

“Where is the wriggle room for an implied term that a charterer’s parent company guarantee precludes further security, following CVLC Three Carrier Corp and Anor v Arab Maritime Petroleum (2021)?

1. Well may you ask?
2. The scope is so limited as to be non-existent.
3. Award of eminent marine arbitrator in this case one of the most surprising I have seen recently

Facts

4. The claimants each chartered their vessels to the same charterer under identical charterparties. In consideration for the claimants entering into the charterparties, the defendant guaranteed the punctual performance of the charterer's obligations.
5. The claimants terminated the charterparties because of alleged breaches by the charterer.
6. The claimants served notices of arbitration in June 2020 contending they had suffered loss and damage because of the charterer’s breaches and that the defendant was liable under the guarantees.
7. On 31 July 2020, the claimants applied to the Angolan courts for an order detaining a vessel owned by the guarantor as security for its claims under the guarantees. An interim order was granted on 3 August.
8. On 5 August, the guarantor made an expedited application to the arbitrator for a declaration that it was an implied term of the guarantees that the claimants would not seek additional security.

9. The Angolan court made a final order for the arrest of the guarantor's vessel on 11 August.

10. On 13 August, the arbitrator made a first award making the declaration sought by the guarantor. A second award was made on 19 August which declared that the claimants were in breach of the implied terms of the guarantees by arresting the guarantor's vessel.

11. The arbitrator relied upon two distinguishing features of the guarantees:

“Firstly, liabilities under the letters of guarantee could only be triggered if it had been established that the charterer had failed properly to perform the relevant bareboat charterparties.

12. Secondly, although the Guarantor was potentially liable as a primary obligor and not merely as a surety under the letters of guarantee, those letters of guarantee were, at the risk of stating the obvious, both identified and correctly categorised as letters of guarantee that were being provided in consideration of the agreement of the bareboat charterparties.

13. From that he inferred that the Guarantees must have been considered adequate security at the time the Charterparties were formed, because otherwise they would not have been concluded.

14. He then concluded:

“For the Owners to be entitled to enforce the rights under the letters of guarantee, however independent of the bareboat charterparties, would have required both an established failure by [the Owner] to perform their obligations under the bareboat charterparties and an established failure by [the Guarantor] to perform their obligations under the letters of guarantee.”

“I do not think that objectively the parties would have assumed that there would be an entitlement to obtain further security and, conversely, business necessity requires the prohibition on acquiring further security.”

15. So the decision was because owners did not stipulate for further security from guarantor at the time the guarantee was given, it was precluded from exercising any rights to obtain further security afforded to it by any legal system e.g. by arresting the guarantor’s vessel.

Look at Analogy of position between guarantor and lender

16. The surety who has not paid the principal for which he is liable cannot require the creditor to proceed against the principal, or any other co-surety, or against any security for the debt guaranteed, before having recourse to the surety.

17. In China and South Sea Bank Ltd. Appellant v Tan Soon Gin (alias George Tan) Respondent [1990] 1AC 536, the Privy Council stated that:

“The creditor had three sources of repayment. The creditor could sue the debtor, sell the mortgage securities or sue the surety. All these remedies could be exercised at any time or times simultaneously or contemporaneously or successively or not at all

The creditor could choose which of its rights to exercise in which order without reference to the guarantor. The guarantor could not say sue creditor first.

18. Accordingly, it could be said by analogy, that if, by the law of Algeria, the creditor/owner had the right to secure itself by arrest of the guarantor’s ships, why should it not be able to do so unless there was an express stipulation to the contrary in the contract of guarantee.

Cockerill J's judgment

19. The appeal against the arbitrator's award came before Cockerill J

20. Not surprisingly, she reached the clear view that the Arbitrator was not correct

21. The legal hurdle for implication of a term is a high one. The test is of necessity which is just that. As Lord Neuberger said in the Marks and Spencer case:

"A term can only be implied if, without the term, the contract would lack commercial or practical coherence."

Or as the Privy Council said in the Ali case:

"The concept of necessity must not be watered down. Necessity is not established by showing that the contract would be improved by the addition. The fairness or equity of a suggested implied term is an essential but not a sufficient pre-condition for inclusion"

22. The alleged implied term relied upon by the guarantor did not go anywhere near to meeting this test

23. The Judge was also troubled by the fact that if this guarantee contained the implied term by the arbitrator then so would many other guarantees since this was a standard form guarantee. So the freedom of action of many parties in the position of owners would be constrained without there having been an express agreement.

24. The judge also made the telling point that the position only becomes more troubling when one adds into the equation the fact that in normal circumstances a party entering into a contract is not circumscribed as to the steps it can take to secure its claim in the event of an arguable default. See creditor/guarantor relationship above. The implied term in this case is therefore in the nature of an exclusion clause. There is of course a good deal of law which establishes that a court will generally require clear words before it will conclude that a contract has taken away the common law rights or remedies of one of the parties
25. In addition, there were considerable doubts as to whether the arbitrator had applied the correct legal test for the implication of a term.
26. The Judge rightly said that it would make no sense to be able to seek security (e.g. by way of arrest) for the Charterer's breach of its obligation, but not to be able to seek similar security for guarantors breach of their own primary obligation. It may well be rare that the financial position of a guarantor is such that it is considered necessary or worth the time, effort and costs to seek security. But that is a matter entirely separate from legal principle.
27. The Judge was rightly scathing as to the arbitrator's conclusion. At para 74 she said:

*Finally [The Guarantor] relies (at least in writing) on the arbitrator's finding at paragraph 27 of the First Award that "I do not think that objectively the parties would have assumed that there would be an entitlement to further security", saying that he was "perfectly placed and ideally qualified" to make that value judgment. **However while due respect must be given to commercial arbitrators they are not***

generally appointed to impose their value judgments at large on the parties or to rewrite their contracts for them. “

Ouch

She continued

The role of the Arbitrator here was not to do this but to apply the law on implication of terms; and here one can clearly see that the assessment is one which is at odds with the exercise called for when implying a term. In the First Award Mr Hamsber is asking: would the parties assume there would be an entitlement (i.e. should a term for security be implied); rather than the correct question: “would they agree in testily dismissing the suggestion that there should be security?”. In essence he has turned the burden of proof for implication of a term on its head, or treated the question as if the implied term was one for which Owners and not AMPTC were contending.

28. As the Judge pointed out relying on cases such as Moschi v Lep:

An alleged breach, in the sense of an arguable claim, is all that is required to “trigger” the right to make a demand under the contract of guarantee. Such arguable claim triggers the right to commence arbitration, for example; or to obtain a freezing order; or to arrest assets to found security. None of these rights is dependent upon finally proving the breach. While the question of whether that demand (or that application for a freezing order) was correctly made will only be ascertained later that does not affect the right to make a demand once there is an arguable breach.

“the creditor's cause of action against the guarantor arises at the moment of the debtor's default” Moschi v Lep [1973] AC 331 at 348 per Lord Diplock

29. In addition, as the Owners note, it is hard to see why it would be the case that they can arrest the Charterer's vessels, but they cannot arrest the guarantor's vessels under a distinct contract "as primary obligor" (which is how they are stated to be under the Guarantees).

30. The Court saw no point in remitting the question to the arbitrator as the answer was so obvious. The arbitrator was wrong and there was no implied term barring owners seeking security from the guarantor

Conclusion

31. This is pretty obvious.

32. Forget about trying to argue that there is an implied term that a charterer's parent company guarantee precludes further security.

33. Stipulate for an express term or take the consequences.