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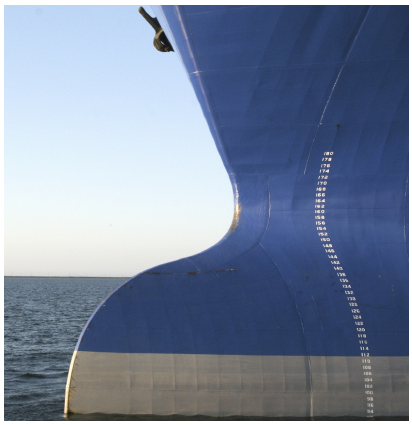

Shipping and Insurance update
Piracy

March 2010

The recent decision in ***Masefield v Amlin*** *[2010] EWHC 280 (Comm)* has given useful guidance regarding a number of issues that have been concerning shipowners, cargo owners and their insurers arising from the piracy problem off Somalia.

The decision is timely, having been handed down seven days before the House of Lords' EU Sub-Committee on Foreign Affairs heard evidence from leading marine insurance and shipping industry figures as part of its enquiry into piracy off the coast of Somalia, which is considering the issue of ransom payments.

In this update we review the decision (which largely centres on issues of actual and constructive total loss of cargo under the *Marine Insurance Act 1906*) and comment on some of the wider issues touched upon in the judgment that will be of interest to the shipping and insurance market in general, in particular the legality and public policy issues raised by ransom payments.

The facts

On 19 August 2008, the chemical / palm oil tanker *'Bunga Melati Dua'*, together with her crew and cargo, was seized by Somali pirates in the Gulf of Aden during a voyage from Malaysia to Rotterdam.

Two parcels of bio-diesel carried on the vessel were insured by the defendant Underwriter under an open cover contract that covered loss by both piracy and theft. About a month after the seizure (while negotiations for the release of ship and cargo were continuing) the claimant cargo owners tendered a Notice of Abandonment to the Defendants, which was declined. Within about 10 days of the Notice of Abandonment a ransom was agreed with the pirates and paid. The vessel, crew and cargo were subsequently released and arrived at Rotterdam on 26 October.

It was common ground that both theft of cargo and the capture or seizure of the cargo by pirates were insured risks under the cargo insurance. The Claimant sought recovery of about US$7 million under the policy for the total loss of the cargo, that sum being the net loss after allowance for the proceeds of disposal of the cargo at Rotterdam.

The issues

The primary issue for the Court, and to which the majority of the judgment was directed, was whether at the time of tender of the Notice of Abandonment it could be said that the Claimant had been irretrievably deprived of the cargo and therefore it had been actually totally lost within the meaning of *s57(1) of the 1906 Act*.

In the alternative the Claimant argued that there had been a constructive total loss under *s60(1)* of the *Act* on the basis that the cargo had been reasonably abandoned due to its actual total loss appearing to be unavoidable. Given the wording of the policy it was common ground that the additional category of constructive total loss provided for under *s60(2)(i)* of the *Act* (where an assured is deprived of possession of the goods by an insured peril and it is unlikely that they can be recovered) was excluded from the cover.

Although exclusion of *s60(2)(i)* was common ground between the parties, it is arguable that such an approach is in fact contrary to previous authority and market practice in respect of a cargo policy on ICC(A) clauses.

Finally, for the purpose of determining whether the cargo could properly be considered to be irretrievable, the Claimant argued that the payment of ransom to pirates was contrary to public policy (though not illegal) and therefore could not be taken into account in considering the prospects of recovery.

The decision

In determining the ATL claim, Steel J noted that there was unchallenged authority confirming that for the purpose of establishing irretrievable deprivation (and therefore actual total loss under *s57(1)* of the *Act*), the assured must show that recovery is impossible. Given the history of previous cases of capture by Somali pirates, there was ample evidence before the Court (and conceded by the Claimant) that in reality there was a reasonable hope and perhaps even a likelihood that the ship and cargo would be recovered by payment of a ransom. The Claimant argued, however, that it had been established in *Dean v Hornby (1854)* that in the case of capture by pirates there is an actual total loss straightaway even though the property is later recovered.

That case was referred to by Rix J in *Kuwait Airways v Kuwait Insurance [1996]* where he noted:

> *"In case of capture, because the intent is from the first to take away dominion over a ship, there is an actual total loss straightaway, even though there later be a recovery: see Dean v Hornby (1854) 3 El.& Bl 179 (a case of piratical seizure)"*

Steel J accepted that, when read in isolation, *Dean v Hornby* might be viewed as determining that a capture by pirates as such would constitute a total loss. However, following an extensive review of the authorities he concluded that this was not in fact the case. The judge held that the proposition was fact sensitive given that the intention of pirates can be various. At one extreme would be pirates who "steal" the vessel and use it for their own purposes. At the other extreme are pirates who simply retain possession of the ship in order to extract a ransom. Mere seizure by pirates without more could not be said to impact on the proprietary interests in a vessel. As Steel J put it:

> *"What has been transferred is possession and not title and the question thus arises, in my judgment, as to whether recovery of possession is legally or physically impossible."*

Applying this test to the facts of the present case the Judge held that the vessel had not been actually totally lost.

Turning to the CTL claim, the Judge noted that in order to satisfy the criteria of *s60* of the *Act*, it was necessary to show that the subject matter was abandoned because an ATL appeared unavoidable. Steel J held that these criteria had not been met for two reasons. First, the meaning of 'abandonment' in this sense did not simply refer to the tender of a Notice of Abandonment, but rather an abandonment of any hope of recovery, which clearly did not exist on the facts of this case. Secondly, for the reasons given in his analysis of the ATL claim, there was no reasonable basis on which it could be said that an ATL was unavoidable.

Having reached these conclusions it was clear that the only way in which the Claimant could now succeed was to establish that the payment of ransom was contrary to public policy. If this were the case then, it was argued, the potential for release of the vessel by this means could not be taken into account when considering whether a vessel and her cargo were in practice irretrievable.

The Judge noted that whilst it might be said that payments of ransom encourage further seizures, particularly where insurance is usually in place, in practice there is little option but to pay a ransom where that is the only effective means (absent diplomatic or military intervention) to remove vessel crews and property from harm. Steel J also noted that the payment of ransom is not illegal under English law (this point had been conceded by the Claimant) and where the 'balance of convenience' was not clear cut the Court should resist any temptation to intervene where there is no clear and urgent reason to categorise an activity as contrary to public policy.

It followed that the Claimant's claim for a total loss, whether actual or constructive, was rejected by the Court.

Comment

The case provides welcome clarification on some of the legal issues raised by the many recent incidents of piracy off Somalia. Although primarily focussed on insurance coverage issues, and in particular the rejection of the Claimant's primary argument that where a vessel is captured by pirates there is an actual total loss straightaway irrespective of later recovery (the *Dean v Hornby* point), the judgment provides helpful guidance on other related issues of interest to the wider shipping community.

The rejection of the Claimant's assertion that ransom payments are contrary to public policy is particularly interesting because it led the Judge to reflect upon both the legality of such payments and whether they can be recoverable as a sue and labour expense. The point also has relevance for ship and cargo owners in relation to general average.

In the event, the Claimant chose not to contend that the payment of ransom was illegal under English law. Noting this concession, the judge remarked that *"the payment of ransom is not illegal as a matter of English law"* and also noted that in other circumstances Parliament had intervened to make ransom payments illegal, but had not done so in this context. Therefore, the fact that payment of a ransom is not illegal was relied on by the Judge as one of the reasons for rejecting the argument that such payments are contrary to public policy.

In relation to sue and labour, the Judge referred to and relied upon the majority opinion expressed by the Court of Appeal in *Royal Boskalis v Mountain [1999]* that *"the assumption of the editors of Arnould that payment of a ransom, if not itself illegal, is recoverable as an expense of suing and labouring is well founded."*

Whilst the Judge's finding reflects market understanding of the legality position in relation to Somali pirates, it should be noted that legality was not fully argued because of the concession by the Claimant in this case.

Further information

Further information on any issue raised in this update can be obtained via your usual Clyde & Co contact or any of the following:

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