NORDISK MEDLEMSBLAD

Membership Circular - OFFSHORE EDITION

No. 575 – December 2012

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Nordisk Skibsrederforening
(NORDISK DEFENCE CLUB)

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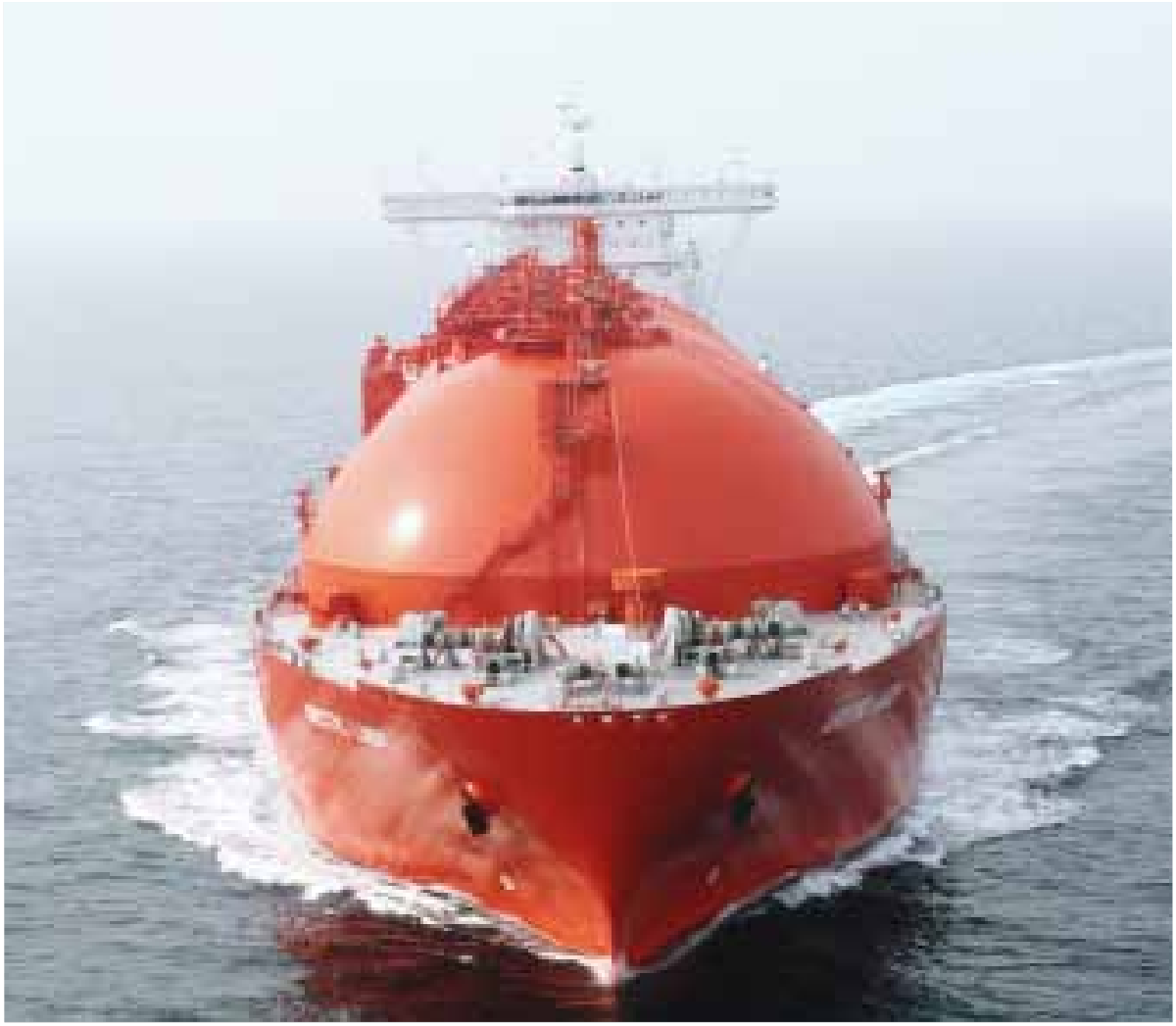

INTRODUCTION

Nordisk normally issues a Membership Circular twice each year. While covering all areas of shipping, generally these circulars tend to focus less on the energy and offshore sector than on other areas. While there may be several reasons for this, certainly a major factor is the tendency of work in this sector to be more concerned with loss prevention measures, such as contract reviews, than litigation. In addition, disputes when they do occur tend to settle before being determined by arbitrators or courts. As a result there are quite simply fewer awards and judgments to report.

Nevertheless, the volume of Nordisk's activities in the offshore and energy sector is substantial and increasing both in absolute terms and relative to our work in other areas of shipping. Accordingly we are issuing this special edition in order to present our Offshore and Energy Group and to highlight our activities within this sector. Following some general remarks in the article immediately below, the remainder of the circular contains articles focusing on particular cases and/or other activities.

We hope this special edition will enhance our members' understanding of the services we provide within the offshore and energy sector.

NORDISK OFFSHORE AND ENERGY – AN OVERVIEW

At Nordisk we have been engaged in the offshore sector ever since the early days of exploration in the North Sea in the late 60s and early 70s. Many of the drilling rigs involved were ordered by existing shipping members and drilling activities were supported by offshore support vessels (OSVs), albeit rather less sophisticated OSVs than the OSVs we typically see today. Following a number of significant discoveries, the start of production in the North Sea created new demands for maritime services. Subsequent technological developments enabled exploratory drilling at gradually increasing depths, in turn leading to deep-water production through the use of floating production units (FPSOs) and ever more sophisticated subsea installations. These new production methods have created a demand for a range of vessels and units to provide the maritime services required, and the Norwegian maritime cluster has shown a remarkable ability to cope with these demands and put itself at the forefront of developing sophisticated vessels and maritime services.

BY KNUT ERLING ØYEHAUG

Another well-known development has been the success of Norwegian maritime service providers in exporting their offshore expertise to virtually all other areas of the world. Norwegian companies are now leading providers of maritime services to the offshore sectors in Brazil and Australia, as well as in other parts of the world. In addition to the gradual development of the offshore oil and gas sector, more recently we have seen a growing trend towards developing renewable energy offshore. Several offshore windfarms have been commissioned over recent years and a number of others are in the pipeline. This has created a need for specialized vessels first to install foundations on the seabed and then the actual wind turbines. Thereafter vessels are required to maintain the installations on a regular basis. Accordingly a new market has emerged in which our offshore members are well positioned to participate.

As the trends noted above had led to a gradual increase in the volume of offshore-related work at Nordisk, some six or seven years ago we decided to establish an internal group of lawyers who would

focus particularly on the offshore and energy sector. The Offshore and Energy Group now accounts for 10 lawyers, including three of our English lawyers (see the list on the back page). The number of offshore vessels and units entered with Nordisk is now close to 600, and as for Norwegian shipping in general, the offshore sector shows a growing trend contrary to many other areas of shipping.

Although the lawyers in this group focus particularly on offshore-related issues and the members engaged in this sector, there is no Chinese wall between this group and the lawyers dealing with "traditional" shipping work. While it is true that some lawyers in the group work almost exclusively on offshore and energy cases, others handle a significant number of cases in other areas of shipping.

The bulk of our activities in the offshore sector relates to case-handling for our members. This includes day-to-day advice on issues arising in connection with the operation of offshore vessels and units, such as contractual issues between owners (Contractor) and charterers (Company). For OSV members in particular, contract reviews are important and we review and comment on a large number of contracts every year. These include tenders by oil companies where several of our members may be among the bidders. In these cases we normally provide the same comments to all members involved.

Occasionally contractual disputes under OSV charters or drilling or FPSO contracts etc. have to be pursued in arbitration or before the courts. In such circumstances we assist our members in handling the proceedings. Court cases and arbitrations in Norway are handled by our Norwegian lawyers, but we also handle a significant number of arbitrations and court cases in the UK and Singapore, as well as in the US. English and American lawyers now account for about half of our legal staff, enabling us to handle many of these cases in-house. With offshore activities now taking place in many different countries, sometimes it is necessary to accept contracts governed by local law and jurisdiction. We handle any disputes that arise under such contracts with assistance from our worldwide network of lawyers.

Notwithstanding the strict safety requirements in most areas of shipping, unfortunately accidents do happen and the offshore sector is no exception. While damage to, or total loss of, vessels and units will typically be covered by other insurance – with matters tending to be simplified by the knock-for-knock indemnity regimes used in offshore contracts – we do sometimes become involved in major accidents in order to safeguard our members' interests. Two tragic examples have been the disastrous capsize of the *Alexander Kielland* drilling rig in 1980 and more recently the capsize of the AHTS *Bourbon Dolphin* in 2007.

A number of our offshore members require legal services outside the scope of what is covered by Nordisk membership. In recent years we have accordingly expanded our transaction-related services quite significantly. As a result we have assisted in establishing new offshore companies in Norway on behalf of foreign interests and we regularly assist members and other clients with transactions such as mergers and acquisitions, sale and purchase of offshore vessels and units, sale-leaseback and financing. This trend of

increasing demand for services outside our traditional cover seems be continuing among our offshore members.

In addition to our case-handling work, we are involved in various other activities of interest to our offshore members. We now seek to arrange an annual offshore seminar for our members, normally at one or two locations on the west coast of Norway. Our Singapore office also arranges offshore gatherings in Singapore for members and clients at regular intervals. Our lawyers are also frequently invited to give presentations at offshore-related seminars arranged by institutions such as Lloyd's Academy and BIMCO in London and elsewhere, as well as at similar events in Norway. Moreover, we have been represented for a number of years on the BIMCO Documentary Committee, as well as on a number of BIMCO working groups, drafting offshore-related documents such as *Supplytime* and – at the time of writing this article – clauses related to the Maritime Labour Convention 2006 (see separate article). Our work in this area also includes contracts and documents that are used in, but that are not specific to, the offshore sector, such as *Newbuildcon, Poolcon, Saleform* etc. Finally, we have for a number of years been engaged in the work of CEFOR (the Nordic Association of Marine Insurers) in various capacities, including participation in the CEFOR Energy and Offshore Group and the working committee drafting the new Chapter 18 (Insurance of Mobile Offshore Units) of the Nordic Marine Insurance Plan 2013 (see separate article).

Overall we have seen very significant and strong growth within the offshore and energy sector. With most indicators suggesting that this is likely to continue, our offshore members are well placed to maintain and perhaps strengthen their position within this sector worldwide. As they do so we have every intention of continuing to play a significant role in this segment and look forward to assisting our members further in the years to come.

NORDIC MARINE INSURANCE PLAN (NMIP) 2013

New Chapter 18 on the insurance of mobile offshore units (MOUs)

In the Norwegian marine insurance market, hull and machinery, loss of hire and war risk insurance have for a number of years been based on the Norwegian Marine Insurance Plan (NMIP), the latest version being the NMIP 1996, version 2010. This Plan also included separate chapters on the insurance of offshore structures (Chapter 18) and builder's risk insurance (Chapter 19). By an agreement dated 3 November 2010, the Nordic Association of Marine Insurers (CEFOR) and the Shipowners' Associations of Denmark, Finland, Norway and Sweden agreed to create a new Nordic insurance plan based on the NMIP 1996, version 2010, to be named "The Nordic Marine Insurance Plan of 2013" (the "Nordic Plan"). This Plan is now completed and will come into force on 1 January 2013.

As was the case with the previous Norwegian Plan, the new Nordic Plan is accompanied by a relatively detailed Commentary. The language of the Plan and the Commentary is now English, while the Plan will also be translated into the four Nordic languages. By contrast, the previous Norwegian Plan and Commentary were issued in both English and Norwegian.

Generally, the new Nordic Plan is based on the most recent version of the Norwegian Plan and the changes are relatively limited. There is, however, one important exception. Chapter 18, which previously was headed "Insurance of offshore structures", is now headed "Insurance of mobile offshore units (MOUs)" and has been completely rewritten. The reasons for this are partly that the previous Chapter 18 to some extent was drafted primarily with drilling units in mind, and was therefore less suited to other units such as FPSOs, and partly a consensus that there was a need for a general update based on insurance practice in this area in recent years.

For the purpose of redrafting Chapter 18, CEFOR established an internal working

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group made up by insurers' representatives to prepare a first draft before somewhat later establishing a Joint Working Party with representatives from insurers, MOU owners and brokers. Nordisk was represented both in the working group and the Joint Working Party.

When drafting the new Chapter 18, one ambition was that the chapter should become more comprehensive and, apart from the general provisions of Part I (Chapters 1 – 9) of the Plan, should include all important provisions otherwise found in Chapters 10 – 14 and Chapter 16, suitably amended to meet the insurance needs of MOUs. Accordingly, all relevant provisions relating to hull insurance, total loss and loss of hire are incorporated into the new Chapter 18. The exception is war risk insurance, where Chapter 18 only refers to the general Chapter 15 on war risks. As a result, the new Chapter 18 is about 25 pages in length, compared to about three-and-a-half pages in the old Plan.

Generally, the new Chapter 18 creates a complete regime for the insurance of MOUs, or at least as comprehensive a regime as can reasonably be expected from a set of standard terms. Chapter 18 is now subdivided into five sections. Section 1 – General Rules to the Scope of Insurance, refers to and makes appropriate amendments to the general provisions of the Plan (Chapters 1 – 9). With the exception of Section 5 – War Risk Insurance, the other sections, 2 – Hull & Machinery Insurance, 3 – Total Loss Insurances, and 4 – Loss of Hire Insurance, are standalone provisions (i.e., they do not refer to the corresponding chapters of the Plan). A general review of Chapter 18 is beyond the scope of this article, and we will limit ourselves to mentioning some of the most important points concerning Section 1.

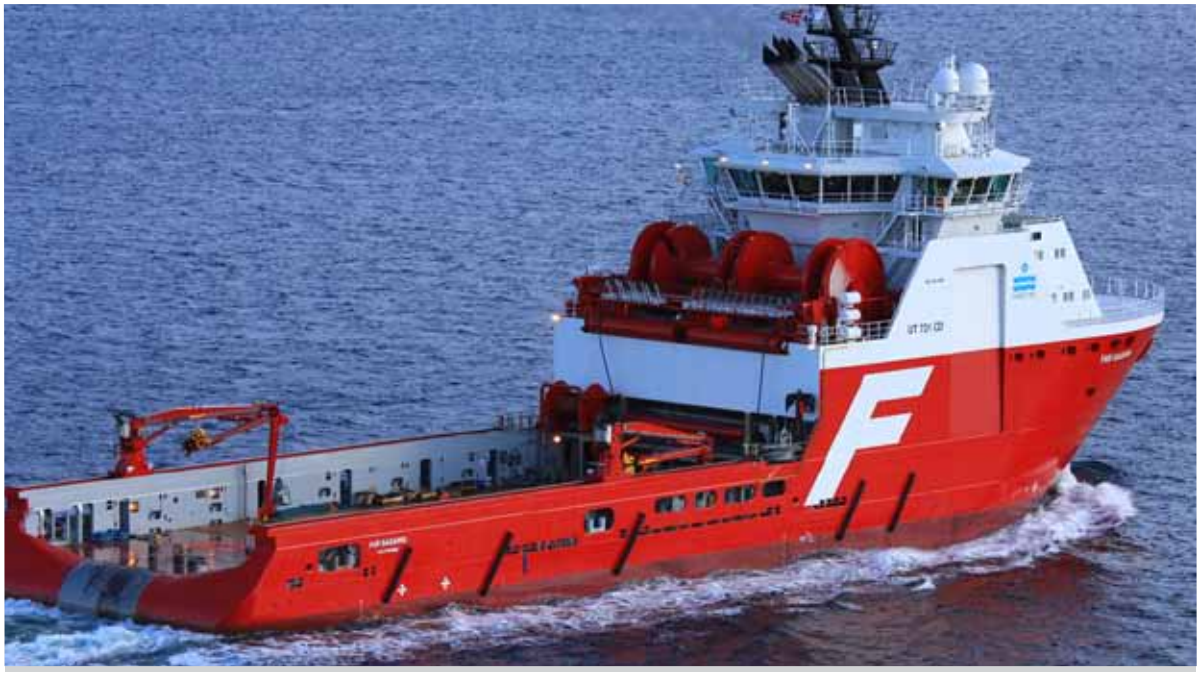
§ 18-1 (a) deals with the insurable value/sum insured. This section states that the sum insured shall be deemed to be the assessed value, unless circumstances dictate otherwise. The rules allow the sums insured to be split for MOUs with disconnectable equipment. This means that the MOU and such equipment (e.g., mooring systems and risers) may be treated as separate insured objects with separate values when the MOU is away from the working location. When the MOU is on location, however, the MOU and the equipment will be treated as one insured object.

§ 18-1 (d) provides that the insurance terminates if the MOU loses Main Class, although if this happens while the MOU is operational the insurance will not terminate until the ongoing operations are completed. Item (e) sets out certain specific safety regulations, such as requirements for blow-out preventers (BOPs) or "other well pressure control equipment of standard issue", and there are requirements to have – and comply with – a "move plan" for moving the MOU. Item (f) states that measures to avert blow-out etc. are not covered, but damage to the MOU as a result of such measures is covered.

Item (g) introduces some new limits on the insurer's liability. Liability for loss mitigation/salvage costs is capped at USD 500 million, and collision liability is capped at the higher of USD 500 million or 50% of the sum insured. Finally, item (i) deals with waiver of subrogation and co-insurance. This provision is based on the concept that the insurer's liability and rights of subrogation shall correspond to the contractual position of the insured, provided the contractual regulation in question is customary or has otherwise been approved by the insurer.

There is a great deal of enthusiasm for the new Nordic Plan in the Nordic insurance market, and it is hoped that a modernized, comprehensive Plan common to the already substantial Nordic insurance market will enhance its competitiveness towards the other main markets, both on the shipping and offshore side.

We trust the new MOU insurance regime will prove to be a better tool for the insurance of such units than its predecessor, and that the need for additional clauses etc. will be reduced. We look forward to assisting our members with any issues arising under the new Chapter 18 or otherwise in the time ahead.



OSV FIXED FOR "WORLDWIDE" OPERATION ON SUPPLYTIME 2005

Risk allocation for delays in obtaining local work permits and visas

A Norwegian arbitration award

Offshore support vessels (OSVs) typically operate for extensive periods within particular jurisdictions. When moving to a new jurisdiction, problems may arise because of the significant variations between different jurisdictions in requirements concerning crew visas and work permits, as well as other permits, licences, local-content rules etc. For instance, both Brazil and Australia require crews of OSVs operating within their jurisdictions to obtain visas and (in some circumstances) work permits. Clearly delays may occur when obtaining these documents. Who should bear the risk of such delays, owners or charterers?

We recently represented one of our members in a dispute with charterers caused by just such requirements. Because of delays in obtaining work permits and visas for the vessel's crew, the vessel was unable to perform the services envisaged under the charterparty for a considerable period. Charterers' claim that the vessel was off hire was disputed by owners and the matter was referred to arbitration.

The facts

The vessel, an offshore construction vessel, was fixed to charterers under a long-term "worldwide" charterparty based on the *Supplytime 2005* standard form with some additional clauses. All of the clauses referred to in this article, however, had standard *Supplytime 2005* wording. The contract was subject to Norwegian law with disputes to be referred to arbitration in Oslo.

In summer 2009 charterers notified owners that they intended to operate the vessel in Brazilian waters. Accordingly they requested owners to start preparing visa applications for owners' crew. The members of owners' crew were not the only members of the vessel's crew to require visas. In addition to owners' crew, the charterers would employ their own project-specific crew and there were also the crew of several of

BY NORMAN HANSEN MEYER

their sub-contractors. Charterers had entered into a contractual scheme commonly seen in Brazil whereby the vessel was bareboat-chartered directly from charterers to the Brazilian client while the construction services (including the entire crew) were provided under a separate contract entered into between charterers' Brazilian affiliate company and the Brazilian client. In order to operate in Brazilian waters for more than 30 days, all non-Brazilian crew members had to obtain Brazilian work permits. Each permit application had to be "sponsored" by a local company. This involved, among other things, confirming that the crew member had sufficient health insurance cover in Brazil and issuing a letter of guarantee. Charterers decided that their Brazilian affiliate would sponsor all members of the crew, including owners' crew. The first step was to obtain approval for the work permits from the Brazilian Ministry of Work and Labour. Thereafter the Brazilian Ministry of Foreign Affairs was to inform the relevant consulates that the approvals had been granted. This would enable individual crew members to apply for and collect their visas at their local consulates.

Most members of owners' crew were Spanish nationals, and owners instructed their Spanish manning agents to start making the necessary preparations at the Brazilian consulate in Madrid. Owners, as instructed by charterers', also contacted charterers' visa agents in Brazil. These agents were to handle the work permit application process in Brazil on behalf of both owners' and charterers' crew.

The application process in Brazil suffered significant delays. Not only was the local sponsor in Brazil slow in submitting the work permit applications, but processing at the Ministry of Work and Labour then took almost two months due to, among other reasons, a lack of staff. In addition, once the work permits had finally been approved in early-to-mid-December 2009, further delays ensued at the consulate in Madrid due to the Christmas holidays. Consequently the vessel's minimum manning requirements were not fulfilled and the vessel was unable to perform any services in Brazil from mid-December 2009 until mid-January 2010 when a sufficient complement of crew was able finally to embark.

Charterers claimed that the vessel was off hire for 25 days due to "deficiency of crew" and suspended payment of hire accordingly. Owners rejected the off-hire claim and commenced arbitration in Norway in order to pursue their claim for hire. Owners argued that 1) there was no "deficiency of crew", and 2) it was charterers' obligation to procure work permits pursuant to Clause 6 (b). The latter clause provides that charterers shall obtain "*relevant permission and licences from responsible authorities for the Vessel to enter, work in and leave the Area of Operation*". According to owners, the term "Vessel" in this context had to be interpreted as referring to both the vessel and the crew. To the extent that owners had any obligation to provide visas, they argued that the off-hire incident fell within one of the exclusions in the off-hire clause. Namely, that the vessel had

been prevented from working as a result of "*any act or omission of the Charterers, their servants or agents*" (clause 13 (a) (vi)).

Charterers asserted that owners were responsible for obtaining all permits relating to the crew, while charterers were responsible for permits relating to the vessel. Charterers relied inter alia on Clause 8 (a), which states that owners shall cover "*all liabilities for consular charges appertaining to the Master, Officers and Crew*". According to charterers, this had the effect that owners had to cover all expenses of, and bear the risk of any delays in, the work permit and visa application processes. Charterers further denied that the off-hire event was the result of their "act or omission" since, in their view, the Brazilian visa agents were owners' agents and charterers' Brazilian affiliate was owners' sponsor in relation to owners' crew. If this were the case, the off-hire event could not fall within the exception in Clause 13 (a) (vi).

The parties jointly appointed a single arbitrator who rendered his award following a five-day oral hearing.

The award

The arbitrator ruled in favour of owners. Firstly, the arbitrator concluded that obtaining work permits and visas was charterers' risk pursuant to Clause 6 (b). Owners, on the other hand, had a duty merely to "assist" in procuring such permits and visas. The arbitrator agreed with owners that the term "Vessel", within the meaning of that clause, included not only the vessel as such but also the vessel's equipment and crew. According to the arbitrator, Clauses 8 (a) and 9 (d) supported his interpretation of Clause 6 (b) that work permits and visas were charterers' risk.

After having reached his conclusion on the interpretation of the relevant provisions in the charterparty, the arbitrator considered whether the parties' conduct nevertheless demonstrated the existence of a common intention whereby owners had accepted partial or full responsibility for obtaining the work permits and visas. Here the arbitrator's firm opinion was that no such common understanding or intention could be established. Indeed, he found the conduct of the parties to have conformed with the risk allocation provided for in the charterparty. In the arbitrator's opinion, several facts clearly indicated that charterers had assumed responsibility for the process of obtaining work permits in Brazil. Firstly, charterers' affiliate company had acted as the local sponsor. Secondly, charterers had appointed, instructed and paid the Brazilian visa agency. Finally, the entire application process in Brazil had been managed by charterers and their servants. Indeed, several important decisions concerning the application process had been made by charterers without even consulting owners.

According to the arbitrator's interpretation of Clause 6 (b), the charterers also bore the risk for the subsequent process of obtaining visas from the consulate in Madrid. Owners' duty here was merely to assist and pay consular charges pursuant to Clause 8 (a). The arbitrator held that the parties' dealings with the consulate in Madrid had been in accordance with this risk allocation.

During the oral hearing, some of the parties' arguments had referred to, and drawn analogies from, case law concerning a vessel's "fitness for service". The arbitrator made some interesting comments in

this respect. As a starting point, he noted that owners had a duty to provide a sufficient complement of officers and crew for the vessel to operate within the agreed area of operation. However, the scope of this obligation would depend upon the interpretation of the provisions of the charterparty and the facts of the case. The arbitrator referred to the comments of Hobhouse, J. in *The Derby* [1984] 1 Lloyd's Rep. 635 and on this basis concluded that owners had complied with their contractual obligation to provide a vessel "fit for service", even though the vessel for a certain period had lacked the necessary permits and licences for carrying out operations in Brazil. The arbitrator emphasised that the need to obtain work permits had been caused by charterers' instructions to the vessel to operate in a particular jurisdiction and be employed on a particular project. He also referred to remarks in the standard text book *Time Charters*, which implied that a vessel would not necessarily be "unfit" if crew changes were needed because of local rules.

The arbitrator then considered whether charterers were entitled to claim off hire for the relevant period. He ascertained that the vessel had been "prevented from working", referring inter alia to remarks in *Time Charters* and in the English case *The Laconian Confidence* [1997] 1 Lloyd's Rep 139. Furthermore the arbitrator held that there had been a "deficiency of crew". Here he referred inter alia to English case law (*The Illissos* [1949] Lloyd's Rep 82 and *The Saldanha* [2011] 1 Lloyd's Rep 187) and remarks in the text book *Scandinavian Maritime Law* by Falkanger and Bull. Clearly there had also been a loss of time.

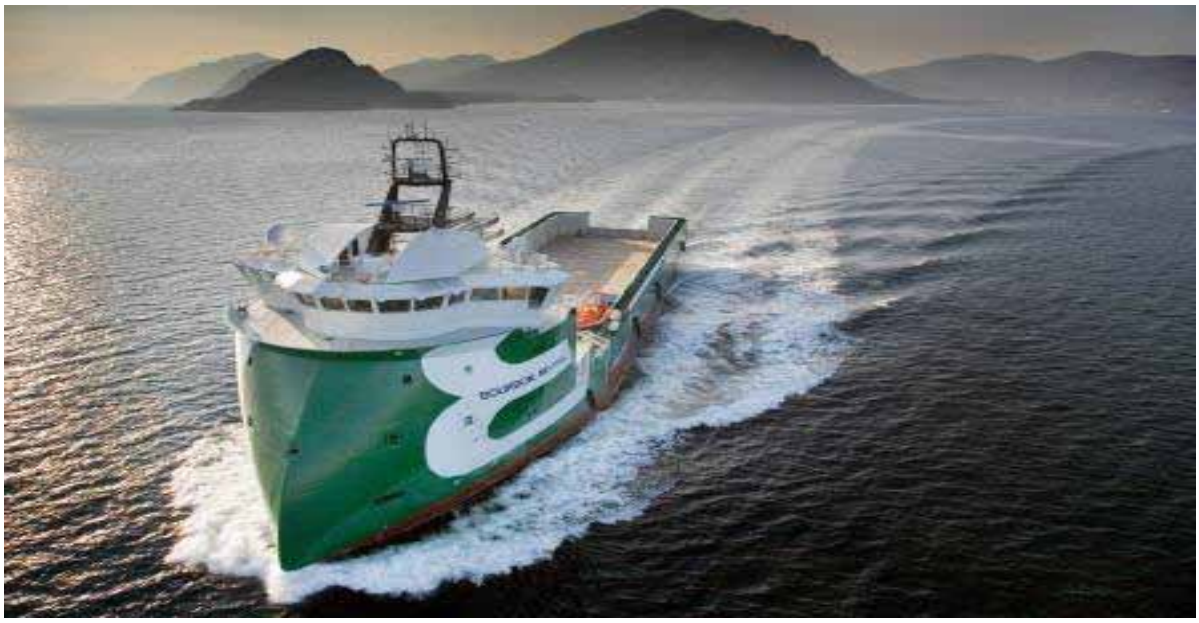
Finally the arbitrator considered whether the exclusion in Clause 13 (a) (vi) applied, i.e., whether the vessel had been prevented from working as a result of "a*ny act or omission of the Charterers, their servants or agents*". He noted that there was no requirement of fault on the part of charterers, before referring to his previous finding that the applications to the Brazilian Ministry of Work and Labour, the Brazilian Ministry of Foreign Affairs and the Brazilian consulate in Madrid were charterers' risk. Despite these previous findings, he noted that Clause 13 (a) (vi) required a separate assessment of whether the loss of time had been caused by charterers' acts of omissions. Nevertheless, as we shall see, he placed considerable emphasis on the interpretation of Clause 6 (b).

The arbitrator concluded that the loss of time had in fact been caused by charterers' acts and omissions. There were three grounds for this conclusion. Firstly, it followed from general principles of causation that if charterers had not delayed the final submission of the work permit applications, the visas would most likely have been available at the consulate in Madrid in December 2009. Secondly, it followed from the arbitrator's interpretation of Clause 6 (b) that charterers bore the risk of any delays in the work permit and visa application processes (in both Brazil and Spain). Finally, the arbitrator held that owners had assisted the application processes satisfactorily and had not caused the delays. Accordingly the exclusion in Clause 13 (a) (vi) applied and charterers were not entitled to suspend hire during the relevant period.

Conclusion

We believe this award is of interest for our offshore members for several reasons. Firstly, there are few court judgments or arbitration awards, either in Norway or in the UK, concerning the interpretation of *Supplytime 2005* and, in particular, Clauses 6, 8 and 13. The arbitrator applied a literal interpretation of the relevant provisions and relied to a significant extent on English case law and standard texts. For these reasons we believe that this award should contribute to clarifying the general allocation of risk under *Supplytime 2005* under both English and Norwegian law. Secondly, the award to some extent clarifies a more specific question that often arises in "worldwide" charterparties fixed on *Supplytime 2005*: are risks relating to work permit and visa applications (and, by analogy, various other local requirements) owners' or charterers'?

Despite this recent award, we would nevertheless advise any of our members who are in the process of entering into charterparties with extensive "areas of operation" (such as "worldwide" or "South Pacific") to include a provision dealing explicitly with local permits, visas and licences (with regard both to the vessel and the crew), as well as compliance with local-content rules. It is important to ensure that such a provision deals with both risk and costs, i.e., who bears the risk of delay and who should bear the costs of compliance. We would of course be pleased to assist any of our members in drafting such clauses.



GREEN OPERATION OF OSVs

Over recent years there has been a significant increase in focus on making the operation of offshore vessels more energy efficient and environment-friendly. A number of new designs have been developed to improve the vessels' energy efficiency and suppliers of all kinds of machinery, equipment and even hull painting promise that their products will bring about significant improvements. In Norway the establishment of a NOx Fund has also enabled owners to fund significant improvements to vessels, e.g., the ability to operate on LNG in addition to traditional fuel. More recently, the focus has shifted somewhat from design to operation as operators have realised that significant efficiency gains can be made on the operational side. This drive towards energy-efficient design and operation has been pushed partly by regulatory requirements designed to reduce emissions, but also by high fuel prices.

While innovative developments in this area are mostly of a technical nature, there are also some other factors worth taking into account. OSV owners make their living by chartering out their vessels, raising the question whether the charterparties currently in use for OSVs have the right mechanisms and incentives to encourage the parties to adopt more energy-efficient and environment-friendly options. Apparently this is not the case. A typical OSV charterparty, such as *Supplytime 89* or *2005*, is a standard time charter whereby owners are compensated by way of a daily hire rate, with charterers providing fuel at their own expense. Charterers are also in most cases responsible for payment of emission-related charges such as NOx taxes. In isolation, this approach provides little incentive for owners to achieve more energy-efficient operation. Moreover, charterers appear traditionally to have paid little attention to such issues. This is now changing. At a seminar on "Green OSV Operations and Design" arranged in London by Lloyds in June 2012, Nordisk gave a presentation on this topic, pointing out the lack of appropriate incentives and mechanisms in existing OSV charters. Below we summarise some of our observations.

In other areas of shipping, we have for some time seen attempts to address the issue of energy-efficient operation. One such mechanism is a "slow steaming" clause, which allows charterers to order the vessel to proceed at reduced speed, reducing fuel consumption and consequently emissions. Under a time charter, this will generally have financial benefits only for

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charterers. Under a voyage charter, however, while the benefits of lower fuel costs favour the owner, the extended voyage period does not. Accordingly, some mechanism distributing the benefits and costs is called for, such as one providing compensation for increased voyage time less bunkers saved and/or compensation for lost demurrage.

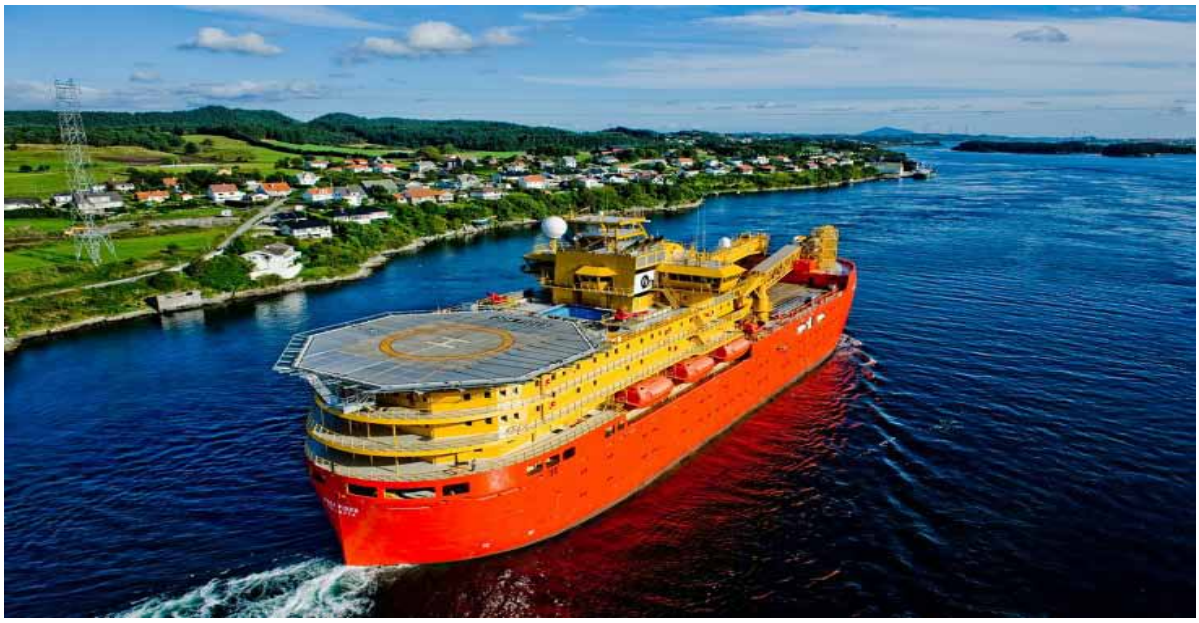
Another mechanism currently in use in voyage charters is the "virtual arrival" clause. This addresses the situation where charterers take the view that there is no need for the vessel to reach a certain port until a certain date and accordingly order the vessel to proceed more slowly. While owners of course benefit from lower fuel consumption, they lose the opportunity to earn demurrage at the port. A virtual arrival clause attempts to deal with this problem by supplying mechanisms to share the burdens and benefits involved.

For various reasons these mechanisms are not so effective in the case of OSVs. This is partly because most OSVs sail only relatively rarely at full speed from one place to another. Instead they may be on standby for significant periods, or involved in activities such as subsea-installation, repair or maintenance or waiting for suitable weather. Moreover, OSVs may well have diesel-electric engines, which tend to reduce the benefits of slow steaming. Accordingly the issue of energy efficiency has to be approached somewhat differently in this sector, given the need to take into account the vessels' characteristics and typical operational modes.

In response to a DNV initiative, a group of seven major OSV operators in Norway has launched the "Joint Industry Project – Energy Efficient Offshore Partners". This project aims to "*identify, assess and describe opportunities for the offshore vessel industry to operate with improved energy efficiency and lower emissions*". During Phase 1 of the project, the participants analysed the operation of their own fleets. A preliminary report identified a number of areas with potential for improvement and put the overall improvement potential at 15.2 %. The project has now progressed to Phase 2, in which a number of significant charterers are also participating.

The potential for improvement identified in Phase 1 of the project includes various measures within the following areas: ship performance; voyage performance and operations; and engines and consumables. The measures fall into three categories: "Shipowner controlled at no or low cost" (4.6 %); "Charterer controlled at no or low cost" (5.8 %); and "Shipowner controlled but with some cost" (4.8 %).

Recommendations made so far by the project include: the issuance of best practice guidelines; the implementation of an appropriate incentive scheme; and the inclusion of energy-efficiency clauses in charterparties. There are clearly some challenges in relation to measuring improvements in efficiency and one possible solution is to focus on behaviour rather than measurable effects, e.g., frequency of hull-cleaning, propeller polishing and so on. In our view, there is reason to believe that such schemes will gradually become a regular feature of OSV charterparties.



THE MLC 2006 – A CHALLENGE FOR THE OFFSHORE SECTOR?

The Maritime Labour Convention (MLC 2006) was adopted by the International Labour Organisation (ILO) in February 2006. The convention is a comprehensive document that consolidates and replaces more than 60 existing maritime labour instruments. It is referred to as the "Fourth Pillar" of the International Regulatory Regime for Quality Shipping, which otherwise consists of the International Convention for the Safety of Life at Sea (SOLAS), the International Convention on Standards of Training, Certification and Watchkeeping for Seafarers (STCW), and the International Convention for the Prevention of Pollution from Ships, 1973 and Protocol of 1978 (MARPOL).

The convention requires ships of 500 gt or more engaged in international shipping to have a Maritime Labour Certificate and a Declaration of Maritime Labour Compliance (DMLC). The convention also applies to smaller ships, but only with respect to inspections, not certification.

In order for the convention to come into force, it had to be ratified by at least 30 countries representing at least 33% of global tonnage. This requirement was met in August 2012 when the Philippines became the 30th country to ratify the convention. At the time of writing 32 countries have ratified, representing significantly more than the required 33% of global tonnage. Norway ratified the convention in 2009, and amendments to existing Norwegian legislation in order to comply with the convention had already been enacted in 2008, but will not come into force until the convention does so. This will happen on 20 August 2013.

The MLC 2006 covers a wide range of issues relating to seafarers' welfare and their working environment. Its provisions are designed to ensure safe working conditions, fair terms of employment, medical care, hours of rest, proper living conditions, recreational facilities, food and catering etc.

The scope of this article does not allow for any comprehensive review of the MLC 2006. Instead we will touch upon a few potential challenges for offshore vessels. The convention will be implemented in the national legislation of the ratifying flag States, which will issue the Maritime

BY KNUT ERLING ØYEHAUG

Labour Certificates and, together with the owner, the DMLC. This certification will have to be revalidated every five years. In addition there will be mid-term assessments of onboard compliance. Port State Control (PSC) inspections will also be crucial for the enforcement of the convention. Under the convention, the starting point is that PSC inspectors will have to accept Maritime Labour Certificates issued by a flag State as prima facie evidence of the vessel's compliance with the MLC 2006. If the inspectors have reason to believe otherwise, however, or have received a specific complaint, more detailed inspections may be carried out. This may in turn result in detention and/or fines.

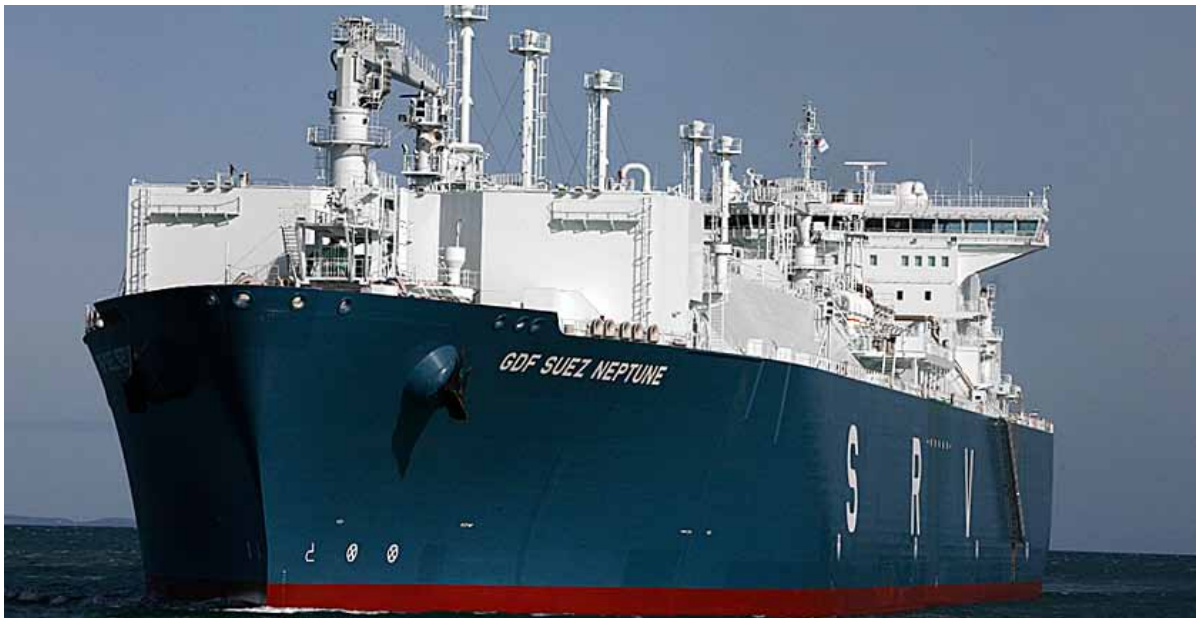
From a charterparty perspective, compliance with flag State requirements based on MLC 2006 will typically be the owner's responsibility and as such no different from compliance with other flag State requirements. However, many offshore vessels, such as offshore construction support vessels (OCSVs), have a number of persons on board in addition to the owner's marine crew during operation. These persons are typically employed by charterers or their clients and have no contractual relationship with the owner. The MLC 2006 sets forth a wide definition of "seafarer", which would be likely to include several categories of such additional personnel. This is a potential challenge for owners, given their responsibilities for compliance with the MLC 2006. For example, the convention obliges the owner to have employment agreements with all "seafarers" on board the vessel and also makes the owner responsible in the event of seafarers' sickness, injury or death etc. The shipowner may also be liable financially for non-compliance revealed by PSC inspections.

Is it possible to pass on such responsibilities and/or their financial consequences down the contractual chain? As an example, while operational an OCSV may have around 20 marine crew and perhaps 50 or more "project" personnel on board. In our view, responsibility for compliance (or at least the associated financial burden) with respect to the project crew should be passed on to the charterers and/or their clients. We look forward to assisting our members in achieving this aim.

Other potential challenges may arise in relation to ship management contracts, crew management etc. The crew may be employed by the manager on behalf of the owners, or in some cases by the manager himself. A manager who is responsible for the operation of the ship (i.e., a technical manager) is likely to be considered the "shipowner" under the MLC 2006. A manager who is only providing crew, however, will not be the "shipowner" for the purposes of the convention, although he may be the employer of the crew. Depending on the circumstances, specific clauses to address these challenges may be required in ship management agreements and crewing agreements.

With less than a year to go until the MLC 2006 comes into force, BIMCO has responded to approaches from several of its members and has established a working group to investigate the need for additional clauses for *Supplytime 2005, Shipman 2009* and *Crewman A and B* (both 2009). Since all these documents have been revised relatively recently, the intention at this stage is merely to propose additional clauses for use with the documents, not a wholesale revision. The working group, on which Nordisk is represented, is aiming to finalise the draft clauses in time for adoption by BIMCO's documentary committee by late spring 2013.

At this stage it is too early to say whether the implementation of the MLC 2006 will create significant challenges. The outcome will depend partly on how the convention is implemented by the various flag States as well as on how it is enforced in practice through PSC inspections etc. We will follow developments closely, watching in particular for any need to adjust charterparties and other contracts used in the offshore sector.



FSRUs AND LNG REGASIFICATION CONTRACTS

Main risks from an owner's perspective

Introduction

As demand for energy and electricity has increased worldwide, since 2005 we have seen some LNG vessel owners developing fleets of LNG regasification vessels (commonly known as Floating Storage Regasification Units, FSRUs). The special feature of an FSRU is its ability to receive and store LNG, which it subsequently regasifies and discharges as natural gas.

The contracts used for fixing FSRUs are quite different from the charterparties used for ordinary LNG transports. The owner under an FSRU contract, as well as fulfilling the usual "owner's obligations", will be providing additional services of a sophisticated technical nature. Furthermore, the interface between the charterer's property, such as the topside facilities and the pipeline securing the off-take capacity, and the FSRU is of crucial importance for the successful operation of the regasification services. The contractual provisions in this respect are similar to those found in some offshore service contracts.

FSRU projects may be fixed on time-charter terms. It is not unusual, however, for the "time char ter" to be split into two contracts: a bareboat charter and a service agreement. In this case the vessel is provided under the bareboat charter while the more specialised FSRU services are rendered under the service agreement.

Below we address some issues that we find need particularly careful consideration in order to mitigate the risks involved in FSRU projects, namely: commencement of hire, staying on hire, liabilities and indemnities, warranties/performance, and taxes.

Commencement of hire

Commencement of hire will normally require the charterer's acceptance of the vessel, evidenced by the signing of an acceptance protocol. In order to mitigate the risk of the charterer rejecting delivery of the vessel, it is important to draft

BY CAMILLA BRÅFELT

the delivery mechanism carefully and to ensure that the owner has full control over the delivery criteria. For instance, if the vessel is a newbuilding, the owner should ensure that the vessel's specification in the FSRU contract, which the vessel shall "(fully) comply with" at the time of delivery, is aligned with the specification in the building contract, including all margins given to the yard.

A concern for the owner in relation to delivery is potential exposure in the event of delay. Such exposure could be onerous if the owner were to face unlimited liability for the charterer's losses due to delay in delivery. Accordingly, such liability should be capped, e.g., by providing for liquidated damages for each day of delay, always subject to a maximum number of days for which liquidated damages may be applicable. Ideally a charterer who terminates in the event of delay in delivery, which option should only be available to the charterer after the maximum amount of liquidated damages has been incurred, should not be entitled to any damages in addition to the liquidated damages.

FSRU contracts usually require commissioning to be carried out in relation to delivery. As some time will necessarily elapse between the time the owner presents the vessel for delivery and the time the commissioning process is completed and the acceptance protocol signed, it is important to specify clearly who will pay for this time. It is not unusual for this liability to be split, with the charterer paying for a defined period and all time used in excess of this period being for the owner's account. It is important to note here that the FSRU will provide some services during the commissioning process, e.g., the regasification and discharging of gas. The charterer should pay for any services rendered during the commissioning process, even if the time spent on commissioning is for the owner's account.

A final point in relation to delivery is that the owner should be wary of a request by the charterer for the right to use the vessel for a predelivery voyage. An owner who agrees to such a request must ensure that all risks relating to such a voyage, including the risk of delivery being delayed under the FSRU contract, are for the charterer's account. Otherwise the owner could be at risk of losing a long-term project by complying with the charterer's order to perform one short pre-delivery voyage.

Staying on hire

Once the vessel has been successfully delivered to the charterer, clearly it is important for the owner that the vessel stays on hire throughout the charter period. Hence the wording of the off-hire clause, and of any other clauses in the FSRU contract that may reduce the time or rate of hire, will be of importance.

From an owner's perspective, the events that may place the vessel off hire should obviously be reduced to a minimum. Equally importantly, the owner needs to ensure that the vessel will only be off hire for the time actually lost due to the off-hire event, and not for the whole period from the commencement of the off-hire event until the vessel is ready to resume service. If the owner has to agree to the latter approach, his position will be improved if the clause states that the owner shall be compensated for services rendered and distance made good while off hire. It is important to note, however, that even though the owner will be compensated for services rendered, off hire days will still accrue and may potentially result in termination due to prolonged off hire. Generally owners should only accept net-loss-of-time off-hire clauses. This ensures that hire is suspended only for time actually lost. Another benefit of such clauses is that the charterer has to prove that time has been lost, instead of the owner having to prove what services have been rendered and the amount of compensation due.

Owners should try to limit the application of off-hire clauses to situations where the vessel is totally unavailable. In cases where the vessel is actually performing some services, the situation should be regulated by a service failure compensation scheme (see below). Such a scheme will compensate the charterer for any reduction in services and potential loss of time, while at the same time allowing the vessel to remain on hire while the vessel is providing some services under the contract.

In order to ensure that the vessel stays on (full) hire, the owner should make sure that the charterer bears the whole risk for charterer's performance of his obligations to provide certain items and services under the contract. Such items and services include the quality of the LNG provided by charterer, the functioning of the charterer's topside facility, and the provision of sufficient off-take capacity. This can be achieved by making the owner's obligation to perform throughout the contract subject to the

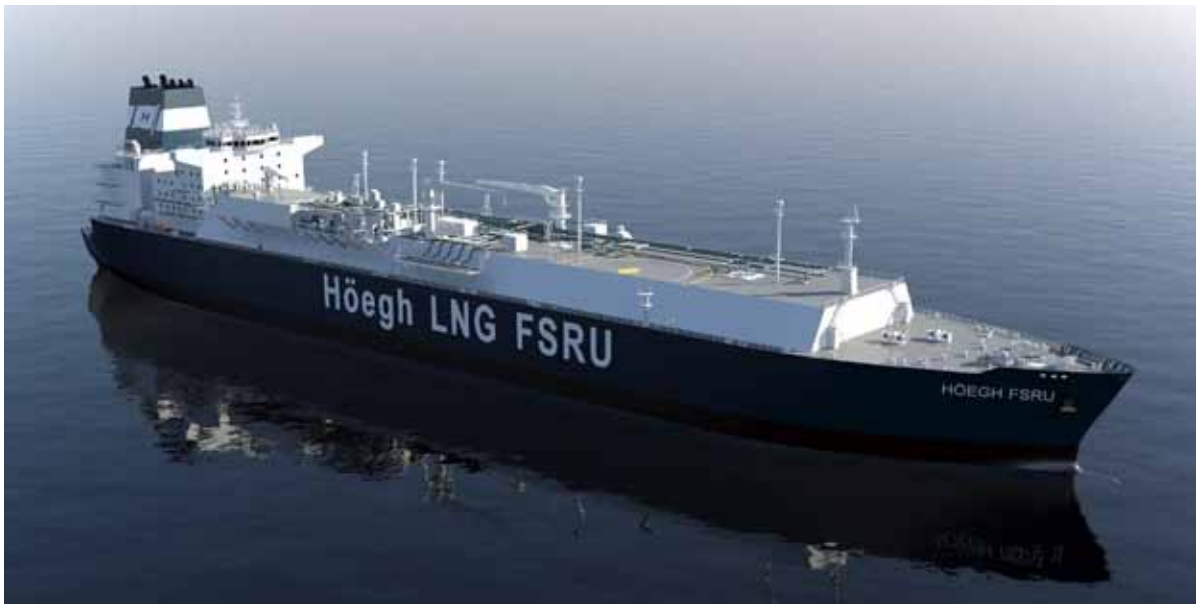
charterer's continued performance of his obligations under the charter. The charterer's obligations should be specified clearly. Examples of the charterer's obligations include importing the vessel, ensuring that the site and the facility are ready and suitable for the vessel, providing mooring for the vessel, and providing the LNG, pipeline and gas off-take capacity. The owner will only be able to perform the FSRU services (e.g., loading of LNG, regasification of the LNG, and gas discharge) if the charterer fulfils his obligations. Consequently, if the charterer is in breach of any of his obligations, the owner should be excused from performing his services while continuing to earn full hire. For example, if the charterer does not provide off-take capacity for gas discharged from the FSRU, this will affect the owner's possibility to perform the services in accordance with the contract. Quite simply, the owner will be unable to discharge gas, which in turn means that the FRSU will have to stop regasification and at some point will be unable to receive LNG. As the owner's non-performance in this situation will be a direct result of the charterer's failure to comply with his obligation to provide sufficient off-take-capacity, the owner should not be penalised for failing to discharge gas.

Likewise, the charterer should accept full risk of force majeure. It is not unusual for FSRU contracts to reserve force majeure as an excuse for non-performance for the owner's benefit. The effect of this is that the owner is entitled to full hire if his performance is prevented by a force majeure event. The rationale for this has usually been that the charterer's main obligation under these contracts is to pay hire, which will not be excused by force majeure, while the owner's obligations are of a nature that easily may be affected by force majeure. A compromise may be to give the charterer a right to terminate the contract if the force majeure event prevents the owner from performing for a prolonged period, e.g., 12 months, but coupled with an obligation to pay compensation to the owner if the charterer choses to terminate the contract in such circumstances.

FSRU contracts contain specific performance criteria that the owner must comply with throughout the charter period, such as a specific loading and discharging rates and regas and storage capacities. If the owner is in breach of any of these performance criteria, FSRU contracts contain regimes, the so-called service failure compensation schemes mentioned above, for compensating the charterer for the reduction in performance. Some regimes operate on the basis of reducing hire in proportion to the reduction in performance, while others apply a system of damages/penalties. These regimes are completely separate from off hire and should not be applicable for the same events. Ideally, as mentioned above, off hire should only apply where the vessel is completely unavailable, while the service failure compensation scheme should regulate situations where the vessel continues to provide some services. Unfortunately, some FSRU contracts we have seen fail to distinguish clearly between the circumstances in which service failure compensation and off hire would apply. Such a contract may expose the owner to two types of liability – off hire and service failure compensation – in relation to the same event.

Finally, the charterer's right to terminate the contract

obviously has an impact on whether the vessel can stay on hire. Several charterers insist on a right of early termination. From an owner's perspective, however, the charterer's right to terminate should be limited. Termination of the contract may have onerous consequences for the owner unless he receives proper compensation. The termination fee the charterer should have to pay on exercising the right to early termination should, as a minimum, cover the owner's capital expenditure for the remaining period of the contract. Any smaller termination fee may jeopardise the owner's financial stability and be devastating if new employment is not secured immediately after termination.



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Liability and indemnity

The liability and indemnity provisions in FSRU contracts have much in common with those found in offshore service contracts. Liability for damage to either personnel or property is usually regulated on a knock-for-knock basis, with each party bearing the cost of damage to its own personnel and property. Such a regime should generally be acceptable to owners. It is not unusual, however, for FSRU contracts to contain more extensive knock-for-knock regimes than the traditional approach. For instance, the knock-for-knock regime may apply to other types of damage than damage to personnel and property, the definition of "Contractor/Owner Indemnified Personnel" may be unusually wide, or the "Charterer's Group" may not include some important third parties with whom the charterer has a contractual relationship, such as the owner of the infrastructure to be used for loading and discharging or the owner of the pipeline that the gas is going to be sent through after discharge. Such clauses may increase the owner's exposure compared to the position under a traditional knock-for-knock regime.

Liability for pollution is an important aspect of the liability regimes in FSRU contracts, and is usually covered by the knock-for-knock regime. The owner should only accept liability for pollution that emanates from the FSRU itself. The charterer should carry the risk of all other pollution.

FSRU contracts, like most other shipping and offshore-related contracts, should exclude liability for consequential losses. This exclusion should be general and not limited to the liability and indemnity provision. Furthermore, it is important to define carefully the meaning of consequential losses in order to ensure the exclusion of potentially significant losses such as loss of profit. We should emphasise that under English law it is not necessarily sufficient to state that "neither party shall be liable for consequential loss" in order to exclude loss of profit. The contract should specify that some important categories of losses (loss of profit, loss of business opportunity, loss of use, loss of revenue etc.) are excluded whether

or not they are considered to be consequential or indirect.

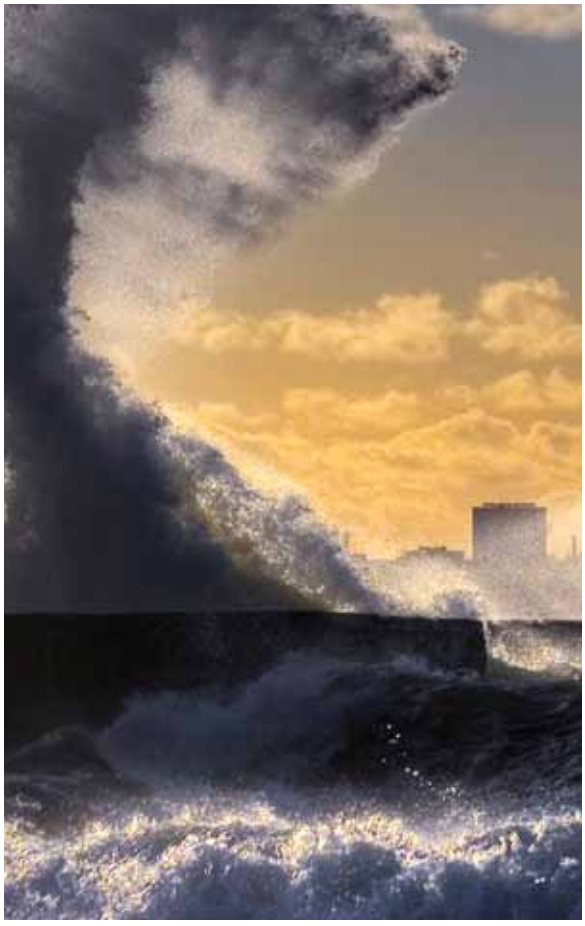
In addition to liability for damage covered by the liability and indemnity provision, both the owner and the charterer will also be exposed to liability for breach of contract. FSRU contracts usually contain detailed provisions regarding damages for breach of contract, in particular in relation to termination for breach of contract. These provisions are of importance when carrying out a contract risk assessment. If the contract is terminated due to the owner's breach, the owner may be liable for damages. These damages may be specified in the contract ("liquidated damages"), with such damages usually operating on a sliding scale according to when the contract is terminated or alternatively a fixed amount applicable irrespective of when the contract is terminated. These liquidated damages should be the only damages available to the charterer. As an alternative to liquidated damages the owner may be liable for losses caused to the charterer by the breach/termination. If this approach is used, it is of the utmost importance that consequential losses are excluded (as discussed above). From an owner's perspective, termination should be the sole remedy available to the charterer for the owner's breach.

Conversely, where the owner is entitled to terminate due to the charterer's breach, the contract should clearly regulate the owner's right to damages. The same liquidated-damages approach as described above should be available, but ideally with different levels of damages. From an owner's perspective, it will be important to ensure the availability of damages in an amount that will reflect his (and his investors') interest in the contract.

Finally, to cater for the owner's need to assess his potential exposure under an FSRU contract (and his need to insure against such exposure), it is not uncommon for such contracts to place a global cap on liability. We do however see examples of carve-outs from such caps, which is unfortunate as it undermines the purpose of a global cap. Generally the liabilities and indemnities included in the knock-for-knock regime are not included in the global cap. This should not however be problematic provided that the liability/indemnity exposure is fully absorbed by the party who has suffered the damage and his insurers.

Warranties/performance

FSRU contracts typically impose a set of more general performance obligations on the owner, concerning matters such as the vessel's specifications, crew requirements and maintenance. When negotiating such contracts we frequently encounter problems in relation to the maintenance obligation. While charterers would prefer an absolute maintenance obligation for the entire charter period, owners should only agree to maintain the FSRU on a due diligence basis. Some charterers argue that the maintenance obligation should be absolute and should apply "throughout the charter period", with any failure to comply with the vessel's specifications and other (vessel) related requirements entitling the charterer to a reduction of hire to the extent necessary to indemnify the charterer for such failure. Some charterers have argued that this is in line with industry standards and referred to clause 3 of *ShellLNGTime* as the "LNG standard" on this issue. *ShellLNGTime* clause 3 is almost identical to clause 3 of *Shelltime 4* (as well as to the equivalent clause in the previous version of



Shelltime). In The *Fina Samco* [1995] 2 Lloyd's Rep. 344, however, this argument was rejected by the Court of Appeal. The Court of Appeal decided that despite the unfortunate wording of clause 3 of the first version of the *Shelltime* charter, the maintenance obligation was a due-diligence obligation as set out in clause 3 (i) and not an absolute obligation. The court stated that on delivery the vessel had to comply with the specifications listed in the charterparty. If the vessel did not comply with these specifications on the delivery date, the charterer would be entitled to a reduction of hire. If the vessel post-delivery failed to comply with the listed specifications, the charterer would be entitled to place the vessel off-hire pursuant to clause 3 (iii), provided that the failure to comply with the specifications was caused by the owner's failure to use due diligence in maintaining the vessel. This result is not obvious from the wording of the particular clause and owners should generally be cautious about accepting similar wording. Accordingly the contract should state clearly that the maintenance obligation is a due diligence obligation only. This will ensure that the owner is not bound by an absolute maintenance obligation.

Contracts where the charterer is given a right to trade the vessel set forth a number of provisions in this regard that we will not discuss in this article. However, one particular warranty given by the owner should be mentioned: the contract will contain a warranty by the owner that the vessel will be compatible with terminals. For an owner it may prove onerous for the charterer to have an unrestricted right to nominate terminals that the vessel shall comply with. Generally such warranties are therefore restricted to compatibility with a list of named terminals at a specific date, e.g., the delivery date. This is because an owner can only be certain that his vessel is compatible with a particular terminal at the date the contract is entered into. If he warrants compatibility at a later date, he will assume the risk of changes to the terminal requirements in the future. Accordingly this risk should be clearly addressed in the contract.

Taxes

Finally we should emphasize that FRSU contracts may have complex tax implications. An FSRU is likely to remain in one country for a substantial period, which may require the vessel to be imported into and exported from the country in question, triggering applicable import and export duties. Accordingly an FSRU contract should establish clearly who is to be responsible for importing and exporting the vessel, the identity of the importer of record, and the tax implications of the import and export. If the owner has to undertake such obligations, the contract should ensure that the charterer is required to participate in the import and export process to the extent requested by owners. In addition, the fact that the vessel will remain in one country for a substantial period of time while rendering FSRU services may create a risk that the owner will have a "permanent establishment" in that country for tax purposes, with the result that the owner will be subject to income tax as a resident company. This may have substantial financial implications for the owner, and the position should obviously be clarified before the contract is entered into.

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