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CHINA DELAYS AUSTRALIAN COAL CARGOES AND THE RIPPLE EFFECT ON ENERGY COMMODITIES SUCH AS LNG

Written by Damon Thompson, Calum Cheyne, Lucy Noble & Zach Barger

CHINESE-AUSTRALIAN RELATIONS

Throughout 2020, the world scrutinised as diplomatic relations between China and Australia progressively soured. Predictably, these tensions quickly manifested in trade by swiftly fracturing established dynamics and forcing realignment of supply chains. Repercussions have been felt within wider international energy commodity markets as well.

The unofficial ban of Australian coal imports is one of the more recent developments to come from Beijing. This ban was the latest escalation in a string of refusals and increased tariff restrictions concerning imports of Australian goods, including beef, wine, barley, rock lobster, and cotton. Coal is one of Australia's largest and most valuable exports with an export value to China of reportedly AUD \$14 billion per year. Likewise, China's chief supply of coal conventionally originates from Australia, ensuring a high degree of interdependence.

THE CHINESE BAN ON COAL

The effect of this unofficial ban was immediate and largely

unexpected. Chinese port authorities denied prescheduled Australian coal shipments from discharging. This left vessels, seafarers, and paid-for cargoes stranded in limbo off the Chinese coastline. Due to the unofficial nature of the ban, even as vessels were being denied discharge in China, cargoes of coal continued to be loaded in Australian ports. According to reports, an estimated 70 vessels carrying approximately 8.1 million tonnes of coking and thermal coal remained anchored for substantial durations as cargo interests scrambled to secure alternate buyers.

The effect of this event is widespread. We are currently advising a number of clients on two primary areas of interest. Our first primary area of interest has been advising on difficulties arising in China specifically because of the delays. [Luke Zadkovich](#) and [Calum Cheyne](#) are handling a number of disputes, including with fast-tracked arbitration, arising out of these delays. We have advised market participants in relation to both shipping and trading disputes and considered the knock-on effects of a declaration of frustration on vessel owners, cargo receivers, and the subject cargo itself. These issues are fraught with legal risk, and we intend to publish follow-up material on this topic shortly.

The second primary area of interest, and the focus of today's bulletin, is price volatility across the energy commodity markets generally. [Damon Thompson](#) spearheads our LNG team and has been active in advising clients on these areas. We discuss whether, from a contractual perspective, parties can benefit from the spikes in commodity prices and freight rates. Next, we turn to contractual regimes that can be used in long-term sale and purchase agreements (“SPA”), particularly in the LNG sector, to optimise a trading portfolio. Finally, from an admiralty perspective, we consider whether owners can “wriggle out” of chartering commitments to take advantage of spikes in the freight market.

PRICE VOLATILITY

The Australian coal ban cast doubt on China's energy supply chains. As news of the stranded vessels spread, markets reacted. Owners of the coal shipments probed to find buyers, and Chinese coal importers searched to secure comparable products from alternative supply chains. This caused international commodity prices to skyrocket in some instances. The uncertainty was amplified further as standard international coal production levels slowed over the duration of 2020 due to limitations from the coronavirus pandemic. Accordingly, China has been forced to pay premium prices for replacement coal and other energy commodities at the height of supplier consumption.

These price spikes were immediately felt within the industry of Australia's largest export, iron ore (of which China is a near majority buyer). Prices rose to levels high enough to claw back some of the losses felt within the coal sector. This increase, due in part to market fears that China would take consequent and comparable action against Australian iron ore, resulted from a surge in Chinese buying. More recently however, attention turned to the headline-grabbing high trading and shipping prices in the LNG sector.

THE LNG SPOT MARKET

In the LNG spot market, characterised by short term, high pressure sales contracts and corresponding single-voyage charterparties, prices surged. Markets are regularly impacted by seasonality, and this was exacerbated by current circumstances with China and northern Asia experiencing a mid-winter freeze. Additionally, the continuing bilateral tensions ensure that supply chains remain uncertain. Reportedly, LNG prices rose to around USD \$30 per mmbtu (even \$40 per mmbtu if some market rumours are to be believed),

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and spot charter rates into Asia were up to around USD \$350,000 per day.

LNG traders worked hard to optimise their volumes. The situation demonstrates the importance of negotiating flexibility into SPAs. It is reported that the majors with most volumes were the entities that were best placed to take advantage of the price spikes. That makes sense because the majors will, mostly, enjoy flexibility as to where their volumes are committed that trading houses do not. The lesson here is to negotiate as much flexibility as possible into an SPA. Long-term SPAs on DES terms generally stipulate well in advance the number of cargoes in a contract year and the destinations for those cargoes. There will often be some flexibility for the buyer as to a range of prescribed receiving terminals to which it can send the cargoes. As this LNG price spike demonstrates, it would also be sensible for a buyer to negotiate further flexibility to send the cargoes to other receiving terminals worldwide. There are various contractual mechanisms which can be adopted to achieve this and, of course, much will depend on the negotiating positions of the respective parties. Typically, a seller and buyer will share upside on cargoes diverted from their original destination. For example, in addition to the contract price for a cargo, the buyer will also pay the seller 50% of the net proceeds. Therefore, it can be in the interests of both parties to include this kind of a mechanism. Both the seller and buyer (and their respective lawyers) need to draft this type of clause carefully to ensure each party's requisite interests are fully protected.

If a seller does not have such flexibility, it may be tempted to default under a SPA and suffer the consequences pursuant to the failure to deliver regime under that SPA to take advantage of a substantial price increase. Often in LNG SPAs, a seller's liability for failure to deliver is capped at a certain level (e.g., 50% of the shortfall quantity x the SPA Contract

Price). That cap might be significantly less than the upside of selling to a different buyer in a volatile market. Of course, to do so is likely to test the commercial relationship between the parties and will do nothing for the seller's reputation in the market. Nonetheless, a seller may consider it worth it!

Traders may also look to the price-review provision to see if such volatility triggers an adjustment. Of course, this depends on the wording of the specific clause, but a price-review right is often activated by an average price increase over a longer period. But note that it may be foolhardy to invoke a price review clause based on such a spike, as a contracting party is typically only entitled to one review option for the life of a long-term contract.

For a more in depth investigation into price review clauses, please see the article "[The Only Constant is Change: Parameters of Price Review and Other Contract Adjustment Disputes in the Energy Sector](#)" below.

LNG SHIPPING ISSUES

LNG freight traders often have less flexibility in their charterparties. Most carriers are already tied into term charterparties for the winter months.

While it may be tempting for an owner to seek early redelivery, this would likely represent a breach of the owner's obligations to follow its charterer's instructions. An engineered early redelivery (without consent) would be likely to amount to a repudiation of the charterparty. The damages for such an approach would be significant: mirroring the market rate that charterers would pay to enter a substitute fixture. This would effectively wipe out any benefit to the owner in being able to take advantage of that same market rate. Such action would also severely damage an owner's

reputation.

A separate question arises as to whether an owner could choose to miss the prescribed laycan in a charterparty that was already fixed at a lower rate. Typically, a charterparty provides a "cancelling date." Failure to deliver by this date is not usually a breach but entitles a charterer to cancel the fixture. Where there is a cancelling date, there is instead an implied obligation on an owner to use due diligence to meet said date, but proving failure to use due diligence to meet a cancelling date is a harder task than simply showing that the vessel was not delivered on time.

The position as described above is the case in the Shelltime 4 standard form, on which the LNG industry standard form charterparties are largely based (see, Clause 5):

The vessel shall not be delivered to Charterers before [DATE] and Charterers shall have the option of cancelling this charter if the vessel is not ready and at their disposal on or before [DATE]

This is a classic cancelling provision. There is no strict obligation on the owner to deliver by a certain date, but a cancelling option will accrue to the charterer if the owner does not.

However, the ShellLNGTime 1 form puts a more onerous obligation on the owner. The charterer retains its option to cancel if the vessel is late, but the requirement to deliver within the lay days is upgraded to a term of the charterparty (see our emphasis below):

*Unless otherwise agreed, the Vessel shall not be delivered to Charterers before _____hrs local time [DATE] but **must be delivered to Charterers no later than _____hrs local***

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time [DATE]. Charterers shall have the option of cancelling this charter if the Vessel is not ready and at their disposal during this period.

This also appears to be the case in ShellLNGTime 2. Part I of that form includes a box for "Laydays/Cancelling". That box then includes an obligation as follows (our emphasis):

The Vessel shall be delivered to Charterers no later than: [DATE]

It could be argued that this is intended to merely clarify the cancelling date, particularly with reference to the label provided for the box containing this obligation. However, an alternative view is that the plain wording of this provision is actually an obligation to deliver by a fixed date. It is certainly arguable that the wording differs from the Shelltime4 wording, said change was made deliberately, and that it should be given effect.

This distinction between Shelltime 4 and ShellLNGTime is significant. If it can be argued that the ShellLNGtime form imposes a hard obligation on owners to deliver within laycan, then when an owner misses the laycan, that is a breach of the charterparty terms, and the charterer may claim damages. In the current volatile market conditions, that could result in a sizeable claim, where a replacement fixture and the knock-on costs of the missed delivery window are likely to be significant.

Charterers should also note that if an owner fails to deliver within the delivery window, the owner remains required to deliver the vessel with reasonable despatch. This obligation survives the missed delivery window unless the charterparty is cancelled.

As a matter of good practice, any cancellation or termi-

nation rights should be exercised with the utmost care. A wrongful cancellation or termination is likely both a breach of the charterparty and sufficient grounds for the other party to terminate (possibly relieving that party of the burden of performing at far below market rate).

CONCLUSION

The current unpredictability and corresponding price volatility that the LNG and wider energy commodity markets are experiencing highlights the overwhelming importance of well-drafted and flexible energy trading contracts. While it is unclear how long this market uncertainty will extend, what is clear is that contracting parties should be looking to the provisions of their agreements when weighing up a proposed cause of action so as not to incur liabilities equal or greater than the potential profits they seek to gain. As 2021 progresses, all eyes will be on China to see whether the unofficial coal ban will remain in force and whether the next step will be the targeting of additional energy commodity imports.

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Additional content on this topic:



VIDEO Length 6 Min.

Commodity Arbitration

Luke Zadkovich LONDON

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U.S. OFFSHORE WIND

Written by Nicholas Paine

The U.S. offshore wind industry is poised for substantial growth in the next decade, with numerous projects in the pipeline for federal approval to begin construction. The construction phase for each project will involve numerous agreements, between project leads, general contractors and their subcontractors, as well as land-based equipment and material suppliers. From a maritime perspective, recent regulatory developments under U.S. law, and the operational limitations of the U.S.-flagged fleet, are likely to necessitate the use of vessels from both Europe and the United States for the installation of many these projects.

With the interaction of European and American commercial entities for these U.S.-based offshore wind projects, and the application of State, Federal, and Maritime Laws, at minimum, to those entities and contracts at various levels of the "chain of contracts", it is important from a cost-efficiency



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and risk-reduction standpoint to maintain a clearly delineated “contract interpretation regime.” That is, the contractual terms and applicable law affecting the interpretation of the contract, including jurisdictional limitations, choice of law provisions, and dispute resolution clauses, and the interplay of each within the several contracts making up the chain, and even agreements peripheral to the chain (i.e. insurance agreements), must be made as orderly and congruent with one another as possible to facilitate the overall efficiency of the negotiating process, and most importantly, to avoid costly litigation in the event that litigation arises. As to the latter, litigation costs often balloon arguing over choice of law and proper venue, not only where the entities to the litigation span different jurisdictional limitations (i.e. Europe vs. U.S.) but also where multiple agreements to a dispute have conflicting terms (i.e. a dispute resolution clause calling for London arbitration in one contract and New York state courts in the other).

To that end and to the extent possible, creating an outline or chart of the “contract interpretation regime” that delineates anticipated jurisdictional limitations, preferred venues for dispute, insurance coverage limitations, and other relevant considerations will help to realize cost-saving and risk-reduction goals by:

(1) informing all parties in the chain as to where they likely fit in the regime, legally and contractually; and

(2) ensuring the end result is a more consistent and congruent delineation of the proper interpretations of the agreement or agreements should a dispute arise, and what venue should be tasked with resolving the dispute.

Of course, providing such information early on in any contract negotiation must conform to any applicable confidentiality clause as well. Moreover, even with a such regime

outline presumably prepared by a project lead or general contractor, due consideration of subcontractors’ counter-proposals should always be considered as these subcontractors (especially in the case of U.S.-vessel operators negotiating with a European entity) may be more familiar with the unique legal considerations applicable to their specialties, and can help to recalibrate the delineations in the regime outline. This is especially true as it relates to each individual entity’s respective insurance coverage requirements and preferred dispute resolution venue.

While it goes without saying that such preferences as to the terms that make up these so-described “contract interpretation regime” takes place in one-on-one negotiations, clarity of such limitations and considerations is not always provided throughout the negotiation process with all levels of the chain, especially when there is merely a “best efforts for sub-contractors to comply” clause in the overarching construction agreement.

Thus it is preferable, to borrow a phrase, “to have a clear plan from which to deviate,” in the opinion of this author, than to fully renegotiate the choice of law and dispute resolution terms at each phase of the contract negotiations resulting in potentially conflicting impacts on inter- and intra-contract interpretation that could be costly in the long run. While the ability to be so transparent at the outset is not without limitations, such an effort at transparency may be rewarded by less litigation costs and higher insurance premiums in the long run.

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THE ONLY CONSTANT IS CHANGE: PARAMETERS OF PRICE REVIEW AND OTHER CONTRACT ADJUSTMENT DISPUTES IN THE ENERGY SECTOR

Written by Lisa Beisteiner

PAST AND PRESENT OF PRICING DISPUTES

Arbitration has played and continues to play an important role in keeping contract prices and conditions in long term contracts aligned with changing market conditions. In particular, price review arbitration has long become an established discipline, at least in Europe: prices or price formulas in long term (often gas supply) contracts are revised *qua* arbitration proceedings. After three waves of natural gas price reviews essentially triggered by the infamous decoupling of oil and gas prices, many contracts have now transitioned from oil price indexation to hub indexation with the help of international arbitration. The focus of gas price revisions has shifted to Asia, where history largely repeats itself.

But even in Europe, work remains to be done: despite a market shift towards short term contracts and hub indexation, a fair number of legacy contracts are still long term and – at least partially – oil indexed. In particular, the further one moves East, the less mature natural gas markets

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are and the less liquid the regional hubs. But markets are maturing, and regional hubs are becoming more liquid, prompting desires to move the contractual hub indexation away from proxy hubs such as the TTF, towards regional hubs which are perceived as sending more relevant pricing signals (e.g. CEGH). Also, whilst traditionally pipeline gas was at the centre of review disputes, the focus of price reviews shifts towards the pricing regime in LNG supply contracts (see our article “[Australian Coal Cargoes and the Ripple Effect on Energy Commodities such as LNG](#)” above). Beyond the realm of classical price review disputes, arbitration plays a significant role in the energy sector in adjusting long term contract conditions more generally (i.e. not only prices or price formulas) to changing circumstances, as e.g. in view of changed regulatory frameworks, financial and other crises, technological revolutions etc.

COMMON PRACTICES

Disputes concerning the review and adjustment of contracts exhibit certain common features, which set them apart from the classical commercial disputes which arbitration has traditionally dealt with.

- Fundamentally, rather than deciding on the consequences of a legal wrong (most frequently by ordering payment or specific performance following a breach of contract), the arbitrators’ task is to adjust a typically long-term contract to changed circumstances: arbitrators need to find a **commercially sustainable solution** so that the long-term relationship can be continued. What is more, they are tasked with finding a commercial solution where the parties themselves have failed to find one (or at least: failed to agree thereupon). This role of adjusting contracts is now well-established in most developed jurisdictions (it may however still be controversial in others, raising ques-

tions as to the nature of arbitration as a method of resolving legal disputes).

- Needless to say, an adaptation of contract conditions which is imposed upon the parties after a lengthy legal process will regularly be the second-best option only. A mutually agreed adjustment will typically be preferable. Accordingly, parties to long term contracts regularly foresee a **mandatory pre-arbitral negotiation period**, kicked off by a formal notice of the respective contract revision request. Agreeing on a contractual (price) adjustment - on how to share the pain of a changed contract environment - however, also involves assuming responsibility for the negotiated outcome. At times, parties may not want that but rather prefer to delegate such responsibility to a panel of arbitrators. If their ultimate decision is not convenient, it is the litigation risk which has materialized.
- Price review arbitrations – but also contract adjustment cases more generally – will invariably turn on the interpretation of **vague contractual language**. There is a wide range of different contractual adjustment clauses, responding to a variety of different purposes. Even price review clauses, a subset of contract adjustment clauses, will vary greatly when it comes to the detailed language used. Structurally, these clauses mostly follow the pattern of (1) defining conditions “triggering” an adjustment, (2) setting out the adjustment criteria and, last, (3) stipulating the adjustment procedure. Not infrequently, the dispute will boil down to the interpretation of one single contractual clause, or even of one specific passage or term within that clause: e.g. it might be disputed what meaning is to be attributed to “significant” (or “substantial”, or “fundamental”), when it comes to a change of a certain quality in the relevant market or other relevant circumstances; what exactly are the “relevant economic circumstances” which must change; when a change is not only

“temporary”; what is “commercially reasonable”; what is “prevailing” on the market; what is “appropriate”; when conditions do “reflect” a certain development; what is the “market value”; what is the “relevant market”, in terms of substantive, geographical and temporal scope; etc. It may be at issue which contracts do qualify as “comparable contracts” which might yield relevant data points for determining the market price. In this regard, the parties may fiercely debate the relevance of the respective contract duration (e.g. spot prices or prices in long-term contracts), of certain contract conditions (e.g. pipeline gas vs LNG; physical storage capacity vs other forms of flexibility etc), of the date of contract conclusion and execution/delivery, of the geographical region, etc. Whilst price review clauses will often provide a more or less specific recipe based on which the contract price is to be adjusted, a general contract adaptation clause may likely just succinctly state that “the contract” be adjusted “fairly” or “accordingly”.

- Intricate questions of legal doctrine aside [as e.g. regarding the “enforceability” of general adaptation clauses, or the ambit and workings of legal instruments such as hardship, change of circumstances etc], the above examples of potential interpretational questions make one thing clear: often the subtle nuances of the legal rules on contract interpretation proffered by the governing law will take a back seat. Instead, the **actual economics of the case** and a thorough and wholistic understanding of the **contractual allocation of risks** and opportunities in that specific contract will take centre stage. Indeed, when interpreting general contractual terms, arbitrators very often charter rough territory at the interface of legal terms and economic concepts, ideally equipped with comprehensive industry knowledge and a sound business judgement. Legal and expert questions often blend into *questiones mixtae* when determining the meaning of general contractual terms (as in: what is a “reasonable mar-



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gin” or an “appropriate adjustment”?).

In general, **identifying the right arbitrator** is sometimes characterized as the single most important decision a party can make in an arbitration. This decision gains even more strategic weight when it comes to price or contract adjustment cases. Whilst there may effectively only be fractions of Eurocents (or another applicable currency) between the opposing parties’ positions, the commercial importance of these disputes is typically huge: even a relatively minor change in the contract price, when multiplied by the large volumes to be delivered/provided over several years, may have a significant financial impact. The ideal arbitrator must be eager to grasp the commercial bargain struck by the parties, to thoroughly understand the risk allocation embedded in the contract. Additionally, they must be pragmatic enough to step in and extrapolate that bargain to changed circumstances – in other words: interfere with the contract terms to re-establish the envisaged risk allocation. In this exercise of interfering with the contract terms – most importantly: the pricing mechanism – in light of external changes, arbitrators will of course heavily rely on expert evidence.

As is well established in most jurisdictions, arbitrators must not award relief other than or beyond what was requested by the parties (**ultra or even extra petita**). If a prayer for relief is not for payment or for declaratory relief but for contract adjustment, delineating what is a “minus” as compared to what was requested (and hence admissible), and what, conversely, is an “aliud”, i.e. something different from the parties’ requests (and thus inadmissible), may become tricky. This may be particularly so where the contract adjustment ultimately granted does not precisely match the letter of the adjustment request. In this regard, it may also be doubtful whether tribunals need to guide parties to adjust (the specific formulations

employed in) their prayers for relief. Typically, these questions will have to be analysed under the law of the arbitral seat – the *lex loci arbitri*. Some arbitrators may adopt a more pragmatic and flexible approach towards such dogmatic question than others.

Specific questions also flow from the **recurring nature of price review disputes**: typically, price review clauses allow parties to periodically (e.g. every three years) request a review of the contract price formula to ascertain whether it should be adjusted in response to changes in the market; “wildcard” price re-openings may be available on top of these revision cycles. As a consequence, one and the same contract may well be subject to several revisions during its lifetime, all based on one and the same price review clause. In this case, arbitrators will have to resolve on the – legal or practical – effect of a previous arbitral award answering the identical interpretational question. A prior award between the same parties deciding which meaning is to be given to disputed key terms of the adjustment clause, reached on the basis of a comprehensive evaluation of expert evidence, may be considered to have – at least – persuasive force. Beyond that, depending on the applicable law, such ruling may even be considered as a legally binding determination barring the parties from re-litigating the same interpretational issue. Indeed, the applicable law may make much of a difference in this regard: this concerns the different nuances of the civil law doctrine of *res judicata* – which may afford binding effect to such determination even if made outside the operative part of the award – just as the differently shaded common law doctrines of estoppel, such as collateral estoppel in the US or issue estoppel in the UK.

CONCLUSION

In conclusion, arbitration has, by and large, worked well to see many contracts through changing times, in particular in the energy sector and in particular when it comes to price adjustments. It will come as little surprise that a diligent choice of arbitrators may be as important as, earlier on, a clever selection of the seat of arbitration, determining the *lex loci arbitri* and thus informing many of the procedural issues arising in review and adjustment cases.

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SEPTO TRADING INC V TINTRADE LTD (THE "NOUNOU")

QBD (Comm Ct) (Teare J) [2020] EWHC 1795 (Comm) – 8 July 2020

Written by Calum Cheyne & Charlotte Larkinson (law clerk)



Under a contract of sale, the rights of the parties to bring or defend a claim that the goods are not of the quality described must be closely balanced. The buyer will not wish to be bound by the results of an early survey, certainly not one undertaken prior to the sale. The seller, to the contrary, will not wish to be faced with evidence of cargo damage taken after the buyer had possession of the cargo. These competing objectives are often closely fought.

A recent case gives guidance on how these competing positions interplay in the sale of fuel oil.

THE CLAUSES

The clause in the Recap was titled: *"Determination of Quality and Quantity"*:

"As ascertained at loadport by mutually acceptable first class independent inspector, or as ascertained by loadport authorities and witnessed by first class independent inspector (as per local practice at time of loading).

Such result to be binding on parties save fraud or manifest error.

Inspection costs to be shared 50/50 between Buyer/Seller."

The clause entitled "General" provided:

"Where not in conflict with the above, BP 2007 General Terms and Conditions for fob sales to apply."

The BP terms provided:

"1.2.1 Provided always the certificates of quantity and quality ... of the Product comprising the shipment are issued in accordance with sections 1.2.2 or 1.2.3 below then they shall, except in cases of manifest error or fraud, be conclusive and binding on both parties for invoicing purposes and the Buyer shall be obliged to make payment in full in accordance with Section 30.1 but without prejudice to the rights of either party to make any claim pursuant to Section 26.

..."

THE DISPUTE

This case concerned a cargo of fuel oil loaded at Ventspils in Latvia in July 2018. The buyer claimed damages arising from off-spec cargo.

Ventspils was nominated as the loading port, and the buyer

instructed SGS, as surveyors, to perform quantity and quality determinations of the fuel oil.

The cargo was then shipped to Gibraltar, where a certificate of analysis issued by local surveyors showed that the cargo fell outside the contractual specification. Further samples collected by SGS prior to and during the loading were subsequently re-tested, to mixed results. While most samples were within specification, a number of the samples showed that the cargo was off-spec.

Buyers claimed USD7,785,478 in damages.

THE DECISION

The key issue was whether the parties had contractually agreed for the load port Certificate of Quality to be binding, and the extent to which it was binding. It was clear from the contract that it was binding for the purposes of invoicing, but less clear whether it was additionally binding on the parties against future claims.

The position in the Recap appeared to broadly and in general terms bind the parties to the load port analyses. Clause 1.2.1 of the BP terms, by contrast, was more nuanced and only appeared to relate to invoicing.

The Court held that Clause 1.2.1 of the BP terms could be read in conjunction with the Recap. Neither replaced the other, and neither stood alone. The BP terms qualified and coloured the general position under the Recap, by highlighting that the 'binding' nature of the loadport surveys was only limited to questions of invoicing. The Court could, and should, give effect to both clauses.



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ZFZ COMMENT

In the commodities and shipping industries it is routine for agreements to be made by recap, with a back end document providing additional and general terms. Competing interpretations of the interrelationship between those terms, particularly where there appears to be a conflict between the two, can lead to wildly different results.

Conceived wisdom is often that the recap prevails. This case shows that the Court will apply nuance and strive to give effect to all of the terms of the agreement. It also underscores the importance that the parties should attach to ensuring that their main terms agreed in the recap sit well together with any standard terms incorporated into the recap. Although in *The Nounou* the Court eventually sided with the Sellers (whose position appeared to be more in line with the parties' apparent intention) and rejected quite opportunistic arguments of the Buyers, this was only after the parties spent many thousand pounds in costs litigating the issue. Since similar interpretation disputes may be avoided by more careful drafting, market participants should therefore continue to take care of all of the terms they are agreeing to, not simply the main terms contained in the recap.

For additional information and queries, please contact calum.cheyne@zeilerfloyd.com

MEXICO: NEW RULES ON IMPORT / EXPORT PERMITS OF HYDROCARBONS AND OIL PRODUCTS - WINDING BACK THE 2013 ENERGY REFORM & AMPARO PROCEEDINGS

Written by Andrea de la Brena

On 26 December 2020, Mexico's Ministry of Energy (SENER) published a resolution in the Mexican Official Gazette introducing, inter alia, new rules restricting permits for the import and export of hydrocarbons, oil, and petrochemical products (the "2020 Resolution"). The resolution entered into force two days after its publication. These new rules substitute, and will eventually replace the rules on this topic, set out in the resolution dated 29 December 2014 (the "2014 Resolution").

BACKGROUND

In December 2013, the Mexican energy framework suffered a major reform ("2013 Reform"). Prior to the 2013 Reform, PEMEX (the national oil company) was the only company operating in Mexico's oil market. However, the Mexican oil market was struggling due to decreasing oil production and reserves, a growing energy demand, oil consumption, and a lack of investment in the industry (Iglesias and Felipe,

p.3; see also Assad, p. 3). A similar scenario applied to the generation of electric power and its delivery to end users, through CFE (national electricity company) monopolistic regime.

Therefore, the 2013 Reform was passed to improve this market situation, allowing the government to maintain sovereignty over hydrocarbon resources and electricity, while simultaneously ensuring greater private investment through production-sharing, profit-sharing and licensing mechanisms. These mechanisms include, in particular; import and export permits on hydrocarbons, oil, and petrochemicals. Private oil companies increasingly started to import and export oil, causing PEMEX's decline in their dominant market position. As a result of the situation, in a memorandum dated July 2020, the President, expressed his intentions to strengthen PEMEX and CFE to reverse the effects of the energy reform (see our article "[Mexican Governmental Recent Measures in the Private Renewable Energy Industry](#)"). Therefore, the 2020 Resolution appears to be a step forward in this direction, due to the restrictions introduced.

NOTABLE CHANGES

Title II of the 2020 Resolution revisits the list of products where import and export activities are subject to regulation by SENER, and amends the existing regulation related to the permits needed to perform such activities. Article 28 explicitly sets out SENER's mandate to protect the states sovereignty in the energy market by securing a balance between the national production of energy and the imports. To restore this balance, the 2020 Resolutions introduced the following notable changes:

- Additional requirements.** Applicants must comply with new general requirements to apply for a permit. For in-



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stance, they must provide information regarding; the final destination of the products, the relationship with the main clients (including contracts, invoices and letters of intent), monthly projections of the products' cost of entry into the country and the volume to be imported during the term of the permit. For long term permits, the applicant must additionally demonstrate contractual commitments from potential customers for at least a five-year term and must evidence they have (or will have) storage and transportation means for the products.

- Permit terms.** The maximum initial term for long term permits was reduced from 20 to 5 years, with the possibility of a one-time extension up to the same term. The one-year permits may be extended by two, instead of three, additional periods of equal length. SENER must perform an analysis of the circumstances of the case at stake prior to extending the permit term.
- Implied negative reply.** Contrary to the 2014 Regulation, if SENER fails to issue a resolution within the statutory term (12 business days), the application shall be deemed rejected.
- SENER's new powers.** If the applicant fails to justify the need for the requested volume, SENER may grant the applicable permit with the volume that it considers appropriate. SENER may also consult state-owned companies (PEMEX and CFE) to determine the convenience of granting the permits. Furthermore, SENER may declare the expiration of a permit, in the absence of transactions for a consecutive period of 30 calendar days for 1-year permits or 365 calendar days for 5-year permits.
- Revocation grounds expanded.** Two additional revocation grounds were introduced: (i) failure to inform SENER of changes in the company's corporate structure; and (ii) notice by the Tax Administration Service to SENER on the non-existence or inaccuracy of the company's name and tax address.
- New products subject to permits.** The list of products

now includes, among others: undenatured ethyl alcohol with an alcoholic strength greater than or equal to 80% by volume; ethyl alcohol; and benzene.

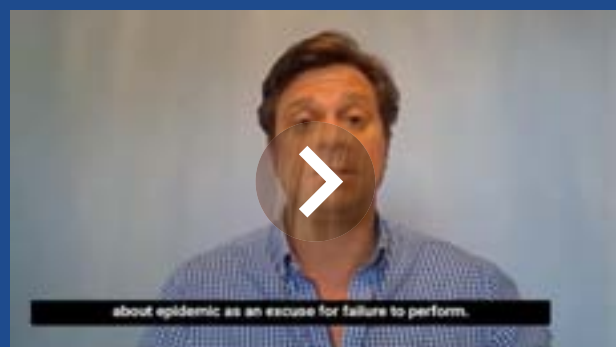
The permits granted prior to the 2020 Resolution's entry into force shall remain valid until the conclusion of their term and will be governed by the 2014 Resolution (as amended in 2015, 2017 and 2018). Similarly, the permit applications or extension requests, submitted prior to the date of the 2020 Resolution's entry into force, shall be reviewed until their conclusion, in accordance with the former regime.

FINAL REMARKS

The new rules are expected to disincentivize private investment in the energy sector. In a regulatory impact analysis, performed by the Ministry of Economy and SENER, it was concluded that the changes could have a "material impact" on the market. A party considering that their rights are affected by the new rules' entry into force, may seek redress under the Amparo Law (Ley de Amparo), within a 30 business day period from the day of their publication, in the Official Gazette (Articles 107(1) and 17(1) Amparo Law). The basis on which affected parties may seek the protection of federal courts must be analyzed on a case-by-case basis.

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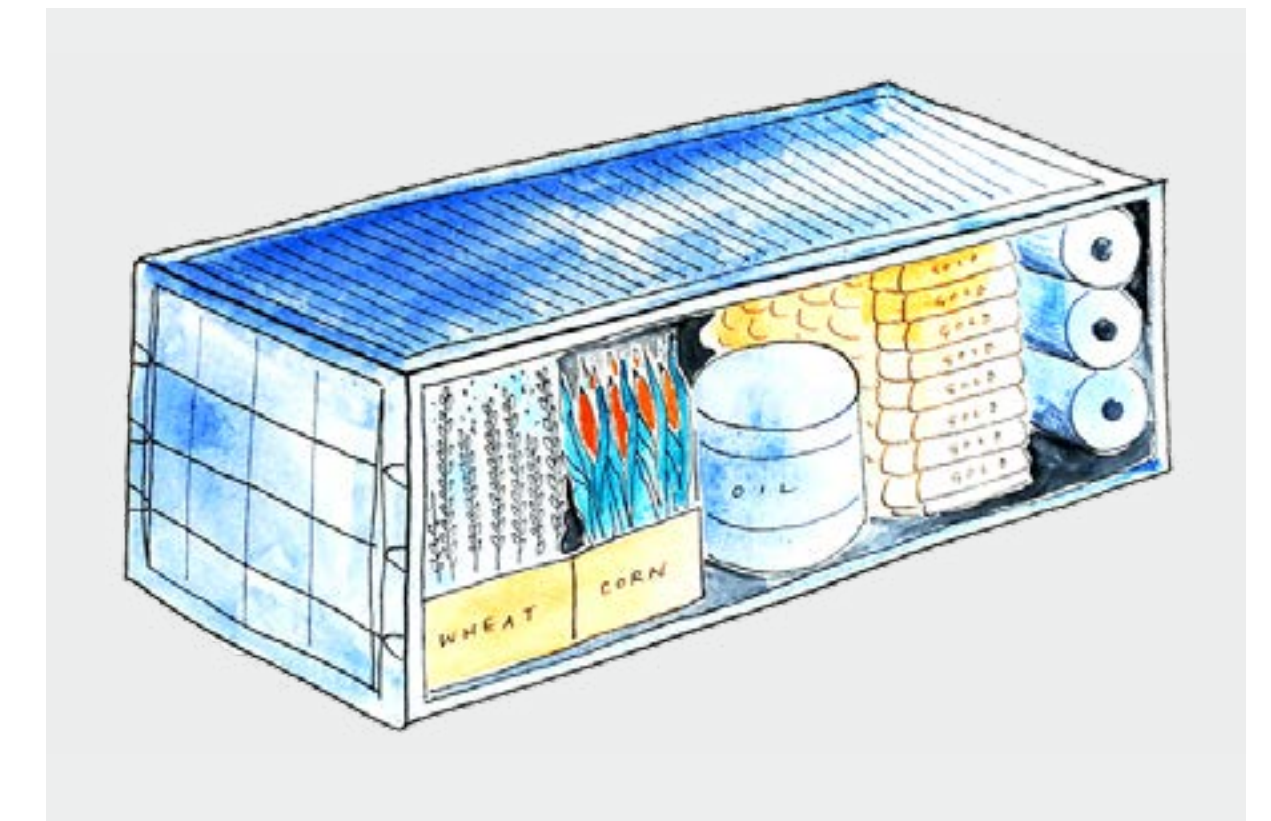
Additional content on this topic:



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Contract Review: Levers and Measures

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ENGLISH COURT: USING THE TORT OF DECEIT TO HOLD DIRECTORS PERSONALLY LIABLE FOR FALSE STATEMENTS MADE IN CONTRACTUAL NEGOTIATIONS

Written by Luke Zadkovich & Aiden Lerch

In May 2020, a team comprising of Luke Zadkovich, Aiden Lerch, Shannen Trout and Calum Cheyne from our firm acted for the successful Claimant in this matter. The claim involved deceit and negligent misstatement allegations before the High Court of Justice in England. The case focused on the circumstances in which a director of a company can

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be held personally liable for committing the tort of deceit when making false statements in contractual negotiations. The tort is extremely difficult to make out, as it must be proven that the defendant knowingly or recklessly made a false statement and intended that it should be acted upon by another, who suffers damage as a result. The finding that the Defendant had committed the tort of deceit in this case therefore proved a big win for the Claimant.

BACKGROUND TO THE CASE

The case was brought against the owner of two companies, along with the companies themselves. The Claimant was a soft-commodities trader and completed a number of small-sale contracts with one of the Defendant companies for the purchase of various seeds and grains over a number of months. In light of these reliable business dealings, the Claimant and that Defendant agreed five further, larger value contracts with pre-payment to be made before delivery of the goods. The Claimant alleged that these latter contracts were made on the back of the following five representations made by the individual Defendant (i.e. the owner of the Defendant companies):

1. That the goods that would be used to fulfil the contracts were already paid for and acquired;
2. That the goods in question were sitting in the warehouse of the other corporate Defendant and were ready to be shipped as soon as the contracts were signed;
3. That, accordingly, the owner of the Defendant companies believed that there was no risk of failure to deliver the proposed cargoes;
4. That the individual Defendant was a man of considerable wealth, owning various assets; and
5. That the individual Defendant intended his company to perform its obligations under the contracts.

Upon signing the five larger contracts, and making payment to the Defendant company, the Claimant contracted to sell the goods to a third party. Importantly, under that contract, delivery was to take place in August/September 2017, only two months after the negotiations between the Claimant and Defendants had taken place. The Defendant failed to deliver the goods in respect of four out of the five of its contracts. Despite this, the Defendant Owner of the companies stated on numerous occasions that the goods were forthcoming. He later failed to respond to any of the Claimant’s demands and withdrew from all forms of communication. As a result, the Claimant was unable to meet its contractual obligations with the third party purchaser and was forced to enter into a settlement agreement.

The Claimant subsequently commenced arbitration proceedings against the Defendants. Judgment was given in the Claimant’s favour and the corporate Defendant was ordered to pay EUR 1,298,928 plus interest and costs. However, the Tribunal found that the company’s owner, and the other corporate Defendant were not liable in the circumstances, and therefore the award was only enforceable against the corporate Defendant that was the Claimant’s contractual counter-party.

Applying a creative approach, the Claimant brought a claim for deceit against the other Defendants in the Queen’s Bench Division, England. If successful, such a finding of liability would enable the Claimant to enforce its claim against all Defendants.

THE LEGAL ISSUES AND THE FINDINGS OF THE COURT

Foxton J summarised the issues in contest as follows:

1. Whether the representations were knowingly made by the Defendant company owner; were false at that time; and were relied upon by the Claimant; and
2. On behalf of which Defendants had the owner made the representations.

As to the first issue, Foxton J was satisfied that Representations 1 and 2 were made. Additionally, those representations were found to be untrue when they were made, with actual knowledge that this was the case. The Defendant company owner was found to have overstated the ability of the other Defendant to ship the cargoes immediately, by expressly stating that they were sitting in a warehouse of the other Defendant and that the cargoes were ready to be shipped. His Lordship found that this statement was clearly untrue, as the goods were never delivered even after a period of 6 months. It followed that these representations were made to induce the Claimant to enter into the contracts, as the Claimant was particularly interested in obtaining quick delivery, which was why it had entered into a contract with the third party purchaser to deliver the identical goods only two months later.

As to the second issue, Foxton J found that when the Defendant company owner made the false representations, he made them on behalf of the entity with the contract with the Claimant. However, the fact that a director of a company makes a false misrepresentation on behalf of that company is no defence to a claim in deceit: *Standard Chartered Bank v Pakistan National Shipping Corpn (Nos 2 and 4)* [2002] UKHL 43, [20]-[28]. Thus, the Defendant company owner was held to be liable in his personal capacity for committing the tort of deceit.

Despite this finding, Foxton J did not accept that he was also acting in the capacity as agent for the other Defendant company. Although this company was named as the supplier in

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the contracts, and although the Defendant company owner had mentioned that he was the owner of this entity during the negotiations, there were never any previous direct dealings between the Claimant and the other Defendant company. Therefore, in Foxton J's view, when the negotiations for the relevant contract took place, this entity was in the periphery of the minds of the parties. His Lordship further observed that it was perfectly open for the individual Defendant to make statements of fact as to the position of a company he owned, without those statements being made by him as a representative of that company. Given the contractual arrangements and the previous dealings between the parties, on the evidence this was the most likely situation.

JUDGMENT AND RECOVERY

After making the above findings, Foxton J entered judgment in favour of the Claimant. The individual company owner was found to have committed the tort of deceit. As a result, the Claimant was awarded damages not only for the prepayments it had made under the contracts, but also for the liability it incurred to the third party purchaser; the legal costs it incurred in settling the claim with the third party purchaser; the legal costs it incurred in the underlying arbitration; and the arbitrator's fees in that arbitration. Additionally, the Claimant succeeded on interest and costs.

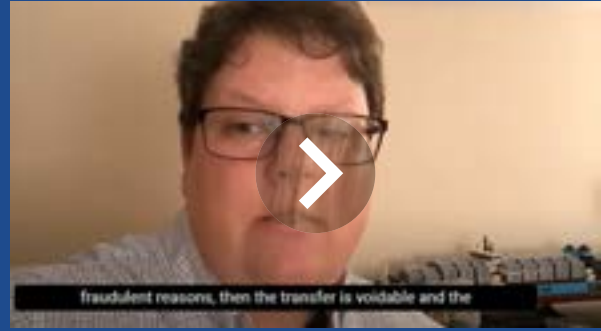
CONCLUSION

This case exemplifies how common law claims can be successfully used in commercial disputes which, prima facie, seem only able to be resolved in arbitration. Under English law, a finding the defendant's shareholder personally liable (e.g. in tort, or under trust or agency principles, as the case may be) may be the key to unlocking the claimant's ability

and enforce the resulting judgment against assets held personally by the defendant's sole or controlling shareholder, which significantly increases the claimant's prospects of actual recovery.

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Additional content on this topic:



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Fraudulent Asset Transfers

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PROVING HYPOTHETICAL PERFORMANCE WHEN CLAIMING FORCE MAJEURE

Written by Calum Cheyne

RECENT DEVELOPMENTS IN THE LAW SURROUNDING FM

Since the word "coronavirus" first started appearing on new streams, lawyers (ourselves included) have been at pains to analyse and dissect the law of Force Majeure. Despite all of those efforts, one piece of advice stands above all others: Read the Clause.

That is moreover the case in the light of the decision in *Classic Maritime v Limbungan Makmur* (*Classic Maritime Inc v Limbungan Makmur SDN BHD* [2019] EWCA Civ 1102).

There is no general concept of 'force majeure' under English law. These clauses exist across contracts of almost every nature, but English law does not recognise a general concept of "force majeure".

Instead, if a party wishes to rely on a general legal doctrine that would excuse non-performance in the face of impossibility in the absence of an applicable contractual provision, they are left with the common law doctrine of frustration. Running a case on grounds of frustration is difficult and uncertain. In fact, it is so difficult and uncertain that most commercial parties agree their contracts around it, hence the development of "force majeure" provisions, which operate as contractual exclusions, and simply do what they say.

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These provisions outline specific events that will excuse the parties from their failure to perform. If the ‘event’ causing problems in performance does not fall within the list of events outlined in the clause, force majeure is not available to the party seeking to excuse its non-performance. The wording of the clause is paramount.

Following a 2019 case, in certain clauses there is additionally a further hurdle that must be satisfied before claiming force majeure. In contracts where this applies, the party relying on force majeure must show that, were it not for the intervening event, the contract would have been performed.

“BUT FOR” THE INTERVENING EVENT

The recent judgment in Classic Maritime Inc v Limbungan Makmur, which we understand has been appealed to the Supreme Court, explored issues relating to the distinction between force majeure clauses, frustration and exception clauses.

Limbungan (as Charterer) and Classic Maritime Inc entered into a COA, under which the Limbungan intended to provide shipments of iron ore pellets. The cargoes were thwarted by a burst dam. Limbungan tried, but failed, to excuse its non-performance by arguing that the burst dam was a force majeure event.

The force majeure clause read as follows:

*“Neither the vessel, her master or Owners, nor the Charterers, Shippers or Receivers shall be Responsible for loss of or damage to, or failure to supply, load, discharge or deliver the cargo **resulting from:** Act of God,... floods... accidents at the mine or Production facility... or any other causes beyond*

*the Owners’ Charterers’ Shippers’ or Receivers’ control; always provided that such events **directly affect the performance of either party under this Charter Party.**”*

Charterers argued that the burst dam was clearly a cause beyond their control. As such, they fell within the clause and performance was exempt. Owners disagreed. Irrespective of the burst dam, Owners argued, Charterers would have been unable to source the cargo due to issues at the mine.

The Court of Appeal considered whether Clause 32 was a “frustration” clause, or an “exception” clause. Such distinction ultimately dictated the outcome of the case.

Frustration Clauses – Where the clause is a frustration clause, the existence of the event excuses non-performance.

Exemption Clauses – Where the clause is an exemption clause, non-performance is only permissible where performance would have occurred but for the event.

The Court of Appeal held that the wording of the force majeure clause clearly required a nexus between the non-performance and the force majeure event. Limbungan’s claim failed, because the Court of Appeal found that they would never have been able to source the cargo, irrespective of the burst dam.

COMMENT

It is better to pay close attention to force majeure provisions when drafting than when litigating. Consider two key points:

1. Does the force majeure clause cover all of the events that the parties want to excuse non-performance? Do

the parties want a general ‘catch-all’ provision, rounding up any other causes outside of their control?

and

2. Is your clause a ‘frustration’ clause or an ‘exemption’ clause. i.e. does the clause require the party relying on it to show that, absent the force majeure event, they would have been able to perform?

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Coronavirus and Force Majeure

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NEWS & EVENTS

TEAM

| Chicago

Zach Barger joined our Chicago office as a Senior Associate. Zach's practice focuses on litigation and transactions within the shipping & marine, commercial, and logistics & transport sectors.



Zach's previous experience includes serving as in-house counsel for Marathon Petroleum Corporation, the United States' largest oil refiner and Fortune 25 company, business development in the marine sector, and 5+ years in private practice in Ohio.

Read more about Zach [here](#).

| London

We're delighted to announce that **Calum Cheyne** has been promoted to Senior Associate!



Since Calum has joined our firm, he has worked on a number of high profile cases, achieved

impressive results and proven to be an invaluable member of our shipping, commodities, arbitration and litigation teams.

Congrats, Calum, very well deserved!

Read more about Calum [here](#).

EVENTS

| MARCH

Disputes for Tea | Insurance

"Captive Insurers: The Commercial Role and Risk Management Benefits"

A discussion with Ali Hauser, hosted by Edward Floyd and Andrea de la Brena.

Wednesday, 24 March 2021

11:00 EST / 10:00 CST / 17:00 CET

| MAY

Disputes for Tea | Arbitration

"False Friends in Arbitration: A (surprising) Comparative View of US and Austrian Law"

A discussion with Univ.-Prof. Hubertus Schumacher and Edward Floyd, moderated by Gerold Zeiler.

Thursday, 20 May 2021

09:00 EST / 15:00 CET

| JUNE

Disputes for Tea | Shipping

With Timothy S. McGovern and Luke Zadkovich.

June 2021 - details coming soon

| SEPTEMBER

Disputes for Tea | Energy

"Energy Disputes: Spotlight on LNG"

Hosted by Damon Thompson and Lisa Beisteiner.

Thursday, 23 September 2021

| NOVEMBER

Disputes for Breakfast | Intellectual Property

"The Human Factor – Creation, Ownership and Infringement of IP Rights in the Age of AI"

With Alexander Zojer and Lukas Hutter.

Thursday, 18 November 2021

| DECEMBER

Disputes for Tea | Litigation

"US Class Action and European Representative Action compared"

With Edward Floyd and Alfred Siwy.

Thursday, 9 December 2021



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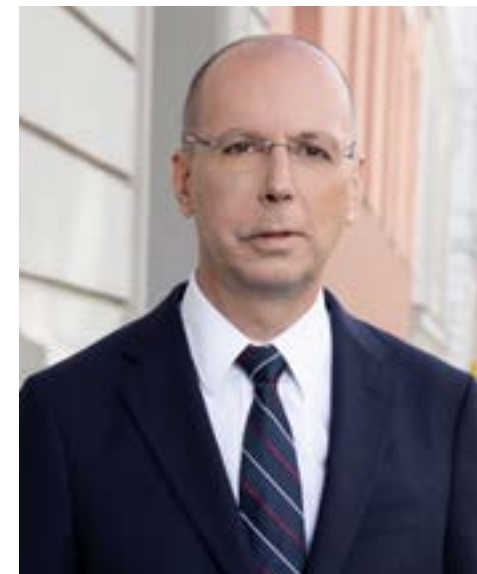
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