rules ans specifically stipulated the costs of demurrage. This possibility follows from the freedom of contract principle and also by the Rules themselves by providing that "If the seller incurs costs under its contract of carriage related to unloading at the specified point at the port of destination, the seller is not entitled to recover such costs from the buyer unless otherwise agreed between the parties".[131]

It also follows from the Sale of Good Act 1979 S. 55(1) that the requirement of reasonableness found in S. 32 (2) "may be negative or varied by express agreement".[132] In addition, the CIF seller may still be under an obligation to pay demurrage under the contract of carriage. In other words, the contract of carriage is

[129] Incoterms® 2010 CIF and CFR B6 b).
[130] *Indian Oil Corporation v Vanol Inc.* [1991] 2 Lloyd's Rep. 634.
[131] Preamble to Incoterms® 2010 CIF.
[132] Lorenzon F, *When is a CIF seller's carriage contract unreasonable? – section 32(2) of the Sales of Goods Act 1979* 2007 13 JIML 241 [249] where exemplified as to 'on or below deck'.

still for the "seller's expense" using a literal interpretation even if there is an independent demurrage scheme under the sale contract.

Taking these observations into account, it is submitted that the parties are free to agree and amend any terms as they would like and a laytime and demurrage clause in the sale contract would not to be in conflict with the Incoterms® 2010 or the Sale of Goods Act 1979. This will however depend on the drafting of the clause, and as suggested, there might be cases where the terms of the carriage contract are no longer considered to be on "usual terms". There is however no possibility to imply that the CIF buyer is to bear demurrage costs under Incoterms® 2010, unless expressed in the contract itself.

7. Conclusion

As the above has shown, the drafting and construction of laytime and demurrage clauses in sale contracts is not straightforward and it seems than the only default position is that laytime and demurrage clauses in sale contracts belong to a different contractual regime than their counterparts under the charterparty. The principles of construction as set out in *The Devon*[133] are noteworthy and provide guiding principles on how these clauses are to be construed, together with the principles of construction in *The Rainy Sky*.[134]

In addition, the development in the authorities show that a laytime and demurrage clause will generally be construed as free and independent where it is accompanied by

[133] *Fal Oil Co. Ltd. v Petronas Trading Corporation Sdn Bhd* [2004] EWCA Civ 822.
[134] *Rainy Sky SA v. Kookmin Bank* [2011] UKSC 50.

a laytime provision, thereby making it able to stand on its own feet. It is therefore submitted that parties seeking to have a laytime and demurrage clause in the sale contract, which should function as an indemnifying provision, must state so expressly in the contract of sale. If the laytime and demurrage clause in the sale contract is free and independent, the parties cannot rely on any exceptions as to laytime under the charterparty, unless stated so expressly.

It is also submitted that the law of penalties provide little to no protection for the CIF buyer or FOB seller if there is a cesser clause in the charterparty, because the threshold for striking down a clause is set very high by the authorities. It would therefore be uncertain for a CIF buyer or FOB seller to rely on the mere possibility that the courts will strike down the laytime and demurrage clause in such a case.

Furthermore, the best method for ensuring that the provision will be construed as free and independent would be by using *The Profindo*[135] method, by drafting a laytime and demurrage clause in the sale contract, which operates without any reference to the charterparty and by providing its own demurrage rate. This method would also seem to provide most clarity from the other alternatives. It should however be noted that the laytime provision needs to be more developed than in the mentioned case so that the parties have clarity and know their right and obligations under the contract of sale.

The parties under a sale contract which seeks to have an independent laytime and demurrage clause must also consider the implications the charterparty has to the commencement of laytime and exceptions. The draftsmen of the sale contract is here

[135] *Profindo Pte Ltd v Abani Trading Pte Ltd* [2013] SGHC 10.

faced with a dilemma. One could make laytime and demurrage clauses in sale contract more complex by expanding the clause with commencement of laytime and incorporate any exceptions that should apply, but that would also be an argument for not regarding the clause as independent anymore by strengthening the ties to the charterparty itself. Or the alternative would preferably be to adopt an individual and specific laytime and demurrage clause that does not refer to the charterparty at all.

As shown in the above, the law on laytime and demurrage clauses in sale contracts is highly complex and the right and obligations for the parties can be uncertain, providing a difficult situation for the parties in the process of negotiation the terms of the sale contract. Depending on how the sale contract is drafted, this will be predominant for the drafting of any other sale contracts in a string sale so that the expenses for demurrage is covered further down the line.

In the view of the author, a fair assumption is that the length and complexity of laytime and demurrage clauses in sale contracts will increase in the future. Thereby developing the law for laytime and demurrage clauses in sale contracts. This view is based on the many uncertainties as shown in the above and the parties' desire to provide certainty when it comes to financial liability in a difficult and all time low freight market.

Even though the understanding of these clause is complex and much depend on their wording and context, the single most important point is to make the parties to the sale contract aware of this uncertainty so that they are able to make enlightened choices when drafting the laytime and demurrage provision before any dispute arise.

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