ITIC
THE PROFESSIONAL INSURER

International Transport Intermediaries Club Ltd.
ITIC is a mutual insurance company with over 80 years experience of providing professional indemnity insurance to companies involved in the transport industry and is backed by A rated security.

International Transport Intermediaries Club Ltd
90 Fenchurch Street, London EC3M 4ST
tel + 44 (0)20 7338 0150 fax + 44 (0)20 7338 0151
e-mail ITIC@thomasmiller.com web www.itic-insure.com

ITIC
THE PROFESSIONAL INSURER

The Intermediary

2008 Edition

ITIC
IS MANAGED
BY **THOMAS MILLER**

Contents

ITIC hosted Forum 2008 this past October with resounding success, thanks to the delegates and the time and efforts of the speakers.

We had the pleasure of hosting over 200 attendees at Forum. With the focus on providing you with access to leading speakers from the industries in which you work and the opportunity to network with colleagues outside of the traditional work environment, the two days mixed formal presentations with interactive discussions and social events.

The first day served as a general forum, which was done in a rolling-debate style, moderated by John Guy. Designed to cover topics that were of a broad interest to our members, the day started with a market overview by Dr Martin Stopford and continued with presentations about the challenges and opportunities facing the different sectors of the industry.

The second day was split into four separate forums to allow for speakers to tailor the presentations and delve into some of the finer points of ship agency, ship broking, ship management, and design and survey. Each forum covered a variety of topics, with some of the new regulations analysed and discussed. Additionally, there were workshops and interactive sessions to stimulate delegate participation.

The quality of the presentations and discussion was entirely due to the efforts of the speakers and interest of the delegates, for which ITIC is greatly appreciative. Forum could not have been successful without the delegates.

For this year's Intermediary, ITIC has decided to use the expertise of the speakers at Forum and reproduce a selection of their speeches. These are all available to download from our dedicated Forum website, www.itic-forum.com/2008.

Where are we now and where are we heading?

Maritime Market Overview

ITIC Forum, Martin Stopford, Managing Director, Clarkson Research Services Ltd

1 October 2008

1. Where is the shipping business today?

Decades can be very different in shipping. The 1980s were miserable, the 1990s were disappointing and the current decade has been astonishingly profitable. Reviewing the current freight statistics we are on the way down from a series of freight market peaks which have produced a historical high in earnings. Whether this is the end of the boom or there are other peaks ahead depends on the fundamentals - the world economy and shipbuilding, discussed below.

2. Where we are now - the world economy?

There is a long and fairly consistent relationship between cycles in the world economy and cycles in sea trade. The world economy has grown at maximum speed for last five years, the best since the 1960s. The historic series shows that growth is interrupted every seven or eight years by a major recession. There are three signals that the next one is due:

Firstly, the credit crisis has undermined the banking system in the Atlantic and seems likely to drive Europe and North America into the fairly serious recession (if they are not there already).

Secondly, the long boom has created "bubbles" in some industries, particularly real estate in most parts of the world and in supporting industries such as steel. These will present real world problems for policy makers (we also have an energy crisis), making it harder to manage the downturn.

Thirdly, China, which was the engine of growth in the last five years, is looking shaky, with slowing GNP, rising costs and falling export volumes.

Like the world economy, sea trade growth of around 5% pa is above trend and is likely to slow (or could even fall – it's happened before). Really the key question is whether we are looking at a short sharp downturn of the type which occurred in 2001, or something that will last much longer than that.

3. Where are we now – shipbuilding?

Even taxi drivers know there is a shipbuilding problem, so I don't really need to brief you. But just for the record ordering over the last three years looks uncomfortably like the big brother of the ordering spree which caused the problems in 1970s.

Newbuilding prices have doubled and this is reflected in second hand prices which have increased even more, especially for dry cargo vessels such as Capesize bulk carriers. Until recently, the sums being invested in new ships are enormous - $233 billion in 2007 and $104 billion to August 2008 - and that makes this a very challenging situation for the shipping industry. Europe still dominates investment, with Greece and Germany accounting for a quarter of investment in new ships. In effect the market has paid for the ships up front with high earnings but where that cash is today and whether it is held by the companies with shipyard orders is anyone's guess. Finally, these orders also represent liabilities which may be difficult for some investors to meet if the difficult financial climate persists.

The distinctive feature of this shipbuilding boom is that the capacity expansion was undertaken at very short notice. The shipyards only started looking at a major expansion in 2004 and the new berths only started to become available for sale in 2006.

As a result, we have been through a "phoney war". Despite all the orders, shipyard production has grown slowly at around five to seven per cent per annum in the last few years. The big surge of output comes in the next three years - I call this "stage 2" production.

The big expansion is in Korea and China. Slippage has become a very big issue which I will deal with in the next section. In the 1973-7 shipyard investment bubble just about everything got built, but the financial climate was very different then.

4. Where are we – slippage?

The delivery schedule is a major issue. The problem is getting accurate information. CRSL has 600 yards on the database, but only specific reported problems at 40, but we would not expect all problems to be reported.

70% of the orderbook is established capacity and 30% in new or extended capacity. However, all shipyards are not the same. The rapid expansion raises 4 questions:

1. Technical performance of start up facilities;
2. Availability of management and skilled labour;
3. Equipment availability; steel prices etc
4. Availability of pre delivery finance.

For the start up capacity, some of which has limited financial and technical backup, these issues could prove very difficult to overcome. Looking ahead, if everything is delivered on time the fleet will grow at over 10% per annum. But if there is slippage of 15-20% and about 5% cancellations, the growth rate of the fleet over the next three years would be 7-10 percent. But, for the reasons given above, we are just guessing how things will develop. At this time, nobody knows whether investors will want to cancel orders in large numbers and if they do, how binding the shipyard contracts will prove to be.

5. Where are we now - world fleet?

The world fleet has now passed a billion tons deadweight and its growth rate will determine how hard times will be going ahead. In the last four years the fleet has grown at around 6% per annum. That compares with trade growth of around 5% per annum. So the fleet and trade were reasonably well in balance.

Looking ahead, based on the slippage scenario we might expect the fleet to grow by 8-10% per annum over the next three years. If we could rely on the sort of accelerating growth we saw in seaborne trade over last five years that might just be manageable. In a recessionary trade scenario the graph shows how difficult things could become if the growth rate of trade slows or even declines.

Just how challenging depends on what happens on both sides of the market, supply and demand. The outlook for sea trade is very poor at the moment and the precise orderbook statistics suggest fast fleet growth – but how much is delivered and when is a matter of conjecture. Indeed these are things it is probably better not to know in advance.

6. Where we are now – conclusions?

We are near to the end of one of the best booms in shipping history. In the preceding paragraphs I lined up evidence that the industry faces a difficult period – a disturbing economic outlook; sea trade growth likely to slow; and the shipyards moving into an extreme expansion cycle which will increase the fleet by 8-10% pa. This is a bad combination for the shipping industry.

We cannot know exactly what will happen but a recession is now very likely and there are some questions we need to consider about the future of merchant shipping:

1. If there is a recession, what will the next decade look like? How deep will the recession be? Where will freight rates bottom? Will they go down to operating costs again? Could modern asset prices fall to one third of their present levels?

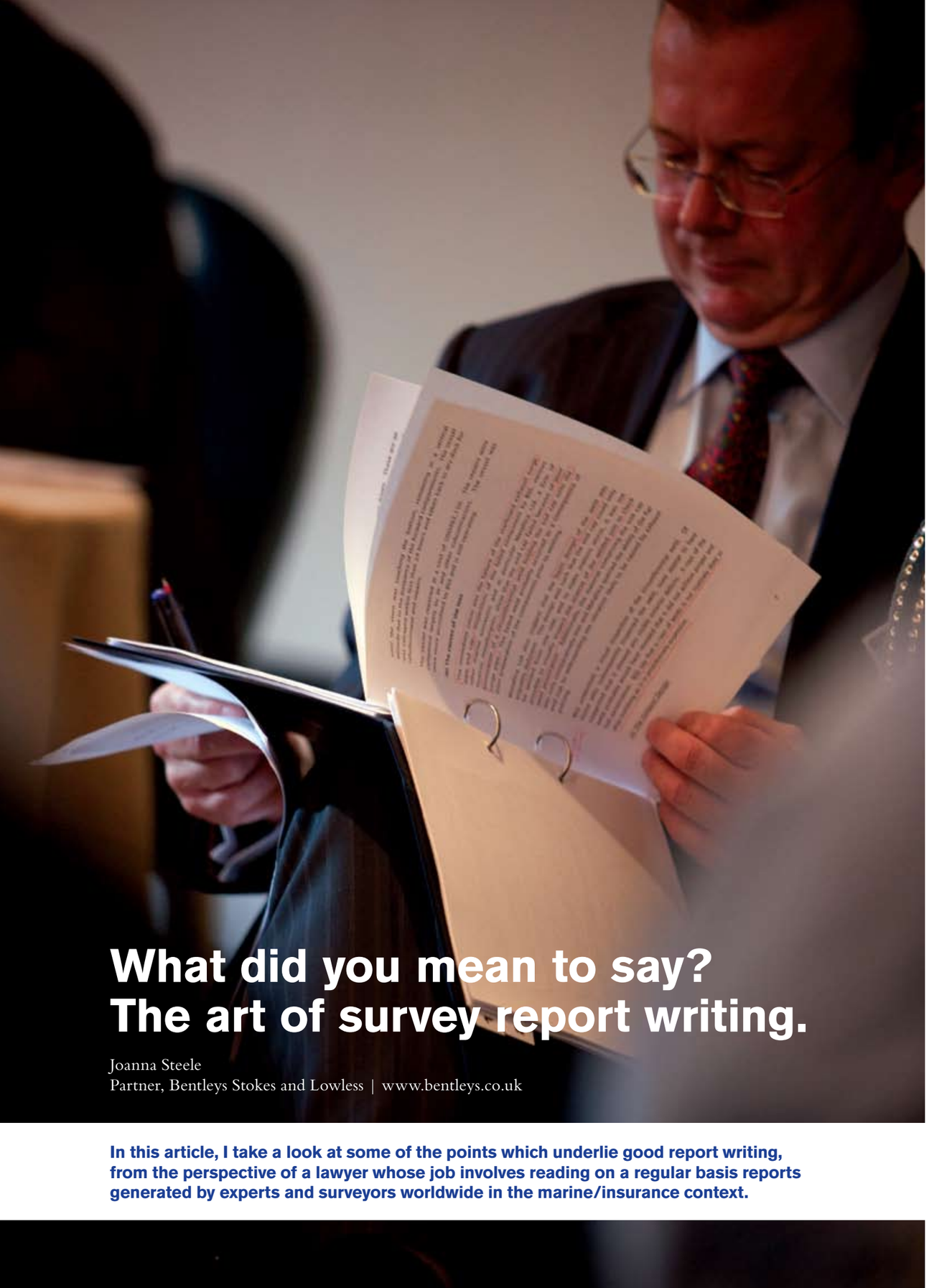
2. If there is a recession, how long will it be? Will it be 2 years (like 2001/2); long but not deep like the early 1990s was for tankers; or a Force 12 hurricane (like the 1980s was for just about everyone).

3. If there is a recession are the problems fundamental enough for a repeat of the sustained market disruption we saw between 1973 to 1997?

4. How will the capital markets respond to falling freight rates and asset values?

Finally, a reminder that shipping faces many other challenges – crewing, energy, regulation of quality and competition, finance and the credit crisis, shipbuilding capacity beyond the present orderbook and political stability.

For full reference to the figures, please see the Powerpoint presentation at www.itic-forum.com/2008



What did you mean to say? The art of survey report writing.

Joanna Steele
Partner, Bentleys Stokes and Lowless | www.bentleys.co.uk

In this article, I take a look at some of the points which underlie good report writing, from the perspective of a lawyer whose job involves reading on a regular basis reports generated by experts and surveyors worldwide in the marine/insurance context.

There is no doubt that a well constructed report makes life easier for everyone - your clients in particular - and minimizes your exposure to complaints/ claims about the job that you have done. But this is not about telling you how to write a report or what you should be saying in a particular context. Why not? Because you have been instructed by your clients who are relying on your particular expertise and want to know what it is that you have found out or you think about a particular problem. So, the key aim the whole way through is clear and accurate communication between you and your client, and anyone else who is going to be reading your report. Rather than telling you what to do or to think, therefore, this article is designed to point up some do's and don'ts and to help you think your way through to a report writing style that suits you and achieves that goal of communication.

The start: who is instructing me?

The obvious point here is that your report should always specify the source of your instructions. By this I mean not just the company providing the instructions, but who it is for whom you are writing your report. If your instructions have come from an insurer - who is the assured? - and are you acting for the assured or just for the insurer? Who your client is will often inform the way you write your report. It is more often than not the case that you are writing a report for people who do not have your expertise or access to the information. You cannot assume that they know and understand all the technical terms or jargon. And sometimes your clients' actual knowledge or understanding is rather more limited than they would like you to think. I have sat in court as an eminent judge has held up a ship's general arrangement plan, gestured at the double bottom tanks and said "And so these are the hatch covers?" This was his way of making sure that the expert witnesses did not make assumptions about his technical knowledge or indeed try to take advantage of his lack of it - he wanted clarity in terms that everyone in that courtroom could understand. Think about the extent to which you will need to explain technical terms, and consider adding a glossary as a convenient way of doing that.

But the other reason for being clear from the very start about who it is that is instructing you is that your clients may have an agenda which you will have to bear in mind. If you have been asked to attend an on hire survey by an owner, for instance, then they are likely to want a report from you which means that the ship is in a deliverable state and they can start to earn hire. A charterer may have a slightly different agenda. Does this mean that you should write your report to accommodate your clients' agenda? Absolutely not, and in fact an important aspect of your professionalism is your ability to manage your clients' expectations. Does it really make sense for an owner and charterer to fall out at delivery, right at the start of a fixture, or is it in the long term going to be better for both parties to start out realistically?

What do they want? Do they really know what they want?

This is not just another aspect of expectation management. How often do you find that you are asked to attend a casualty and "investigate and report"? Make sure that before you get there (ideally) or at the least before you leave that you have discussed and agreed with your client your terms of reference. This may well be a process of evolution and may depend on your initial findings: your clients are likely to be relying on your expertise to guide them as to their requirements. They may not know what they need - they want you to tell them that. What is important is that you and your client understand and agree the scope of your instructions as they evolve. And again, that you record that in your report and identify the issues you have been asked to consider.

What are your clients entitled to expect?

Having identified your clients, their expectations and the scope of your instructions, your clients are entitled to a report from you which has been compiled with reasonable skill and care: an objective standard, which means that it should live up to the standard to be expected from someone who has been asked to do the job which you are doing and who is reasonably competent. Here are some pitfalls to avoid:

Factual investigation – be precise

When reporting your investigation, make sure that your report sets out precisely what it is that you have done. If you carried out an inspection of a cargo space for instance, how did you do it? Did you peer through some small opening or climb down into the hold? How good was the lighting? If you have not done something, say so and why not.

Be clear about the way in which you report facts: often you may actually be reporting a version of the facts given to you by someone else. To take a simple

example, how can you actually say that the weather was bad if you were not out in it? What you can say of course, is that the ship's officers reported to you that the ship had encountered bad weather and that the conditions were reported in a particular way in the ship's logbook. Be conscious that the mere fact of your presence may make people feel under pressure to give you an answer, any answer, just to keep you happy. As a junior lawyer I was sent to sea on a client's ship to gain a bit of experience of life on board a cargo ship: it was a couple of days before I convinced those on board that I was not snooping for the P&I club, but was just asking questions for my own interest and education! Be clear about what you have been able or allowed to find out. A particular danger is to rely on an assurance received from someone else and to report a feature or characteristic that you have been unable to test or verify. There may be a perfectly good reason for your inability to verify something, for instance cargo preventing access to relevant spaces, but it may be that someone does not want you to test something. If you specify in your report why you were unable to verify a particular fact, then not only will you avoid criticism but you may also assist your client with a fruitful line of future enquiry.

Photographs and diagrams will very often be an incredibly helpful way of explaining what you have investigated and found out. If your camera has a time and date stamp facility, then if possible make sure that it is set correctly. A photographic record of what you have looked at will often make your job of describing what you have done much easier, but beware of relying too much on pictures to tell the story. A photograph of a patch of rust on a frame for instance may support the suggestion that rust was found all over a cargo space, but conversely it may equally support the suggestion that a cargo space was largely free of rust. Which leads on to another point: avoid generalisations. Whilst your job may be to decide and certify whether a ship is generally capable of doing the job planned for it, you will have considered a series of specific points and your report should try to be precise about your findings in respect of those specific points.

Opinion – be careful

If you have been investigating an incident, consider carefully the extent to which you are in a position to offer an opinion on its cause. Have you been able to consider and investigate all the possible contributing factors? Are you basing your opinion on the facts? When writing your report, identify and set out the assumptions you have made and any limitations to the view that you are expressing.

If you are regularly instructed as an expert witness for court or arbitration proceedings, you will know that in addition to your professional duty to your client, you will owe a primary and overriding duty to the court or tribunal. In broad terms it is a duty to express an independent view uninfluenced by considerations of your client's requirements. I would suggest that in fact the ability to keep that independence at the forefront of your mind in all areas of a surveyor's work is the mark of the true professional. There is no doubt that at times you will perceive a conflict between what your clients would like the answer to be and what you think it is. Will they thank you in the long run if you do not alert them to the bad news at the outset? Will your professional standing be enhanced if you earn a reputation for doing the client's bidding? These are issues that are well beyond the scope of this article but an independent mindset is something that in my view enhances your report writing.

Structure – be logical

Try to communicate the results of your work in a logical way. Keep facts and opinion clearly differentiated and identified as such. Do create checklists and perhaps document templates for yourself so that when you sit down to compile the report you are communicating in an organised fashion. Your client will thank you for a section setting out your key findings and conclusions either at the end or beginning but make sure that they can understand and relate them to your actions and thought processes set out elsewhere.

The goal: clarity and independence

The foregoing is a series of points which aim to achieve clarity of communication with your client – or indeed anyone else who may in due course read or wish to rely on your report. Clear communication in turn will help you to produce a report which is your professional, independent work product. It is by no means a comprehensive list of suggestions, and you may think they are all terribly obvious. However, I would suggest that they are all points which are usefully borne in mind when you are working on a report and they will help to keep your clients happy, enhance the professionalism of your report and avoid unnecessary complaints and claims.

The current situation is that we do face liability issues, both under the present legal regimes, which courts in different countries are trying to extend, and under EU proposals, which we are trying to modify.

Therefore my objective today is to ask for your support to obtain a dedicated convention which clearly limits our liability in the same fashion as happens for other players in the maritime industry, namely shipowners, charterers, agents, and managers.

We, as classification societies, are in an increasingly exposed position.

Challenges Facing Classification Societies

Ugo Salerno,
Chief Executive Officer, RINA S.p.A

I hope I will provide you with some thoughts about unlimited Class liability that, even if they do not impact financially on ITIC, may very seriously affect the whole Maritime Industry as later I hope I will be able to demonstrate to you.

Every time an oil spill reaches a coastline the local people get justifiably upset. They look for someone, anyone, to blame.

Quite often they cannot identify or trace the shipowner, and even more often, the cargo owner is not visible. However, usually we are, and in the press we are labelled as the people who said the ship was safe.

And we, along with our much larger colleagues, are businesses that have done well in a buoyant shipping market, and all of us publish our financial results. So naturally, we make attractive targets.

We are convinced we should enjoy the same limitation that is granted, as I previously said, to the owner and charterer, being service providers as defined in the CLC convention.

Challenges Facing Classification Societies

I will give you an example that demonstrates that there is a lot of confusion about this issue. In the Prestige case, the attempt by Spain to hold ABS responsible for the Prestige loss and subsequent pollution damages was dropped by the US court, at the beginning of January 2008, because it accepted that classification societies are covered by the CLC Convention under the definition of service providers.

That is in line with the interpretation I was giving before. However, unfortunately for us, in the first instance of the Erika judgement, at around the same time, the Paris court held RINA partially responsible, under French law, for the loss of the Erika, alongside the cargo owner, the shipowner and the ship manager.

What we find amazing is that such a burden was put onto RINA's shoulders on the basis of what was defined by the same Court as a simple "imprudence" by one of our surveyors.

And what is even more incredible is that, if the other parties will be entitled to limit under the CLC, we will be left with the largest part of the bill.

All of us in this room are here because we provide services to shipping. All of us can be held liable if things go wrong when we provide these services. And all of us are have chosen to insure those liabilities.

As long as we can insure the liabilities, and we act prudently, then we can stay in business.

However, if any of us should suddenly find themselves facing unlimited liability, we might also find we would not be in a position to be invited back to the next ITIC Forum. And nobody wants to miss a good party with nice people.

This is where we are today.
This is the legal bit.

Class faces liabilities to:

- **The builder or owner** of a vessel for negligent acts or omissions in performing their duties under the classification contract with the shipbuilder or shipowner.

- **The Flag State** for which the classification society acts as a Recognized Organization (RO) for negligent acts or omissions in performing statutory duties on behalf of the Flag State.

- **Third parties such as:**
  - a coastal state whose waters and/or shoreline have been
  - polluted as the result of an incident involving a classed vessel,
  - the charterer
  - the owner of the cargo who may incur loss as a result of an incident affecting a classed vessel.

We address the issue of potential claims made by the shipbuilder or shipowner through the wording of our Rules and the terms of the class contract. Case law has upheld these terms and shown these contractual arrangements to be a reasonable, fair and effective method of addressing the relationship between the parties concerned.

But claims with respect to acting as a Recognized Organization and potential third party claims now give us a headache. Within the EU, a small number of flag states (Italy, France, Spain) require class societies to accept unlimited liability if they are to be accorded RO status. Moreover the EU, through its Directive governing the recognition of class societies as ROs (article 6 of Dir.94/57/EC), is attempting to extend unlimited liability for classification societies to other states.

The Directive is currently subject to revision and IACS has lobbied for liability caps to be adopted but, to date, has been unsuccessful.

And with respect to third parties, courts are trying more and more, as in the case of the PRESTIGE, to hold liable the only person they can see, which is the classification society.

And we have very limited means of defence.

The answer to such an unfair situation is the introduction of a balanced convention, developed by the IMO, which would unequivocally extend to class comparable liability limits to those accorded to the other principal sectors of the industry. Is that too much to ask? Shipowners, ship managers, charterers, captain and crew, pilots, tugs, salvors, port authorities and all their servants and insurers have a right to limit their liability for negligence pursuant to international conventions such as the CLC 69/92, the LLMC '76 or the Athens Convention '74 et al. Their liability becomes unlimited only if it is proven that they acted "recklessly with the knowledge that damage would probably occur." Flag States may also benefit from sovereign immunity, protection or immunity granted by national and international public law.

How can it be considered fair that the actions of a class surveyor, acting as a statutory agent on behalf of a Flag State, may expose the class society to disproportionate claims while the self same actions, if performed by a direct employee of the Flag State, would allow the State to invoke sovereign immunity against a claimant?

Indeed, in the ERIKA case, we saw Malta granted sovereign immunity by the French court.

Class is usually the body with the least ability to limit liability, yet also has the least ability to influence the course of actions at any time. Class does not design, manufacture, operate, own, maintain or derive commercial benefit from the vessel, equipment or the installation it surveys.

We see the vessel infrequently and for short periods and you can notice it is not the easiest job. We cannot control the vessel or its operations. But if something goes wrong we face claims which could threaten our existence.

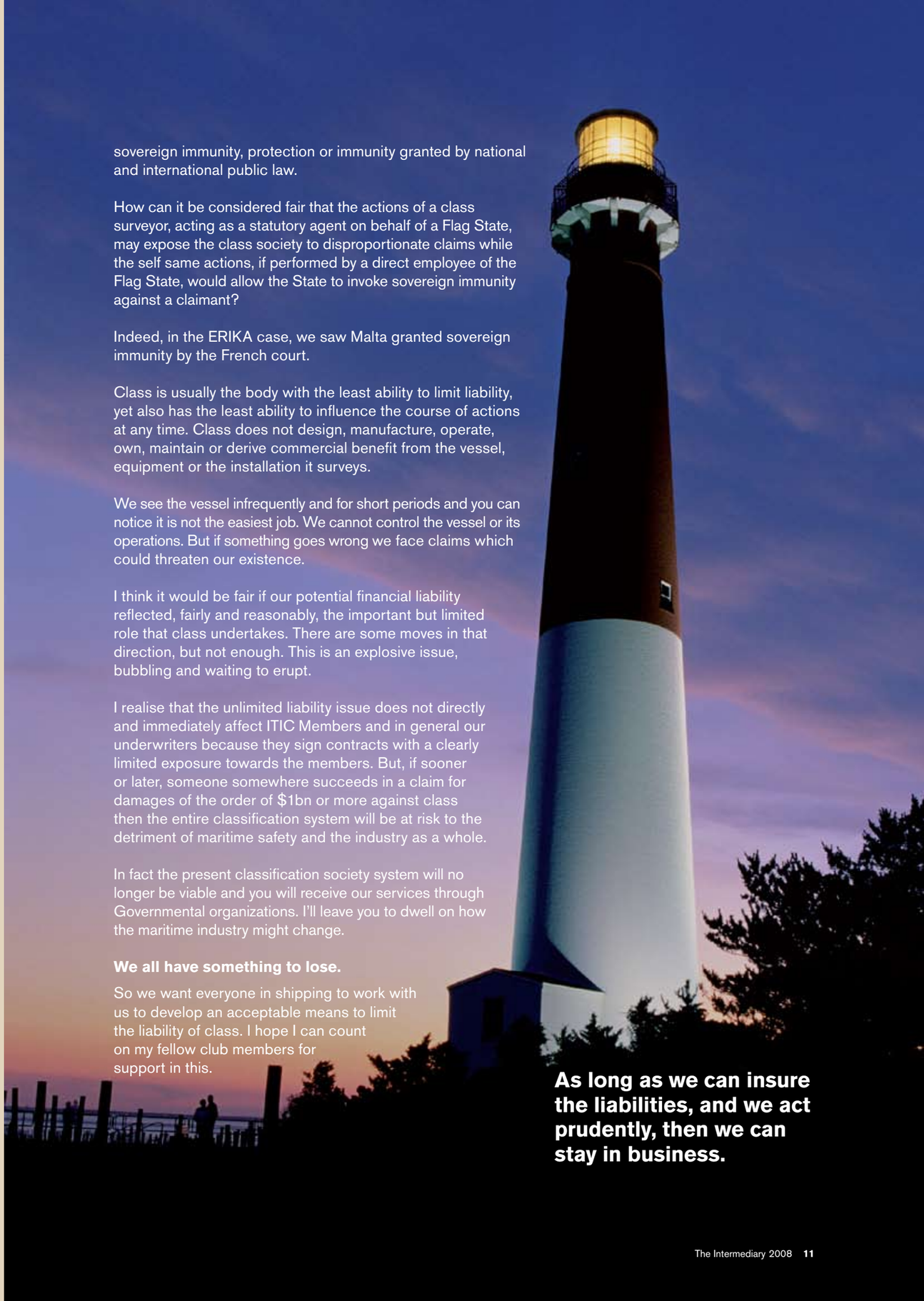
I think it would be fair if our potential financial liability reflected, fairly and reasonably, the important but limited role that class undertakes. There are some moves in that direction, but not enough. This is an explosive issue, bubbling and waiting to erupt.

I realise that the unlimited liability issue does not directly and immediately affect ITIC Members and in general our underwriters because they sign contracts with a clearly limited exposure towards the members. But, if sooner or later, someone somewhere succeeds in a claim for damages of the order of $1bn or more against class then the entire classification system will be at risk to the detriment of maritime safety and the industry as a whole.

In fact the present classification society system will no longer be viable and you will receive our services through Governmental organizations. I'll leave you to dwell on how the maritime industry might change.

We all have something to lose.

So we want everyone in shipping to work with us to develop an acceptable means to limit the liability of class. I hope I can count on my fellow club members for support in this.



As long as we can insure the liabilities, and we act prudently, then we can stay in business.

CONTRACTS OF EMPLOYMENT IN A DOG EAT DOG WORLD

Siân Heard
Partner, Heard & Co. | www.heardlaw.co.uk

Employees are your most important asset, but a business must also be afforded appropriate care and respect. Do your contracts of employment achieve this?

"A business's most important assets are its staff". A platitude, perhaps, but true. Yet there is real tension between the imperative of successful motivation and inspiration of one's employees and protecting the business from the perennial attraction of greener grass. This is a particular challenge where shareholders demand greater profits, the government, quite rightly, requires demonstrable equality and transparency is crucial for effective trading.

continues

1. The Contract

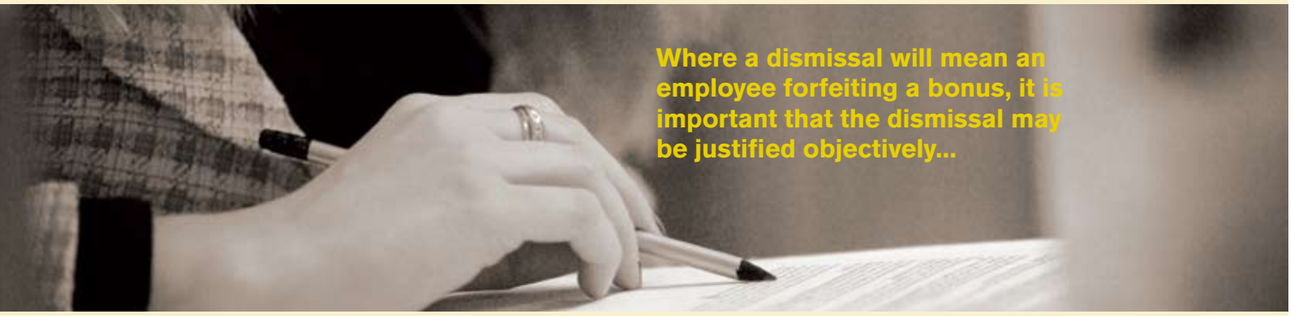
This is the foundation of a successful employment relationship.

There is no legal requirement for contracts of employment to be in writing, although this is obviously highly desirable. All that is in fact required is a "written statement of particulars of employment" (Employment Rights Act 1996 S.1) which must be provided within two months of commencement of employment.

A surprising number of employers have traditionally been content to let matters go at this basic statement. A well drafted contract in the commercial and increasingly mobile world is, however, indispensable. If a balance between employee incentives and client retention when employees leave is desired, that contract should, contain, in addition to the minimum terms referred to above, the following provisions, as a minimum[1]:

(1) a carefully drafted commission and/or bonus entitlement (I will refer to both as "bonus").
(2) Termination provisions, with particular reference to what happens when an employee is under notice.
(3) Post termination restrictive covenants.

Careful and proportionate drafting is essential. Over enthusiastic drafting has invalidated entire clauses, and even contracts, for being too general.



Where a dismissal will mean an employee forfeiting a bonus, it is important that the dismissal may be justified objectively...

2. The Bonus

Most trading and broking jobs are remunerated by way of salary, commission and/or a bonus. This brings with it its own particular issues-

Does a bonus form part of "wages"
Yes. The Employment Rights Act 1996 S.27(1) defines wages as:

> *"…any sums payable to the worker in connection with his employment including (a) any fee, bonus, commission, holiday pay or other emolument referable to his employment, whether payable under his contract or otherwise…".*

This matters because s.13 Employment Rights Act prohibits an employer from making a deduction from wages save, inter alia, where *".. the worker has previously signifies in writing his agreement or consent …*

In *J Sweeney v Peninsula Business Services Ltd* Mr Sweeney was employed as a sales executive. Shortly after commencing employment, Mr Sweeney signed a formal contract and a separate "commission document", which read, inter alia:-

> *If the Contract of Employment is terminated, either by the company through dismissal or by the sales representative through resignation, then special rules apply in relation to commission and bonus payments that might otherwise have been payable.*
>
> *Commission payments on new and renewal business are only paid if the sales representative is in employment at the end of the calendar month when the commission payment would normally become payable. This does not apply in circumstances where the termination by the company or the employee is by virtue of retirement or redundancy.*
>
> *It is, therefore, an express contractual provision that an employee has no claim whatsoever on any commission payments that would otherwise have been generated and paid, if they are not in employment on the date when they would normally have been paid.*

Mr Sweeney's basic salary was £8,500 per year, and the commission element as very important to him. He left, and claimed he had been constructively dismissed, shortly before the bonus became payable.

The EAT found in favour of the employer. They found that the commission clause had been incorporated into Sweeney's contract and that payment of commission was contingent on his being employed at the date commission became payable.

Is a bonus payable even if the employee is in repudiatory breach?
A bonus will usually be payable only at the end of the bonus period in question. Where the contract, without more, states that an employee is *"entitled to receive a bonus, payable on …….. in each year.."*, a pro rata entitlement is probably payable if the employee leaves, whether of his own accord or by way of dismissal before the end of the period for which the bonus is payable.

The contract should therefore provide that the bonus is a) payable only where the employee remains under contract on the date the bonus is paid and has not given or been given notice to leave, b) will not be payable in the event the employment contract is terminated as a result of a breach by the employee, and c) is subject to the absolute discretion of the employer (for more on discretion, please see below).

Dismissal to avoid paying a bonus.
In **Takacs-v-Barclays Services Jersey Ltd** [2006] IRLR 877, an ex-Barclays employee claimed that his employer dismissed him to avoid paying his bonus. Takacs was entitled under his contract to a minimum bonus payment plus an additional bonus if he reached certain targets. He failed to reach those targets and was dismissed, without payment of the additional bonus, on notice shortly before the end of the first year of his employment.

Takacs claimed that Barclays had recruited a team which took over the negotiation of a deal he had been working on. He claimed that Barclays was in breach of implied terms in the contract, being the duty of trust and confidence, a duty of cooperation in the achievement of targets, and a term that the company would not dismiss him specifically to avoid paying his bonus. Barclays tried to have the claims dismissed without a full trial. But it was decided that all these alleged breaches deserved a full hearing and a trail was ordered.

The decision in this case was made at an interlocutory stage only and was subsequently settled. It was very fact specific and, for all these reasons, it needs to be treated with caution. The moral, however, is that where employees are promised performance related bonuses, changes in the systems and distribution of work which may affect their ability to meet their targets need to have a clear rationale and be implemented sensitively.

Similarly, where a dismissal will mean an employee forfeiting a bonus, it is important that the dismissal may be justified objectively; the employee may otherwise claim the dismissal was solely to avoid the bonus payment.

The contract should provide that the bonus will not be payable if the employee has been dismissed or is serving notice.

This formed part of the decision in the Sweeney case considered above. It was more recently considered in **Commerzbank AG v Keen AG** [2006] EWCA Civ 1536).

Keen was employed from November 2002 until June 2005, at which time he was made redundant following the closure of the desk he managed.

Commerzbank operated a discretionary bonus scheme, which provided, inter alia, that no bonus would be paid if the employee was not employed by the bank or was under notice.

Following his redundancy, Keen claimed damages for an alleged underpayment of discretionary bonuses for the years 2003 and 2004 and for non-payment of a discretionary bonus in 2005, the year in which he was made redundant.

Commerzbank made an application for summary judgment on the basis that his claim had no real prospect of success, but was unsuccessful. The bank appealed.

There were two critical issues before the Court of Appeal. First, the court had to determine whether the decision not to pay Keen any bonus for the work in 2005 was an irrational exercise of the bank's discretion. Keen argued that the bank had benefited from his work until he was made redundant (i.e., a half year) but had not paid him for it. The court found that Keen was not entitled to any bonus payment for 2005 as he did not satisfy the clear contractual condition of being employed (in March 2006) when the bonus became payable.

Discretion
The term *"in our absolute discretion"* does not give an employer an unfettered discretion. The leading case is **Clarke v Nomura** (2000) IRLR 766. Mr Clarke was employed as a senior proprietary trader. He was, by common consent, a "profit machine" and in the first 12 months of his employment, he made profits in excess of £13.75 million pounds. For that period, he was awarded a bonus of £2.55 million.

In February 1997, Mr Clark was dismissed without, it transpired, good cause. He was given three months notice and placed on garden leave, and paid his full salary (a comparatively modest £125,000 per annum) until his employment ceased.

Nomura decided to award him a nil bonus for the period immediately before his employment ceased, even though in the relevant period he had achieved profits in the region of £6.5 million and, further, had secured another transaction which generated further profits of £16 million.

Clark's contract of employment provided.

> *"…Nomura operates a discretionary bonus scheme, which is not guaranteed any way and is dependent upon individual performance and after the first 12 months your remaining in our employment on the date of payment. As discussed, for the first 12 months of your employment you will be eligible for payment as per appendix A…"*

Appendix A read, inter alia, as follows:-

> *"..The purpose of this document is to establish a clear outline of the parameters for a European Proprietary bonus scheme that is open and understood and that continues to provide senior equity management with discretionary elements dependent on overall performance and contribution to the business.*
>
> ***Bonus Calculation and Methodology***
> *Trading activities generate a bonus pool of 20% of performance profit (ie revenue less expenses other than group overheads), after return on regulatory capital of 15%.*

[1] There are, of course, many other terms, beyond the scope of this article, which employers, operating within an increasingly regulated employment, should include, such as maternity and paternity terms, working time regulations, and so on.

Up to 33.3% of individual bonus payment is at the discretion of Senior Management. This discretionary element is dependent on corporate contribution, team working, capital usage and due regard to risk..”

Clarke challenged the decision to award a nil bonus. In reaching his decision, the judge had first to determine what express parameters determined the bonus award and, second, whether that discretion was fettered by any implied parameters.

As for express parameters, Clarke claimed that the key phrase was *“individual performance”* and that this referred only to profitability. He brought expert evidence to the effect that a proprietary trader’s main function is the increase of profitably, his talent for which was not in dispute. Nomura contended that “individual performance” was one factor alone.

The judge endeavoured to reach a compromise. On balance, he preferred Clarke’s evidence that profitability was, in the context of assessing “individual performance” of a proprietary trader, the main factor but that “total contribution” was also a factor.

Having thus determined the express parameters to which the discretion must be addressed (“individual performance” and “total contribution”), Burton went on to consider what implied fetters operated as a check on discretion.

This question was construed in the light of a number of authorities which had established that where an employer has the apparent right to “total discretion”, without any express parameters, he cannot exercise that discretion capriciously (**Clarke v BET Plc** (1997) IRLR 348) or without reasonable or sufficient grounds. **White v Reflecting Road Studs Ltd** (1991) ICR 733).

The judge defined capriciousness as carrying with it aspects of “arbitrariness, domineeringness, or whimsicality”. Ultimately, he held that the correct test, when considering whether an employer had exercised his discretion legitimately, was

“… one of irrationality or perversity (of which capriciousness would be a good example) ***i.e. that no reasonable employer would have exercised his discretion in this way…”***

Clarke had been dismissed without good cause. Some of the factors given as a reason were a failure to attend management meetings, erratic time keeping, wearing inappropriate clothes. These reasons, which were in any event, not accepted as being appropriate, were, crucially, nothing to do with the performance criteria by which his bonus was, lawfully, to be assessed. In the circumstances, Mr Clarke won his wrongful dismissal claim and was awarded damages of £1.35 million.

Subsequent cases have affirmed the Clarke v Nomura approach. In **Horkulak v Cantor Fitzgerald International** [2004] EWCA Civ 1287, a broker (Mr Horkulak) who resigned with two years left to run on a fixed term contract of employment. The contract stated that “the company may in its discretion, pay you an annual bonus”.

Having successfully brought claims for unfair and wrongful dismissal (on the basis that he had been subjected to bullying and abuse by his superiors), Mr Horkulak claimed an entitlement to the bonus that he would have expected to receive had he remained working for the company for the full term of the contract. Cantor Fitzgerald resisted this claim, arguing that, as the bonus was discretionary, they would have been under no obligation to pay any bonus.

The Court of Appeal approved Clarke v **Nomura** and held that Mr Horkulak was entitled to a “bona fide and rational” exercise of discretion by Cantor Fitzgerald in relation to the bonus scheme. In reaching this decision, the Court of Appeal relied on the fact the clause related to a high earning and competitive activity in which the payment of discretionary bonuses was part of the company’s remuneration structure. The Court of Appeal thought it clear from the wording and the purpose of the clause that it was intended to be read as a contractual benefit to the employee, as opposed to merely a declaration of the employer’s right to pay a bonus if it wished.

Unfortunately, the **Horkulak** decision offers no assistance as to how an employer may ensure that a discretionary bonus clause remains truly discretionary. This was considered in **Keen v Commerzbank AG** [supra]. Keen had challenged the bonuses awarded to him in 2003 and 2004, the two years before he was made redundant. The court held that the burden of establishing that the level of a discretionary bonus payment by the employer was irrational or perverse, where much depended on the employer’s discretionary judgment having regard to fluctuating markets and labour conditions, was very high, and, since the bank had a very wide contractual discretion the bank’s awards of bonuses to the claimant for those years could not be said to be irrational.

In addition, the court noted that Keen’s assertions about the irrationality of the bank’s decision were not supported by independent or expert evidence. It held that his arguments were based mainly on recommendations that his boss had made to the bank regarding the size of the awards.

The court made some other comments in its judgment that will prove helpful to City institutions. It emphasised that it was not its function to usurp the bank’s exercise of its discretion and substitute its view for that of the bank. The court’s function was solely to decide on the legal limits of the bank’s discretion and whether it had acted within or outside these limits.

No guaranteed minimum

The Nomura decision is again of assistance here. You will recall that Clarke’s contract provided:

“…Nomura operates a discretionary bonus scheme, ***which is not guaranteed any way.”***

The judge found that this meant that there was no guaranteed minimum payment. However, he also found that a legitimate exercise of discretion was still required. A legitimate exercise may mean that a nil bonus award is made, but the discretion must nevertheless be capable of analysis and exercised within the express and implied constraints.

3. Garden Leave

It used to be perfectly permissible for an employer, seeking to restrain an employee from working for any rival during his contractual period of notice, to ask that employee to stay at home, provided he was prepared to provide the employee with all his contractual benefits until the contracts expired, without insisting he perform any serves (**Evening Standard Ltd v Henderson** [1987[ICR 589). However, this is now possible only where this has been expressly agreed.

In **William Hill Organisation Ltd v Tucker** [1999] ICR 291, Mr Tucker gave only one months notice (his contract required six) of resignation, with the intention of joining a competitor. His employees sent him home, and agreed to pay his salary in full, but advised him that he was not to come into work.

The Court of Appeal held that in the absence of such a clause, William Hill was in breach of such a contract. In reaching the decision, the Court held that the contract could and should be construed as giving rise to an obligation on the employer to provide the employee with work. Relevant factors were:

- the uniqueness of the employee’s post as the only senior dealer on the desk.
- Tucker’s particular skills would unless exercised frequently, diminish. The court held: *“Although it is not a case comparable to a skilled musician who requires regular practice to stay at concert pitch, I have little doubt that frequent and continuing experience of the spread betting market, what it will bear on the subtle changes it goes through, is necessary to the enhancement and preservation of the skills of those who work in it…”*

Placing Mr Tucker on garden leave in these circumstances amounted to constructive dismissal.

This left the employer in a very difficult position, as wrongfully terminating a contract, whether by way of constructive dismissal or otherwise, serves to release an employee from any restrictive covenant. In **General Bill Posting Co Ltd v Atkinson** [1909] AC118 a bill poster had been dismissed without notice. His contract had sought to restrict his right to trade as a bill poster within a certain radios for two years after the termination of employment. The House of Lords held that the employer’s wrongful dismissal had brought to an end all contractual terms.

It is therefore imperative to incorporate a specific garden leave provision.

The period during which the employee may be placed on garden leave must not be excessive and there is a growing tendency to take into account any period spent on garden leave from any post termination non compete clause, as to which I comment further below.

4. Post Termination Restrictive Covenants

Post termination covenants are designed to restrain the activities of a former employee for a period after employment has come to an end.

The basic position is that such covenants are void as being contrary to public policy, as they are by their very nature anti competitive and in restraint of trade. To enforce such contracts the ex employer can show that the covenant is no more than is reasonably necessary to protect “his legitimate business interests”. The burden of proof is on the employer, who must show that the covenant is reasonable in terms of its geographic extent and period.

A “legitimate” interest is proprietary in nature. It will include such matters as trade connections, customers’ lists, trade secrets and other confidential information. Particular post termination restrictive covenants include the following:

(a) Non compete and non dealing clauses

Non-compete provisions endeavour to prevent a former employee contacting his former employer’s clients for a particular period. Such a clause is difficult to police and, if enforceable, would not prevent a client contacting the ex-employee. A non-dealing covenant achieves greater protection and prevents a former employee working for a client - even if that client wishes to work with the ex-employee. Such provisions are, however, onerous and will be upheld only if reasonable. They must, as a minimum, be expressly limited to those clients whose business was handled by that employee.

In **Cantor Fitzgerald (UK) Ltd v Wallace** [1992] IRLR 215. A restrictive covenant sought to restrain employees (brokers dealing in Euro bonds) from working in any competing business for a period of six months after the termination of their employment. The employees resigned and joined a competitor. Cantor sought an injunction and

argued that the five employees had built up relationships of trust with the various traders with whom they had worked during their employment with Cantor UK and that, because of this, they would continue to deal with those traders after leaving that employment, thus causing unquantifiable loss and damage to Cantor UK. It was argued that the restrictions were necessary for the protection of Cantor's UK trade and should be enforced. The Court held that an employer was only entitled to protect a proprietary right recognised as a legitimate object of protection. There was no proprietary right in the connection built up while the employee was in employment; such connections were based on nothing more than the personal quality of the employee.

(b) Covenants seeking to prevent an employee "poaching" a former colleague
Non-poaching covenants were, until relatively recently, considered unenforceable. The courts now, however, accept that employers have a legitimate business interest in maintaining a stable workforce, and a 'non-solicitation of staff provision' can, therefore, be effective. It is imperative, however, that the clause is carefully drafted .It should, for example, be restricted in duration and refer only to those people with whom the ex employee worked directly.

(c) Geographical Extent
A clause will be struck down if its geographical ambit is unreasonably wide. Thus in **Office Angels v Rainer Thomas** [1991] IRLR 214, the Court of Appeal struck down a clause which sought to prevent a manager and consultant from working within a radius of 1000 metres of their branch. The branch concerned was in the City and thus prevented them from working in most of the City of London.

(d) Duration
The approach here should not be 'how long can the employee be kept out' but 'how long do I reasonably need to protect and repair my business?'

Of increasing relevance here is the length of any preceding garden leave provision. In **TFS Derivatives-v-Morgan** [2005] IRLR 246, for example, Morgan's contract of employment contained a clause restricting competition for a period of six months following the termination of his contract less any period spent on garden leave". On giving 3 months' notice, he was put on garden leave for the notice period. TFS then sought to enforce the non-compete clause which after permitting set-off was for a period of 3 months.

Morgan argued that the non-compete was an unlawful restraint of trade because TFS could have adequately protected itself by providing for six months' notice on garden leave. This would have been a more flexible and more reasonable restriction to impose and employers who wish to restrict the future employability of a former employee should be prepared to pay for such restrictions.

The judge was invited, in the absence of decisions on the relationship between garden leave and post termination restrictive covenants to take the opportunity to say something about the reasonableness and greater attraction of garden leave clauses generally. This did not form part of her decision, but she commented that garden leave could be regarded as "more onerous" than a post-termination restriction, since it would stop the broker from exercising his skills entirely for 6 months. She also suggested that a 6 months' enforced period of garden leave, even if in accordance with an express term of the contract, would be likely to face resistance on the basis that its use would amount to a breach of the implied term of trust and confidence.

In a more recent decision, however, a more robust long term non-compete clauses was upheld. The case was **Extec Screens & Crushers Ltd v David Rice** [2007] EWHC 1043. The employee argued that a period of 3 months spent on garden leave should be deducted from the eight months post termination non compete clause. The judge disagreed, however. That was not what the non-compete clause said; it referred to a period of *"8 months after the termination of the employment"*. A total of 11 months was not, in his judgment, excessive period and as periods of up to 12 months are commonly upheld by the courts, he found no reason to cut down the extent of the non compete clause.

(e) confidential information and trade secrets
During employment the employee owes the employer a duty of confidence which may be stated in the employment contract, but if not it will be implied by law and restrictive covenants will usually expressly prevent the employee from disclosing confidential information after employment ends. However, what information is truly "confidential" and for how long can it survive the end of employment? Examples given by the Court of Appeal in **Faccenda Chicken v Fowler** [1985] 1 All ER 724 included 'secret processes of manufacture such as chemical formulae', 'design and special methods of construction' and 'other information which is of a sufficiently high degree of confidentiality to amount to a trade secret' The court also held that the obligation of confidence existing post-employment was more restricted than that which operated during the currency of the employment and identified four aspects which are relevant to differentiating between trade secrets and other information which could not be protected post-employment, and the most relevant of these for our purposes are:

(i) Has the information been given to only a limited number of employees
(ii) Has the employer impressed on the employee the confidentiality of the information
(iii) Can the confidential information be easily separated from other information acquired by the employee during the course of employment.

It is also important to differentiate between confidential information and know-how, which is the general skill and knowledge that an employee acquires during the course of employment and is entitled to take to a future employer: See **FSS Travel & Leisure Systems Ltd v P.A. Johnson & The Chauntry Corporation Ltd** [1998] IRLR 382.

In summary, therefore, where an employer has information that he wishes to protect care should be taken to identify that information as confidential, to separate it from other non-confidential information and to restrict its availability within the workforce.

5. Severability Provisions
It is essential that any contract, which seeks to incorporate restrictive clauses, contains a clause which provides that, in the event of any one provision being declared void and unenforceable, the other parts of the contract shall nevertheless remain valid, and the contract shall be read as though such a provision formed no part.

6. Can Restrictive Covenants Be Imposed After Commencement Of Employment?
In **Willow Oak Developments Silverwood** [2006] EWCA Civ 660, the employer required existing employees to enter into widely drawn covenants restricting their business activities after their employment ended. The claimants refused and were dismissed.

Upholding complaints of unfair dismissal, the employment tribunal held that the covenants were so unreasonable that the refusal was not a "reason of a kind such as to justify the dismissal" for the purposes of section 98(1)(b) of the Employment Rights Act 1996, nor, alternatively, could the claimants' dismissals be regarded as fair under section 98(4), since there had been a lack of consultation, no proper opportunity for the employees to understand the covenants and no warning that a failure to agree might result in dismissal. The Employment Appeal Tribunal dismissed the employer's appeal, holding that, although the employer's reason for dismissal fell within section 98(1) (b), the claimants' dismissals were unfair under section 98(4).

On appeal by the employer, the Court of Appeal held that although an employee's refusal to accept covenants proposed by the employer for the protection of his legitimate interests could be a reason "of a kind" such as to justify dismissal under section 98(1) of the Employment Rights Act 1996, the claimants' employer did not in all the circumstances, in particular in giving no warning that failure to agree the new terms might result in dismissal, act reasonably, as required by section 98(4), in treating that reason as a sufficient reason for dismissing the claimants and, therefore, the dismissals were unfair.

7. Conclusions
Lucrative lures from competing employers have, in the last ten years, created a volatile recruitment and employee retention environment. It remains to be seen whether the credit difficulties of 2007 and 2008 will lead to a restriction of the reward culture that has rewarded risk and short term gain over long term stability. Whatever lies ahead, however, a prudent employer should ensure that employment contracts for key staff are routinely and regularly reviewed. His objective is to reward his employees and protect his shareholder's interests and in doing so, his mantra should include realism, proportionality and reasonableness.

MARPOL, Magic Pipes and Whistleblowers.

The Do's and Don'ts for Effective Environmental Compliance.

George M. Chalos, Esq.
Chalos & Co.

Since the tragic events of September 11th, the United States Coast Guard has undertaken a comprehensive program of boarding vessels calling U.S. ports. As a result of the heightened security measures, there has been a significant increase in the scrutiny to which a vessel, her logs, and her records, are being inspected. Such scrutiny, rightly or wrongly, continues to result in numerous vessel and crew detentions, as well as massive civil and criminal charges against vessel Owners, Operators, Managers, Officers and crew.

Specifically, the U.S. Coast Guard established an Oily Water Separator Task Force to examine a wide range of issues related to pollution control equipment and its use on vessels in U.S. waters. The Coast Guard and other law enforcement personnel regularly examine the use and functionality of oily water separator systems more carefully than ever before, and have made it clear that they will seek jail sentences for Masters and engineers of ships committing pollution offense, or falsifying records, including but not limited to Oil Record Books (hereinafter "ORB"). The fact that an Owner, Operator and/or their shore-side staff may be located outside the U.S. is no deterrent to dogged prosecution efforts. Quite often, even if no pollution incident has occurred, the Coast Guard and U.S. prosecutors, upon the mere "discovery" of potential by-passing paraphernalia, (such as a flexible hose or suspicious fittings and piping in the engine room), will commence a Grand Jury investigation seeking to prosecute alleged illegal by-passing of the OWS system and/or the presentation of an ORB containing "false entries".

Document Review During Port State Control Inspection

A document review during a Port State Control inspection will often include an examination of the vessel's IOPP Certificate, ORB, Incinerator Log, and Shipboard Oil Pollution Emergency Plan (hereinafter "SOPEP"). See 33 C.F.R. § 151.23(a). These documents are often utilized during the inspection of the vessel to ensure the vessel, its documentation and equipment meet all applicable APPS and Annex I requirements.

Oil Record Book ("ORB")

Since the ORB is supposed to record all shipboard oil transfer, and all bilge water and sludge discharge operations, it is thoroughly inspected. For this reason, the ORB must be filled out in accordance with all applicable regulations, and all internal transfers, as well as all overboard discharges, must be recorded without delay.

For example, APPS requires an entry shall be made in the ORB whenever any of the following machinery space operations take place: 1) ballasting or cleaning of fuel oil tanks; 2) discharge of dirty ballast or cleaning water from fuel oil tanks; 3) disposal of oily residues (sludge); and, 4) discharge overboard or disposal otherwise of bilge water that has accumulated in machinery spaces. Entries shall also be made in the ORB whenever any of the following cargo/ballast operations take place on any oil tanker: 1) loading of oil cargo; 2) internal transfer of oil cargo during voyage; 3) unloading of oil cargo; 4) ballasting of cargo tanks and dedicated clean ballast tanks; 5) cleaning of cargo tanks including crude oil washing; 6) discharge of ballast except from segregated ballast tanks; 7) discharge of water from slop tanks; 8) closing of all applicable valves or similar devices after slop tank discharge operations; 9) closing of valves necessary for isolation of dedicated clean ballast tanks from cargo and stripping lines after slop tank discharge operations; and, 10) disposal of residues. See 33 C.F.R. 151.25(e).

All such entries "shall be fully recorded without delay in the Oil Record Book so that all the entries in the book appropriate to that operation are completed." MARPOL, Annex I, Regulation 20(4); 33 C.F.R. §151.25(H).

During a Port State Control inspection, the Coast Guard may question the engine room staff to determine if the recent entries in ORB represent actual procedures followed by shipboard personnel. If the Coast Guard discovers any of the following "red flag" entries in the ORB, they will likely call in the Coast Guard Investigative Service ("CGIS")[1] to begin a criminal investigation:

1. An ORB entry where the amount of bilge water or sludge processed exceeds the rated capacity of the pollution prevention equipment that is indicated on the IOPP;
2. ORB entries that utilize the wrong code for the task performed;
3. ORB entries that are not in chronological order;
4. Missing pages in the ORB or entries that are concealed by "White-Out";
5. Repetitive entries that are indicative of the falsification of ORB activities;
6. If waste oil, sludge, bilge and other tank levels noted during the inspection vary significantly from the last entries in the ORB;[2] and,
7. If the recorded quantities of oily bilge water pumped to holding or processed by the OWS directly from the bilge wells does not compare to observed conditions within the machinery space.

If the vessel maintains an Incinerator Log, it, too, will likely be inspected by the authorities. If the vessel is utilizing the incinerator to dispose of sludge, the Coast Guard will compare the entries in the Incinerator Log to the corresponding entries in the ORB. If there is a discrepancy between these numbers or if the log indicates that the incinerator is working beyond its rated capacity, suspicions will be raised that the vessel is improperly disposing of sludge.

The Coast Guard will also examine the SOPEP to verify that it has been approved by the vessel's Flag. The Coast Guard will spot check the pollution response equipment listed in the SOPEP and verify that the phone numbers and points of contact listed in the SOPEP are up to date (i.e., National Response Center, local Captain of the Port, or Coast Guard or Sector offices).

Penalties for Violations

Generally, it is well settled U.S. law that in order for a person to be guilty of a crime, the person must act with "criminal intent." However APPS, like most environmental and public health and welfare criminal statutes, does not require that the government prove that a defendant wrongfully intended to violate the law. Instead, the government need only prove that an actor knowingly committed an act and that act violated an existing law or regulation. For example, the criminal enforcement provision of APPS provides that any person who

[1] The Coast Guard Investigative Service (CGIS) is a division of the Coast Guard that carries out the Coast Guard's internal and external criminal investigations. When personnel from CGIS board a vessel it is a tell-tale sign that the inspection is no longer civil in nature, and a criminal investigation is underway.

[2] For example, the ORB indicates a liquid level in the vessel's sludge tank at the completion of the previous voyage, the sludge level is currently at a lower level, and the ORB fails to indicate how the ship disposed of this liquid.

"knowingly violates" a specific provision of the statute may be guilty of a felony, even if an individual did not know that such conduct was a crime. In addition to criminal fines, if an individual or corporation is found to have violated a provision of APPS or MARPOL, the government can also impose a civil penalty of up to twenty-five thousand dollars ($25,000.00) for each violation. See 33 U.S.C. § 1908(b).

APPS places an affirmative duty on the Master, Chief Engineer - or other person in charge - of any vessel subject to APPS to report any "discharge, probable discharge, or presence of oil" while the vessel is within the navigable waters of the United States. APPS places the same duty to report on persons in charge of seaports and oil handling facilities within United States jurisdiction. To ensure compliance with these regulations, the Coast Guard is authorized to inspect any vessel at any U.S. port. If it is determined that a vessel or her crew may have violated pollution prevention laws, its customs clearance will be revoked and the vessel "held-up" until the owner and operator post a surety satisfactory to the Secretary [of the department in which the United States Coast Guard is operating].[3] The vessel may also be arrested and sold to satisfy any fine or penalty under APPS.

As stated above, APPS applies to every vessel that is operated under the authority of the United States (i.e., "U.S. flagged vessels"). In addition, it is applicable to foreign flagged vessels when these vessels are in the navigable waters of the United States[4]. This is a critical distinction, since the jurisdiction of the United States to criminally prosecute Owners, Operators and crewmembers of foreign flagged vessels, is strictly limited to acts committed in U.S. navigable waters. Parenthetically, we note that for Owners, Operators, and crewmembers of U.S. flagged vessels there are no such limits on the jurisdiction of the United States to prosecute violations of APPS and MARPOL. Thus, if a U.S. flagged vessel knowingly violates the provisions of APPS or MARPOL anywhere in the world, it can and will be prosecuted by the United States government.

In short, it is a class D felony to knowingly violate the provision of APPS. A class D felony is publishable by up to ten (10) years imprisonment, and a fine up to $250,000 for an individual, and up to $500,000 for a corporation, for each violation. A violation of APPS where the individual or corporation did not knowingly violate these sections is punishable by a civil penalty not to exceed $25,000 for each violation.

Other Pollution and Environmental Protection Statutes

In addition to APPS, there are a number of other federal environmental protection statutes that make it a crime to discharge oil or waste in U.S. waters. Specifically, the Clean Water Act, 33 U.S.C. § 1251, et seq. prohibits the unpermitted discharge of any pollutant, including a discharge of oil, by any person into navigable waters of the United States[5]. A "knowing" violation of the Act is a felony. A "negligent" violation of the Clean Water Act is a misdemeanor. Failure to report a discharge is punishable by imprisonment of up to five (5) years, and a fine of up to $250,000 for an individual, and up to $500,000 for a corporation.

Similarly, the Rivers and Harbors Act of 1899, 33 U.S.C. § 401, et seq., provides that any discharge of refuse of any kind from a vessel into navigable waters of the United States is strictly prohibited. A violation of the Act is a misdemeanor. The courts have taken a broad view of what constitutes "refuse" under the Act, and the Act has been extended to a discharge of oil or petroleum. A person can be convicted of a misdemeanor violation of the Rivers and Harbors Act based solely upon proof that the person placed a banned substance into navigable waters of the United States.

A party can also be found guilty of a felony for conduct that does not directly involve the discharge of oil or waste into U.S. waters. Under 18 U.S.C. § 1001, it is a felony to make a false statement to the U.S. Government. To sustain a conviction for a violation of the Act, the Government must only show: (1) that a statement or concealment was made; (2) the information was false; (3) the information was material to a government investigation or activity; (4) the statement of concealment was made "knowingly and willfully;" and (5) the statement or concealment falls within the executive, legislative or judicial branch jurisdiction.

The false statement need not be an affirmative statement, but can also include the concealment of the truth when an individual has a duty to answer. For example, a false statement about, or concealment of, any discharge of oil is a violation.

Additionally, the U.S. authorities vigorously prosecute individuals and corporations suspected of tampering with witnesses in connection with an on-going investigations. Under 18 U.S.C. § 1512, anyone who knowingly uses intimidation or physical force, threatens, or corruptly persuades another person, or attempts to do so, or engages in misleading conduct toward another person with the intent to hinder, delay or prevent the communications to a law enforcement officer or a judge of the United States of information relating to the commission, or the possible commission, of a federal offense, shall be fined or imprisoned up to ten (10) years, or both.

In situations where two (2) or more persons conspire either to commit an offense against the United States, or to defraud the United States, or any agency thereof in any manner or for any purpose, and one or more of such persons do any act to effect the object of the conspiracy, (pursuant to 18 USC § 371), each shall be fined or imprisoned up to five (5) years or both.

Recently, the Department of Justice has also been charging crewmembers and vessel owners and operators accused of presenting false records to the government with violations of the Sarbanes-Oxley Act, 18 U.S.C. § 1519.[6] This statute is commonly known as the "Enron" statute and was intended to apply to corporate fraud. The significance of utilizing this statute is that it carries a potential jail sentence of 20 years, which is a powerful motivator for someone threatened with prosecution under this statute to turn "state's evidence' as the phrase goes. In fact, no vessel Owner, Operator or crewmember has ever been convicted under this statute, although it has been charged in recent Indictments.

Recommendations for Shipboard Personnel on How to Respond to U.S. Authorities Conducting Port State Control Inspections and Prepare for Criminal Investigations

1. Shipboard personnel **must**, at all times, obey all international and U.S. environmental regulations;

2. All shipboard personnel must be truthful and forthcoming during all port state inspections;

3. If the Port State Control inspection appears to be more than a routine inspection, immediately notify the manager and/or the vessel's port agent and/or the P&I Club's local correspondent;

4. Once an investigation commences, do not under any circumstances remove or destroy any documents, computer files, emails, correspondence, piping, flanges, or other potential evidence and do not give or accept any orders to do so;

5. Officers and crewmembers must not attempt to influence other officers and/or crew as to their discussions with the authorities, other than to insist that the officers and crew are honest and forthright with all authorities; and,

6. Seek the advice of competent maritime criminal counsel.

The Fifth Amendment to the U.S. Constitution

The most basic, yet essential, advice any maritime criminal lawyer can give to today's mariner is: **seek the advice of counsel as soon as practical, and always be truthful and forthright in your dealings with the U.S. authorities.** It is extremely advisable that if U.S. authorities undertake any onboard investigation, which goes beyond the scope of the ordinary port state control inspection, competent criminal counsel should be engaged to protect the rights of the vessel officers and crew, not to mention her Owner, Operator, Manager, and their shore-side personnel. For example, if a member of the CGIS comes onboard a vessel during a Port State Control Inspection, a criminal investigation has begun and it may be in the crewmember's best interest to invoke his Fifth Amendment Privilege against self-incrimination.

The Fifth Amendment of the United States Constitution states that:

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a grand jury, except in cases arising in the land or naval forces, or in the militia, when in actual service in time of war or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

The Fifth Amendment Privilege against self-incrimination is not dependent upon the nature of the proceeding in which the testimony is sought. It is applicable wherever the answer might tend to subject one to criminal responsibility and applies in both civil and criminal proceedings.

A seaman may also invoke his Fifth Amendment privileges even if there is no U.S. criminal investigation, but rather may subject the seamen to criminal liability outside of the U.S., so long as the seaman can show that the subject of the government's questions raises "a real danger of being compelled to disclose information that might incriminate him under foreign law," and second, that there is a "real and substantial fear of foreign prosecution."

Individual crew members should invoke their Fifth Amendment privilege against self-incrimination until competent counsel is engaged and present. In short, once a criminal investigation has commenced and a mariner invokes his own Fifth Amendment privilege, he is not required to speak with the U.S. authorities and/or respond to any of their questions, which may lead to self-incrimination.

Conclusion

Environmental compliance and the U.S. Government's prosecution of suspected violations are extremely serious matters. For more information on the subject, please feel free to contact George M. Chalos at gmc@chaloslaw.com.

[3] The Coast Guard, acting on behalf of Homeland Security, in order to release the vessel from any Custom's hold, has generally been demanding bond security in amounts of $1 million or more. In addition, as part of its investigation, the Coast Guard generally removes from the vessel as potential "material witnesses the entire engine room crew and many times other crew members, as well. Consequently, as part of any security agreement for the vessel's release, the Coast Guard requires, among other things, the vessel owner and/or operator to house, feed and pay the salaries for any crewmembers so removed for periods ranging from 90-270 days. Depending on the length and breadth of the investigation, such expenses can be substantial.

[4] The navigable waters of the United States are: 1) the territorial seas of the United States; 2) internal waters of the United States that are subject to tidal influence; and, 3) internal waters of the United States not subject to tidal influence that are or have been used as highways for substantial interstate or foreign commerce. See 33 C.F.R. §2.36(a). Territorial seas of the United States are the waters, 12 nautical miles wide, adjacent to the coast of the United States and seaward of the territorial sea baseline. See 33 C.F.R. §2.22.

[5] "Navigable waters of the United States are those waters that are subject to the ebb and flow of the tide and/or are presently used, or have been used in the past, or may be susceptible for use to transport interstate or foreign commerce. A determination of navigability, once made, applies laterally over the entire surface of the waterbody, and is not extinguished by later actions or events which impede or destroy navigable capacity." See 33 C.F.R. § 329.4.

[6] 18 U.S.C. §1519 reads: "Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both."

Debt collections and ship arrest

Verónica Meana, Partner, Meana Green Maura

Meana Green Maura, with offices in Madrid, Bilbao and Cadiz, has wide experience in shipping and transportation law, particularly in the dark art of ship arrest, both for members of ITIC and for other players in the shipping world.

A dark art is quite an accurate description of ship arrest because it is powerful and dangerous and can be complicated. Also, although sometimes our clients think that we can perform magic, we are not Harry Potter or, in my case, Hermione Granger.

A colleague once said to me that all a ship owner needed in order to trade was a sympathetic bank manager, a bunker supplier, and a ship agent. Unfortunately, and increasingly in this market, ship owners tend to confuse their agent with their bank manager and this is a situation that you need to avoid at all costs. It is rather similar to falling off the Eiffel Tower, at each floor the agent may say “so far so good” but, of course, it is not the fall that hurts but the landing. There is no point in putting lots of appointments through your books if you have to write off half of them as bad debts.

Before taking on the agency you need to consider whether it is worth your while. By this, I mean, that you need to ask yourselves the question, “will I be paid for supplying the services I am requested to provide to this ship?” If you think that there will be a problem, ask ITIC. I was told once that a lawyer in this position is nothing more than an “ambulance driver”. I prefer to think that we are “doctors”. A lawyer can try to cure, minimise or contain the damage but the person who can prevent the problem arising in the first place is you. Therefore, before taking on the ship, please consider the following:

a. Ship age
b. Is she entered with a respectable P&I Club, by which I mean an International Group Club.
c. Is she in class?
d. Has she been detained anywhere and why?
e. Who are your principals?

If you don’t know the answer to these questions, ask ITIC. ITIC has access to the most up to date information available.

If an owner of an elderly ship, whose class expired three years ago and which has been detained by Port State Control in her last port of call, and who asks you to issue clean bills for a cargo of steel coils when the Mate’s receipts have been claused, you may have an issue and need to speak to ITIC.

To give another example, in a recent case, I was instructed to arrest a ship in Vigo on behalf of a ship agent. However, despite scrap prices being high at the time, it was questionable whether the value of the ship exceeded the quantum of the agent’s claim, let alone the innumerable maritime liens which the ship was likely to be subject to during her detention (given that it was clear that her owners were not going to put up security to release her). In that case, we proceed to arrest because surveyors could not rule out that she was worth considerably more than the quantum of the claim. Regrettably, the ship remains in the port and the Spanish authorities are threatening to commence abandonment proceedings. In that particular case, it is possible that the agent may recover some monies even if the authorities seize the ship but my point is that this could be two or three years down the line and there are no guarantees of success. Of course, had the agent been more selective in his choice of principal, he may not have been faced with this situation.

As I said before, ship arrest is a powerful tool. Once the arrest is in place the chances are that the claim may be settled. However, the consequences of wrongful arrest can be serious so, like a marriage, one must not enter into lightly. Before making the decision to arrest, you and your legal advisors and insurers must consider its many implications:

Ship arrest is time consuming and stressful. You are all business people providing a service to your principals. You want to maximize your income and profit in as simple a way as possible. Spending time discussing the legal niceties of ship arrest with your lawyer or the Club is not what you want to be doing on a Friday afternoon when your wife or husband is screaming for you to come home.

You must also consider the possible economic consequences that the detention of the ship may have for the parties involved in her operation. If it goes wrong, it can develop into a serious claim for wrongful arrest.

Also, just because “you can” arrest does not mean that “you should” do so. Ship arrest is only a tool to make sure a future judgement is enforceable. It is merely accessory to the substantive proceedings. It does not create rights of actions or liens. Yet, sometimes an arrest may be possible but enforcement against the ship is not. This is when you may need to consider who your principal is. For example, an agent may have a maritime claim, which does not have the status of maritime lien, against a time charterer. A maritime claim affects the personal assets of your principal. A maritime lien on the other hand affects or follows the ship regardless of whether the owner is your principal or not. Yet, in some jurisdictions, all that is needed for a ship arrest is to allege a maritime claim. In those situations even though ship arrest may seem like the leverage one needs to settle an arrest will be declared wrongful and you may have to pay a substantial amount in damages to her owner. If your

A dark art is quite an accurate description of ship arrest because it is powerful and dangerous and can be complicated.

principal is a charterer and his only asset is a mobile phone then you are in trouble.

Ship arrest differs from jurisdiction to jurisdiction: for example, in Spain, the claimant does not need to make an appearance in Court in order for the judge to grant the arrest. In Portugal, however, the ship agent is obliged to do so prior to an arrest being granted. This must be fine if you are a Portuguese ship agent but a greater logistical problem if you are based in Hong Kong. You should have received a copy of ITIC's ship arrest handbook. This details the procedures and documentation required in many jurisdictions and will assist you in preparing the documentation you require in order to arrest.

Also, if you are using ITIC to arrest, please make sure that you reply to the final message that the Club sends you prior to making the arrest. Without a satisfactory reply to that message, ITIC will not instruct me or any other lawyer to arrest on your behalf.

The particular legal complications of the jurisdiction where the arrest is going to take place must also be taken into account when deciding to arrest. For example, there are jurisdictions which require you to provide:

a. A power of attorney issued by a notary public and duly legalized and translated if the power of attorney has been issued in a foreign country.

b. Prima facie evidence of the claim – this sometimes means not only presenting documentation but also translations of the same.

c. Countersecurity – this would be to cover the shipowner's losses in case of wrongful arrest. Countersecurity may be provided either by cash deposit or bank transfer to the assigned account or by bank guarantee. As I understand the situation, ITIC does not provide this countersecurity. You must do it yourselves and this can be a problem if you are arresting in a foreign jurisdiction because putting up a bank guarantee or transferring money from a foreign account takes a few days. In that few days the ship could have sailed and the time, money and effort spent thus could be wasted.

d. Bond – to maintain the ship during the arrest.

e. As stated before, a court appearance.

f. Deadline to present the complaint in the substantive proceedings.

g. Also, you must consider the Court's availability and idiosyncrasies.

For example, in some jurisdictions, such as South Africa, the Admiralty Courts are extremely proactive and you can even find a Judge on a Saturday morning when he or she is on the golf course who is willing to arrest a ship. However, other jurisdictions, including my own, are trickier. From my own experience, some judges fail to see the urgency of an arrest and the necessity to move swiftly to make ruse the arrest is in place before the vessel departs. This is because they may not be professional judges or if they are, they could be more used to handling other types of matters.

I had this experience when a Judge got upset because he had been allocated two ship arrest cases in the very last days of July prior to his holidays. He rejected both and his state of mind was probably at the base of his decision. Fortunately the vessel was for sale and remained in the Port during the time it took the Court of Appeal to reverse the Judge's decision.

On another occasion, the arrest order was not issued on the date the petition was made because the Judge to whom the petition was assigned had other hearings scheduled for that day and was unable to deal with the petition. Also, please try to avoid needing to arrest a vessel in Spain in August which is the month in which the Courts are "on holidays".

You may think I'm trying to do myself out of business by telling you all the pitfalls of arrest. However, sometimes arrest is the only option and you must go for it and go for it early. There is little point advising the Club and/or your lawyers of a large outstanding debt a week before your lien expires and the ship is sailing off the coast of Somalia. The key is to notify early. Certainly, the Club will thank you. There is an obligation in ITIC's rules that debt collections must be notified to the Club within twelve months of the debt arising, although, given the state of the current market, you would be well advised to notify Club much earlier. Hopefully, this means that, if you need to arrest, you will get your money sooner.

ITIC
THE PROFESSIONAL INSURER

Other insurances available from ITIC

In addition to professional indemnity insurance, ITIC also offers the following products:

Directors' & Officers' insurance
Directors' & Officers' insurance (D&O) is a personal insurance purchased by the employer for the benefit of its directors and officers. ITIC's D&O product protects these individuals from claims against them in person and the company that has to indemnify them.

Loss of management fee
This insurance is offered specifically to ship managers if they are not paid their fee as a result of a ship under their management being lost through actual or constructive total loss.

Cash in transit and money insurance
ITIC offers this insurance to cover cash when it is in the temporary care of a ship agent, whether kept in a strong room at the office or in a safe at home, and is offered either on a single occurrence or annual basis.

Debt collection
This insurance covers the legal costs of pursuing outstanding commission for ship brokers, disbursement accounts for ship agents and other debts. ITIC has collected over USD 90 million for its members and employs a debt collection specialist. We understand that tact is vital to preserve commercial relationships and often a polite reminder is all that is needed to secure payment. However, if proceedings are unavoidable, ITIC will use whatever legal means necessary to try to recover the monies owed to you.

Loss of commission
ITIC offers two levels of cover to ship brokers:-

- Loss of commission resulting from the actual or constructive total loss of a ship.
- Loss of commission due to a wide range of marine perils, such as heavy weather, fire, piracy, collision, engine breakdown and negligence of master or crew, in addition to actual or constructive loss.