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Offshore Energy Law

On the spot: boil-off and delivery obligations

A peculiar feature of the carriage of LNG is that part of the cargo is bound to boil off. It follows (and indeed is so understood by those involved in the trade) that the quantity of cargo on discharge will be lower than that recorded on the bill of lading as shipped. A difference between shipment and discharge figures raises an inference of breach of the contract of carriage, and could lead to a shortage claim by the cargo interest.

Typically, this has not really been a problem within the LNG industry, as LNG sales have been principally on a long term take or pay basis with delivery "ex-ship" or "at terminal". Charterers are generally bill of lading holders and the buyers under the sale contract. Shipowners have therefore generally avoided shortage claims as issues of boil-off are dealt with in the charterparty (including the right of the shipowner to use the LNG cargo as fuel for the ship) and the sale contract (by annual reconciliations of cargo shipped and discharged).

However, as the nature of LNG trading evolves into a true spot market, with traders buying and selling cargoes while they are at sea, the fact that the quantity of cargo delivered will be different from what is stated in the bill of lading could present a real problem. A third party holder of the bill of lading may be able to claim either fraud against the seller or, more likely, short delivery against the carrier.

The Hague Rules (and the Visby Protocol) were agreed in order to bring much needed uniformity in relation to rights and responsibilities under bills of lading. These include questions as to the carrier's obligations as to seaworthiness and care for the cargo. It is fair to say that the carriage of LNG was not in contemplation in 1924.

Application of Hague or Hague-Visby Rules (HVR)[1]

The HVR may apply by force of law to a bill of lading (eg where carriage originates from a HVR state) or by contract. Both ShellLNGTime 1 and LNGVOY, require that bills of lading include the HVR.[2]

Although the HVR are drafted to apply to bills of lading, both ShellLNGTime 1 and LNGVOY incorporate the HVR[3]. Under ShellLNGTime 1 there is a specific carve out however, in relation to boil-off.

Short-delivery Claims?

Two common heads of short-delivery claims are unseaworthiness under Art 3(1) and breach of the carriage obligation under Art 3(2) of the Hague-Visby Rules.

For unseaworthiness, while the occurrence of boil-off is not, on its own, evidence of unseaworthiness of the vessel, if, by reason of unseaworthiness, the vessel is delayed on a voyage, which then causes the boil-off to be greater than it would otherwise have been, the carrier may be liable.

Cargo interests may also argue that the carrier is in breach of his obligation to properly and carefully load, carry and care for the cargo. The obligation to carry "properly" means "in accordance with a sound system",[4] whereas that to carry "carefully" generally

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[1] *Although there are differences between the Hague and Hague-Visby Rules the relevant provisions referred to in this article are similar and therefore they will be referred to together.*
[2] *Cl 39 of ShellLNGTime 1 and cl 28 of LNGVOY*
[3] *Cl 29(c) provides that the Hague-Visby Rules or Hague Rules or Hamburg Rules which ought pursuant to the clause paramount to have been incorporated in the relevant bill of lading shall apply to any claim "arising out of any loss of or damage to or in connection with cargo"; cl 28 of LNGVOY*
[4] *Albacora Srl v Westcott & Laurance Line Ltd* [1966] 2 Lloyd's Rep 53

relates to the operation of the system.[5] In most cases an inference of breach may be drawn from the mere fact that there is a difference between the shipment and the discharge figures. However, in the context of LNG carriage, this could be more problematic. The carrier would be able to argue that a breach can only be inferred if the claimant could demonstrate that the amount of boil-off is greater than it would otherwise have been. This may be difficult for a carrier facing a third party holder of a bill of lading who has no sight of the charterparty and the agreement as to the boil off rate.

Defences of Inherent Vice and Inevitablity

If the claimant successfully draws an inference of breach of Art 3(2), the carrier may try to rely on the inherent vice exception to liability under the HVR (Art 4(2)(m)); because the cargo is prone to boil off, it has an "inherent vice" for which the carrier should not be held responsible. There is likely to be little difficulty for the carrier to establish that the cargo of LNG evaporated naturally in the circumstances due to its inherent quality,[6] especially when the carrier would only have to establish a *prima facie* case.

The carrier may also plead that the boil-off was inevitable for carriage of LNG. This appears to be a rebuttal of the cargo interest's inference of breach.

Safe System of Carriage

Once the carrier has shown a prima facie defence of inherent vice, the burden then shifts to the cargo claimant to negative the defence by establishing negligence or failure to properly and carefully carry the goods on the part of the carrier. One important issue would be whether there was a sound system in place for the carriage. Here questions as to the integrity of the containment system, and whether a system that permits the cargo to evaporate and permits the carrier to use the cargo for their own purpose (propulsion of the vessel) is one that is "safe" i.e. preserves the integrity of the cargo.

In the recent case of *Volcafe v CSAV*[7] , there was extensive discussion as to what constituted a sound system in relation to the carriage of coffee beans which had suffered damage due to an inherent vice. The first instance judge ruled that there should be empirical scientific evidence to establish what the best system of carrying the cargo would be.

However, on appeal this was reigned in. The court decided that the standard of establishing a sound system should be based on the general practice in the industry. However, if in future there are improved methods of carrying LNG cargo which reduce boil-off, there may be arguments that these improved systems are the only sound systems.

Conclusion

It is clear from the above that defending a claim purely based on the HVR would give rise to much uncertainty in establishing liability and quantum of damages. This is why in practice, most contracts of carriage for LNG cargo put into place a contractual scheme of compensation, under which remedies for boil-off are often absolute and not dependent on proof of loss. Such a scheme offers certainty and simplicity, which is something to consider when drafting or reviewing a carriage contract for LNG cargo.

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[5] *Volcafe v Compania Sud Americana de Vapores SA* [2017] 1 Lloyd's Rep 32
[6] *Soya GmbH Mainz Kommanditgesellschaft v White [1983] 1 Lloyd's Rep 122*
[7] *Volcafe v Compania Sud Americana de Vapores SA* [2017] 1 Lloyd's Rep 32

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