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Transport Law: Preparation of a draft convention on the carriage of goods [wholly or partly] [by sea]

Proposal of the United States of America on carrier and shipper delay

Note by the Secretariat*

In preparation for the nineteenth session of Working Group III (Transport Law), the Government of the United States of America submitted to the Secretariat the proposal attached hereto as an annex with respect to carrier and shipper delay in the draft convention on the carriage of goods [wholly or partly] [by sea].

The document in the attached annex is reproduced in the form in which it was received by the Secretariat.

* The late submission of the document reflects the date on which the proposals were communicated to the Secretariat.

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Annex

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I. INTRODUCTION

1. At the 13th session of the Working Group, a draft article providing for carrier liability for consequential damages resulting from delay was included in the draft convention (A/CN.9/552 at paragraphs 18 – 31). More than two years later, at the 18th session of the Working Group, a further provision imposing liability on shippers for consequential damages resulting from delay was included in the draft convention (A/CN.9/616 at paragraphs 83 – 113). When these provisions were considered, it was understood that liability caps for both carriers and shippers would eventually be stipulated.[1] As the provisions on carrier and shipper delay are necessarily related in order to ensure an overall fair balance in rights and obligations among relevant interests, it was unfortunate that these provisions were not simultaneously considered by the Working Group from the outset. It is widely recognized that the final text produced by the Working Group must be viewed as equitable and balanced to increase the likelihood of widespread acceptance and ratification.

2. A number of delegations did not concur with the approach of introducing liability for consequential damages arising from delay for either carriers or shippers, believing such a course would result in legal uncertainties, unnecessary costs, and severe difficulties in practical implementation. Moreover, those delegations anticipated it would prove impossible to determine suitable caps on this type of liability for either carriers or shippers.

3. Although the United States was one of the countries strongly preferring no delay provisions in the draft convention, since the 13th session of the Working Group the U.S. delegation has engaged in extensive consultations within our Government, as well as with the academic community and industry, in order to develop a reasonable position on the appropriate liability caps to complement the regime proposed in the draft convention. We have not been able to find any caps that are acceptable to all of our major industry participants (shipper, carrier, and intermediary interests). Therefore, the United States continues to believe that it will be difficult, if not impossible, to establish caps on this type of liability that would be equitable and acceptable to interested parties. Moreover, the United States does not believe that including delay liability in the draft convention advances any legitimate public policy objective. Imposing delay damages will be practically unworkable, and it will be bad public policy.

4. The United States respectfully requests that other delegations consider the economic and policy arguments set forth in this paper. This type of analysis has not previously been presented to the Working Group. We hope that other delegations will, like the United States, come to the conclusion that liability for consequential

[1] At the 18th session, there was a suggestion that the carrier liability cap for delay might be one times freight, and the shipper liability cap for delay might be 500,000 SDRs (approximately €570,000 Euros or U.S. $751,500). These proposed caps are strongly opposed by shippers involved in the U.S. trades, as they are not perceived to be fair and equitable.

damages caused by delay should not be included on a mandatory basis in the new convention.

5. Preliminarily, it may be useful to remind delegations of the very limited scope of the issue that is before us:

-- Everyone agrees that physical loss caused by either shipper or carrier delay is covered by the draft convention. The question here is whether consequential, i.e., pure economic, loss should be covered, and, if so, what the liability caps should be.

-- Everyone agrees that the shipper and carrier should be liable for consequential loss caused by delay if their contract so provides. The question here is whether there should be liability for consequential damages caused by delay if the goods do not arrive in a "reasonable" period of time, even if there is no delivery date in the contract.

-- Everyone agrees that any delay liability rules included in the draft convention would not be mandatory for "volume contracts" covered by draft article 89's special rules.

-- We are left with only two situations: (1) The carrier may be liable for consequential damages if it causes the vessel to be delayed, but only to shippers that prove that they were damaged as the result of the carrier-caused delay (e.g., the shipper's plant was forced to shut down for lack of a part); and (2) A shipper may be liable to the carrier for damages that the carrier incurs (e.g., loss of use of the vessel or additional port charges) as a result of the shipper-caused delay.

With these parameters in mind, we present the following analysis.

II. IMPOSING DELAY LIABILITY ON SHIPPERS AND CARRIERS IS AN UNNECESSARY CHANGE TO CURRENT LAWS AND COMMERCIAL PRACTICES IN MOST COUNTRIES.

6. As documented in A/CN.9/WG.III/WP.74, the most widely accepted legal conventions governing maritime shipping liability, the Hague and Hague-Visby Rules, do not hold carriers or shippers liable for consequential damages resulting from delay. It appears that only the Hamburg Rules and the Scandinavian Maritime Code provide for such liability, and on carriers only. Thus, for most of the trading world, incorporation of delay liability into the draft convention would represent a dramatic change from the status quo, at the risk of introducing greater complexity and uncertainty into the draft convention.

7. With respect to carrier liability for delay, even in those jurisdictions that apply the Hamburg Rules or the Scandinavian Maritime Code, it is difficult to find instances in which claims have been pursued to recover delay damages from carriers. This suggests that such provisions have not proven effective in accomplishing their expressed purpose, or that there is no need in practice for the imposition of such liability.

8. Moreover, the lack of cases in which shippers have sought to recover delay damages from carriers in maritime transport, both in the few jurisdictions that

expressly provide for such recoveries and in other countries, strongly suggests that this is an issue that as a practical matter tends to get resolved amicably between carriers and shippers.

9. With respect to shipper liability, the scenario in which a shipper is most likely to cause vessel delay is when it fails to provide accurate or complete shipment information to the carrier, the carrier reports such information to customs authorities under new security regulations, and a customs authority delays the vessel to ensure that the cargo loaded on the vessel is not a security threat or otherwise unlawful. Just as shippers appear to have made few or no delay claims against carriers, however, the United States is not aware of any delay claims made by carriers against shippers for this type of delay since the relevant security regulations were adopted in 2002.

10. Based on the relatively recent adoption of security rules and the lack of claims or cases involving vessel delays, we believe there are too many questions and uncertainties surrounding the issue of liability for delay. The United States does not believe it is wise to insert those uncertainties into the draft convention. These circumstances argue strongly against the radical change to current law that would result from the inclusion of delay in the draft convention, which is intended to modernize the liability regime by addressing real commercial issues involving maritime commerce.

11. Furthermore, the Working Group has not been presented with any factual evidence whatsoever that there is a need to include liability for delay in the draft convention. In light of the foregoing, the United States is not aware of any pressing need for governments to impose these new liabilities on shippers and carriers.

12. In this regard, many goods moving via ocean transport are relatively low value commodities (agricultural commodities, raw materials, paper, etc.). Even if the draft convention were to provide a basis for shippers to assert claims on account of delays, it is unlikely that shippers of such commodities would be in a position to prove that they sustained any consequential damages, and thus they would be unable to recover compensation for delay under the draft convention. As explained in section III below, however, if delay liability is included in the draft convention, all shippers will experience increased costs, with those costs disproportionately impacting shippers of goods that are not time-sensitive.

13. Moreover, other developments in the Working Group have had an effect on how delay should be treated in the draft convention. Recalling the Working Group's deliberations at its 13th session, a principal justification asserted for making a significant change to current law and providing for carrier liability for delay was that such action was thought to be necessary in light of the increasing prevalence of "just-in-time" inventory management techniques in global supply chains, whereby assured delivery of goods by an agreed date is an essential element of the transport undertaking. But at its 15th session, the Working Group decided to include draft article 95 on "volume contracts," which upholds the integrity of private shipping contracts. As explained in greater detail in section IV below, such contracts are a much more efficient means of addressing this issue, particularly for time-sensitive shipments, and, as a practical matter, virtually all shipments in "just-in-time" supply chains are transported pursuant to volume contracts of that nature. Thus, the need for protection against delay for "just-in-time" arrangements in this draft convention

appears to have been overstated and the Working Group should not continue to pursue inclusion of delay without pausing to consider the implications of the subsequent decision to adopt draft article 95.

III. DELAY LIABILITY WILL LEAD TO UNNECESSARY COST INCREASES FOR SHIPPERS AND CARRIERS.

14. As noted above, imposing delay liability on shippers and carriers will add significant costs to the ocean transportation industry. Carriers facing exposure to this new liability will be required to purchase insurance to cover their potentially significant maximum exposure (e.g., perhaps one times freight on each container or other unit of cargo on the vessel) and will factor this cost into their freight rates. Shippers facing liability for delay can likewise be expected to purchase insurance cover in an amount equal to the cap on their liability for delay, also a significant maximum exposure (e.g., perhaps 500,000 SDRs per voyage). The end result is an increase in cost to all shippers in the form of higher freight rates due to the increased costs imposed on carriers, and their own increased insurance costs to protect against the liability risks created by the draft convention. These costs will be borne not only by shippers of high-value, time-sensitive commodities, but by many small- and medium-sized enterprises that are shipping lower value commodities and do not need protection against the consequences of shipping delays. This second category of shipper in effect will be required to subsidize the cost of providing such protection for others if liability for carrier delay is included in the draft convention. The shipper delay provisions will likewise add an extraordinary cost to the industry on a cumulative basis. In addition, the exposure created by the proposed shipper delay provisions could have a devastating effect on small businesses that fail to purchase insurance protection but cause a vessel delay due to a documentation or other error.

15. The cost increases described above could have a double impact on transportation intermediaries such as NVOCCs and forwarders, which provide much needed competition to the ocean carriers that otherwise would offer the only transport options in many trades. This is because intermediaries will be required to insure against liability for delay in their capacity as carrier, as well as against liability for delay in their capacity as shipper. These costs will necessarily be passed on to the customers of the intermediary, which are typically small- and medium-sized enterprises. Thus, inclusion of delay will not only again have a disproportionate impact on small- and medium-sized shippers, but will also make intermediaries a less attractive option for all shippers because their cost of doing business will be so significantly increased.

16. Moreover, most businesses that rely on “just-in-time” inventory management have put in place business interruption insurance, which compensates them for losses of this nature whether due to ocean transportation delays or other factors. This approach, because it is specifically tailored to the needs and business model of the individual shipper or carrier, is a far more efficient and economical means of risk management than the “one size fits all” approach reflected in the current draft of the draft convention.

IV. DELAY LIABILITY SHOULD NOT BE IMPOSED ON ALL SHIPPERS AND CARRIERS BUT SHOULD BE ADDRESSED IN PRIVATE CONTRACTS BETWEEN PARTIES THAT NEED SUCH PROTECTION.

17. The United States notes that the Working Group, at its 15th session, decided to incorporate in draft article 95 a regime applicable to "volume contracts" that upholds the integrity of private shipping contracts that derogate from the otherwise applicable terms of the draft convention subject to the limitations provided in that article. Virtually all cargo moving in "just-in-time" supply chains is (and will continue to be) transported pursuant to such volume contracts, which reflect appropriate delivery time commitments and penalties, as agreed between the shipper and carrier or intermediary in question. Simply put, carriers and shippers both are free to negotiate and agree upon contract terms relating to carrier delivery requirements or cargo documentation requirements, including the consequences that will occur in cases of late deliveries or vessel delays.

18. It would be more efficient and equitable to leave the issue of delay to contractual arrangements between those parties who want and need protection such that they may negotiate appropriate terms based on their specific factual circumstances. It would be far more preferable to have contracting parties make appropriate transportation and risk management decisions based on their specific circumstances and shipping arrangements, than to impose a system of delay liability and the resulting costs on all carriers and shippers, many of which have no need or desire for such protection.

V. INCLUDING DELAY LIABILITY IN THE CONVENTION WILL HAVE SIGNIFICANT NEGATIVE IMPLICATIONS FOR ALL CONCERNED PARTIES.

19. At present, carriers typically do not guarantee that goods will arrive on any specific date or even within a prescribed time window, as a number of operational factors may arise that could cause deviations from the usual timeline. Parties doing business in the ocean shipping environment fully understand and accept these inherent uncertainties of this form of transport. In cases in which a shipper cannot tolerate an uncertain delivery date, the goods are normally transported pursuant to a volume contract whereby a time-definite delivery commitment has been negotiated and is reflected in the freight rate. Alternatively, many such time-sensitive goods are not sent by sea at all, but are transported instead by air freight.

20. If the draft convention were to include new provisions imposing liability for delay, a number of unfortunate consequences will likely ensue. As explained above, because the ocean shipping industry does not at present generally operate on the basis of exact delivery dates, it could prove difficult and would introduce much uncertainty to attempt to discern at what point a delay is significant enough to trigger legal liability to pay damages. The draft convention takes the approach of applying a reasonableness standard to resolve this question. This, of course, really just defers the issue until an actual claim arises, at which point both the carrier and the shipper will likely find it necessary to incur substantial expenses litigating their respective positions on the question. Moreover, it seems inevitable that different courts in different jurisdictions may reach different results as to what constitutes

reasonableness, thus resulting in inconsistent treatment of similarly situated claimants, and a lack of certainty and predictability for shippers, carriers, and their insurers going forward. Insurers may understandably have to assume they may face exposure under a "worst case" scenario – i.e., the highest liability under the most extreme interpretation of reasonableness adopted by any forum anywhere in the world – even though the probability of a claimant actually recovering damages of that magnitude may be low.

21. Faced with potential delay liability, carriers can be expected to protect themselves by altering their published schedules and transit times to increase delivery times. This inevitable expansion of transit times would make projected deliveries less rather than more certain, and could needlessly lengthen shippers' supply chains and thereby create inefficiencies. The risk of shipper liability for delay created by the draft convention could compound those inefficiencies if shippers are forced to alter their documentation processes and information flows in order to provide shipment information to carriers earlier than is already required under existing security laws (generally 24 hours before loading) out of fear of inadvertently causing a vessel delay. These adverse consequences are the exact opposite of the purpose for which delay liability is proposed to be included in the draft convention.

22. Moreover, under a new regime imposing liability for delay damages, ocean carriers may be less willing to undertake to arrange inland transportation, since they would find it untenable to be held potentially liable for delays caused by the inland carriers, and for delays resulting from missed connections between the inland transportation and the ocean voyage. This would only add to the cost and complexity of international shipping, particularly for small- and medium-sized businesses, and would tend to narrow the access to world markets for otherwise competitive producers. Such an outcome plainly is contrary to fundamental economic interests of all concerned, and to the over-arching objectives of the exercise with which this Working Group is tasked.

23. The United States believes that the intense competition that characterizes the ocean shipping industry, the potential loss of business by carriers that fail to perform as advertised, and the economic consequences to a carrier of failing to adhere to its schedule (having to speed up vessels thus increasing fuel costs, using alternate and more expensive means of transport, skipping ports of call, port and terminal congestion and the like) all provide a major incentive for carriers to perform in a timely fashion. In addition, shippers likewise have strong commercial incentives to provide carriers with accurate and complete information in order to ensure that their cargo gets loaded onto the vessel and delivered in time to meet their customers' or their own business requirements. Furthermore, if a shipper fails to provide accurate and complete cargo information to a carrier and that failure causes a breach of security regulations, the shipper is already exposed to potential liability outside of the Convention. Thus, there are significant commercial and legal incentives already in place that will cause shippers to exercise due care to avoid causing delays.

VI. CAPS ON LIABILITY DO NOT ADDRESS THE FUNDAMENTAL PROBLEMS WITH DELAY DAMAGES.

24. The current draft provisions contemplate that there will be caps on the amount of carrier and shipper liability for consequential delay damages. As noted in the report on the 18th session (A/CN.9/616 at paragraph 105), it was suggested that the caps might be in the range of one times the freight with regard to carrier liability, and 500,000 Special Drawing Rights (SDRs) with regard to shipper liability. The United States strongly believes that caps on delay liability do not address the broader problems resulting from the inclusion of delay in the draft convention.

25. As noted above, the inclusion of delay requires both carriers and shippers to insure against their respective risks. The cost of insurance will be passed on to shippers by carriers, resulting in higher freight rates. This increases shippers' costs, which will be further increased by the cost of insuring against their own potential delay liability. As further noted above, many shippers do not need this protection and should not be forced to pay for it. Moreover, caps on liability only serve to make the risk reasonably insurable, and do not remedy the fact that including delay liability in the draft convention imposes additional costs on all participants and will create inefficiencies in the ocean transportation industry that are unwarranted.

26. Moreover, resolving the issue of consequential damages for delay in a manner that will be viewed as fair and equitable by the industry is essential to ensuring broad acceptance of the draft convention and widespread ratification. The United States believes that including delay liability in the draft convention for both carriers and shippers is a mistake for all of the public policy and commercial reasons stated above.

VII. POSSIBLE COMPROMISE

27. For all of the above reasons, the United States believes that including delay liability in the draft convention would hurt, not help, all of the affected commercial interests (except, perhaps, the insurers), as well as consumers. If the Working Group nevertheless decides to retain delay liability, then it is essential that language be included making such liability optional in all contracts.

28. At its 18th session, the Working Group decided (A/CN.9/616, at paragraph 113) that text should be prepared that would make shipper's delay liability subject to freedom of contract, just as there is bracketed "unless otherwise agreed" language in the provision on carrier's liability for delay (draft article 63 in A/CN/WG.III/WP.81). Thus, the Working Group has recognized that the issue of whether shipper and carrier delay liability should be optional in all contracts is an open issue that has not yet been decided. The recently submitted Swedish proposal (A/CN.9/WG.III/WP.85) addresses all other parts of the Working Group's conclusions on shipper's delay liability, but does not address the freedom of contract aspect.

29. If delay is included in the draft convention, the United States believes that language must be included that would make these provisions subject to freedom of contract. Unfortunately, however, simply including "unless otherwise agreed" in the articles on shipper and carrier delay liability would not work. This is because in

most non-volume contracts (which are all that need concern us here as it has already been agreed that volume contracts can derogate from the draft convention's delay rules), the shipper may have little or no real opportunity to object to any of the contractual terms, and, in fact, might not even see the contract until after the goods have been delivered. Thus, if the language in the draft convention on both shipper and carrier delay liability simply states that the draft convention's rules apply "unless otherwise agreed," the carrier theoretically could delete all delay liability for itself, while leaving in (and even increasing) delay liability for the shipper. In order to avoid this inequitable result, the draft convention should include an "all or nothing" rule on delay liability. In other words, the parties should have two, and only two, choices: either be silent in the contract on the delay issue, in which case the draft convention's rules apply; or, state in the contract that the draft convention's delay liability rules for both carrier and shipper do not apply. Such a provision could read as follows:

> "Any contract to which this Convention applies may provide that there is no liability under the contract for economic loss caused by delay, notwithstanding the provisions of Articles 30 and 63."

VIII. CONCLUSION

30. The Working Group has benefited from the breadth of views contributed by the wide range of Member States and Observers participating in this process, each of which has its own unique perspective and interests in regard to maritime shipping. One fundamental point that has become very clear is that the end product of our collective efforts must reflect a fair balance among the relevant stakeholders, and a fair and equitable distribution of risks and liabilities. On the issue of liability for consequential damages for delay, the United States is very concerned that it will be difficult, if not impossible, to find caps that will be accepted as fair and equitable by our shipper and carrier interests..

31. A convention of broad applicability such as this draft convention necessarily must propose "one size fits all" solutions. In the case of delay damages, however, the truth of the matter is that "one size fits no one." Not only is there no factual evidence supporting a need to address delay in the draft convention, but the inclusion of delay is being pursued with no analysis of or appreciation for the potential consequences that will result. The United States believes that the introduction of this novel form of liability could have far-reaching consequences on international trade, including a negative impact on the availability of affordable ocean transportation service and the competitiveness of certain commodities, particularly those of relatively low value.

32. The Working Group is in the final stages of a truly historic endeavor, which all of us hope will lead to a widely-adopted maritime liability regime to replace the patchwork quilt of arrangements that currently exists. This exercise has resulted in a lengthy and complicated draft convention. The current draft actually contains more articles than the Hague Convention, the Hague Convention as amended by the Visby Protocol, and the Hamburg Rules added together. To attempt to introduce this new liability for carrier and shipper consequential delay damages will add further layers of needless complexity.

33. If the Working Group nevertheless decides to include carrier and shipper consequential delay damages in the draft convention, despite what the United States believes is overwhelming evidence that this will most likely harm, not help, all parties except insurers, it should do so on a non-mandatory basis. (The question of whether the delay issue should be subject to freedom of contract in all cases has been "on the table" since the beginning of these negotiations, and has not yet been decided. See para. 29, above.) Otherwise, we fear that the delay issue could jeopardize the broad support and acceptance that this draft convention needs in order to be successful.