

Update

The English Supreme Court examines issues of Causation

Under English law, to succeed under an indemnity (such as a (re)insurance contract) a claimant must be prove (i) something has happened which triggers the indemnity (in the insurance context, a peril insured against); (ii) the claimant has incurred a loss; and (iii) there is a sufficient causative link between the trigger and the loss. In relation to causation, the English courts have long held that the breach must be an “effective” or “proximate” cause of the loss – though the parties can contract for a looser requirement. Does the decision in the *Petroleo Brasileiro S.A v E.N.E. Kos 1 Ltd*¹ charterparty dispute introduce a new test for causation generally? If there is a new test, what are the implications for (re) insurers?

The contractual background

The case concerned a 36 month charterparty which required the Charterers to pay hire fees in advance and entitled the Owners to withdraw the vessel if this did not happen. There was no anti-technicality clause to prevent the Owners from exercising this right for minor breaches by the Charterers. The charterparty also contained an indemnity from the Charterers to the Owners as follows:

“The Master (although appointed by Owners) shall be under the orders and direction of Charterers as regards employment of the vessel, agency or

other arrangements ... Charterers hereby indemnify Owners against all consequences or liabilities that may arise ... from the Master otherwise complying with Charterers’ or their agents’ orders ...”

The facts

On 30 May 2008 the vessel tendered a Notice of Readiness. The next day, at the order of the Charterers, the Master began loading their cargo and this was completed the following day. On 31 May the Charterers failed to pay hire fees in advance as required and on 3 June the Owners withdrew the charterparty for late payment. The Owners then offered a new

¹ 2 May 2012.

charterparty at the current, but much higher, May 2008 rates. When the Charterers refused the Owners required the Charterers' cargo to be removed. The Owners then sued the Charterers for 2.64 days of lost hire fees. This was the time between the issuing of the Owners' withdrawal notice and the completion of the unloading of the Charterers' cargo.

The decision at trial

When considering the scope of clause 13 the judge agreed that the vessel would not have needed to wait for the cargo to be removed had the Master not complied with the Charterers' order to load it. That being said, however, the judge held that the loss resulted from the Owners' decision to withdraw the vessel. This was a decision over which the Charterers had no control. As a result, the judge held that the Owners' loss was not directly caused by the Charterers' Order. As such, the judge held there was not sufficient proximity between compliance with the Charterers' order and the Owners' loss. The Owners thus failed on causation.

The Court of Appeal decision

The Court of Appeal noted that clause 13 was not all-embracing and was subject to principles of remoteness and proximity of causation and agreed with the trial judge that the Owners' claim failed on causation. The Court of Appeal accepted that the cargo would never have needed to be removed if the Charterers had never ordered it loaded in the first place. It was not, however, a natural consequence of the cargo being loaded that it had to be removed at the port where it was loaded. Instead, the Court of Appeal held that the true cause of the need to remove the cargo was that the Owners required the Charterers to remove the cargo following the Owners' withdrawal.

The Supreme Court decision

The Supreme Court observed that the Owners' decision to exercise an express right of termination under the charterparty, rather than perform the charterparty, was morally and legally neutral. The Supreme Court then held that there are no standards by which the Owners' reasons were to be judged other than those to be found in the charterparty. Turning to clause 13, The Supreme Court held that the purpose of the indemnity was to protect the Owners against losses arising from risks which they had not agreed to in the charterparty.

The Supreme Court noted that different adjectives have been used over the years in relation to causation. These included "proximate", "dominant" and "direct" cause. The Supreme Court observed, however, that these terms were misleading. This is because they tended to suggest that the relevant cause must be either the most proximate in time or that the relevant search was for the sole cause. The Supreme Court, instead, said that the real question

was whether the Charterers' order to load the cargo was an effective cause of the Owners having to bear a risk which they had not contractually agreed to bear. If so, the Charterers' order was an effective cause of the Owners' loss.

Lord Sumption, delivering the main judgment, took the view that, once the cargo had been loaded, it had to be discharged somewhere, and the Owners' decision to withdraw the vessel, including the timing of that decision, merely determined the place at which the cargo was removed. It did not change the fact that the effective cause of the Owners' loss was the original order by the Charterers to the Master to load the Charterers' cargo in the first place.

Lord Sumption noted that removing the cargo at the point of origin was more beneficial to the Owners than the Charterers and felt that this might have unfairly coloured the lower courts' views of the Owners. This was, however, not a relevant consideration in the circumstances. Instead, what mattered was whether the Owners' withdrawal was legitimate under the charterparty (it was) and whether the subsequent removal of the cargo had to be done in the Owners' time (it did).

In other words, removing the cargo in their own time and at their own expense was not a risk that the Owners had agreed to bear in the ordinary course of events under the charterparty. It was, however, precisely what the Owners ended up having to do after their legitimate withdrawal following the Charterers' breach of the charterparty advance payment obligation. It was for this reason that the Supreme Court held that the Owners succeeded on causation.

Lord Mance dissented on this causation issue. Agreeing with the lower courts he considered that the loss suffered by the Owners was caused because the charter was at an end, so the Owners were not performing the Charterers' instructions and were not receiving hire for the time wasted prior to discharge of the cargo. There was therefore no direct, unbroken link between Charterers' orders to load the cargo and the Owners' loss: "Subsequent events superseded charterers' orders and rendered them a matter of history". He added that the majority's decision stretched this standard form charter indemnity beyond any previous decision without justification and without need (he would have found for the Owners on a different basis that had nothing to do with the indemnity).

Commentary

On the face of it the majority's interpretation of the indemnity was very generous to the Owners, in that the loading of the cargo would not naturally be considered to be the proximate or effective cause of the loss of hire. Does this decision from the herald a more relaxed approach to the causation requirement for indemnities generally, and insurance in particular?

It is important to take account of the context of the decision. The terms of the clause and the charterparty as a whole influenced the majority's willingness to give the indemnity an extended meaning. Lord Sumption described the scope of the indemnity as "very wide" and explained why this was appropriate in the context of the parties' rights and obligations under the charterparty as a whole. The Supreme Court did not purport to lay down any broader guidance on the interpretation of indemnities.

Turning to insurance, determining which of several perils is the proximate or effective cause of the loss, and whether one of the perils has broken the chain of causation from another, is as problematic as it has ever been. So we may well see this decision cited in support of a broader, more pro-insured test.

However all the more caution is required when considering the impact of the decision in this sphere.

To test this, imagine that the Owner had arranged a similar indemnity under a freestanding insurance policy instead of obtaining it from the Charterers. Given that the indemnity would be provided by a stranger it would not form an integral part of the rights and obligations of the Owner and the Charterer.

In such an insurance context, it is perfectly possible that the circumstances would be sufficiently different from this case to justify a different conclusion, even though the indemnity was widely drawn. So it would be unwise to conclude that the Supreme Court's decision has significantly changed the law on causation in this area.

Further information

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