

LETTERS OF INDEMNITY

By Charles Williams

THOMAS COOPER & STIBBARD

Ibex House
42-47 Minories
London EC3N 1HA

Tel: 020 7481 8851

Fax: 020 7480 6097

Email: charles.williams@tcssol.com

Website: thomascooperandstibbard.co.uk

A. INTRODUCTION

1. The Bill of Lading is a document dating back long in history. It is a unique document insofar as its negotiability (which will be dealt with below) allows it to fulfil a number of functions. Furthermore, it has been the central cog in an entire framework of instruments and contract relating to international trade. Structures have grown up which owe their basis of the negotiability of the Bill of Lading. However, it is essential if these structures are to work as intended, that the actual and original Bill of Lading is present through the sale/purchase/letter of credit chain at about the same rate as the goods take on the voyage. If this does not happen, then the system, as it was designed, cannot work.
2. The pragmatic solution is the use of the Letter of Indemnity (LOI).
3. However, the use of the LOIs is not a perfect solution. The question is the extent to which legal rights/obligations arising for the use of LOIs fall short of those provided by the Bill of Lading.

B. LETTERS OF INDEMNITY FOR THE NON-PRODUCTION OF BILLS OF LADING

1. Letters of Indemnity can be used for numerous situations where a voyage is not completed in accordance with the terms of the Bill of Lading (e.g. a change of discharge port). However, the most common Letter of Indemnity is the Letter of Indemnity used to procure the delivery of cargo in the absence of production of the Bill of Lading. In this regard, where a receiver/ultimate buyer is unable to present a Bill of Lading to the carrier in order to obtain his cargo, then he may seek a Letter of Indemnity instead. This happens in every trade, but in view of fast voyage times and multiple sales/purchase contracts, it is almost invariable in the oil/tanker trade.
2. The question is, therefore, what extra risks or problems does a Letter of Indemnity have as against a Bill of Lading?
3. In order to find the answer to that question, it is necessary to consider the function of a Bill of Lading.
4. A Bill of Lading is, as noted, a document derived from antiquity. In English law, this is the basis of its legal status. It has acquired its status by virtue of ancient mercantile custom¹.
5. Traditionally, it has three functions², namely:
 - As a receipt
 - As evidence of the contract of carriage; and
 - As a document of title.

¹ *Lickbarrow –v- Mason* (1794) STR 683;

² See Bowen LJ's judgment in *Sanders –v- Maclean* (1883) 11 QB 304 at 341.

6. The Receipt Function

The Bill of Lading will state, on the face of it, details of the cargo and the apparent order and condition within which it was shipped. The description³ is prima facie evidence of the condition of cargo as against the shipper and conclusive evidence as against third parties.

7. Contract Function

The Bill of Lading is not a contract in itself but evidence of the contract. Invariably, the Bill of Lading will either incorporate the Hague or Hague-Visby Rules⁴. A liner bill will contain, on the face of it either the full terms or incorporate the carriers' standard terms. A Charterparty bill will expressly incorporate the Charterparty terms.

8. Under the Hague⁵/Hague-Visby Rules⁶, there is:

- An obligation on the carrier to use due diligence to make the ship seaworthy before and at the beginning of the voyage⁷ and an obligation on the carrier to keep and care for the cargo⁸.
- A package limitation⁹.
- A one year time limit for the cargo owners to bring the claim¹⁰.

³ At least under the Hague-Visby Rules (see below)

⁴ It is possible for the Bill of Lading to contain neither or, alternatively the Hamburg Rules, but both of these are rare situations (but most usually the Hague-Visby).

⁵ "The International Convention for the Unification of Certain Rules of Law relating to Bills of Lading" signed at Brussels of August 25 1925

⁶ "The International Convention for the Unification of Certain Rules of Law relating to Bills of Lading" signed at Brussels of August 25 1924 as amended by the Protocol signed at Brussels on February 23 1968 and by the Protocol signed at Brussels on December 21 1972.

⁷ Article III, Rule I

⁸ Article III Rule II

⁹ Article III Rule 6

¹⁰ Article IV Rule 5(a)

The key point about any contract covered by the Hague-Visby Rules is that a carrier cannot contract out of them in that although he can increase his obligations above those set out by the Hague-Visby Rules, he cannot try to decrease them and any clause which purports to do this will be void¹¹.

9. The Document of Title Function

The document of title has also been referred to as a “control document”¹². It is also “the key to the floating warehouse”¹³.

It is a thread linking a number of contracts, a sale contract, the shipping contract, the letter of credit and the pledge and other security arrangements.

¹¹ Article 3 Rule 8 and Article V, but see Article VI

¹² R. Goode Commercial Law (2nd edn) p.902.

¹³ See also the discussion in Interest in Goods (2nd edn) Chapter 22 (S. Dromgoole and Y. Baatz)

C. THE LETTER OF INDEMNITY

1. It has been noted as to how a Bill of Lading works to draw transactions together. In a perfect world, the Bill of Lading will arrive at the discharge port at the same time as the vessel. However, invariably, this does not happen. Thus, delivery is taken as against an LOI. A typical LOI is set in the Appendix. This is the wording required by the P&I Clubs¹⁴.

2. This LOI:

- Indemnifies the carrier for delivery;
- Undertakes to surrender the Bill on receipt of the Bill;
- Will also include a choice of law jurisdiction clause.

It is to be noted that under English law, a Master is not obliged to give delivery under an LOI¹⁵ (unless ordered by the Court)¹⁶. He is entitled to insist on the original Bill of Lading being presented. However, in relation to Charterparties, there are often Charterparty terms requiring the Master to give delivery against an LOI.

In many cases, where the Receiver is not a well-established company, the receiver will require the LOI to be signed by a bank.

3. P&I Clubs do not regard delivery of cargo without a Bill of Lading as a mutual risk. The carrier is, therefore, “off cover” in respect of mis-delivery if he gives such an LOI. Thus, the LOI effectively takes the place of his P&I cover.

¹⁴ As recommended by the International Group or P&I Clubs.

¹⁵ *The Stettin* (1889) 14 P.D. 142 – See also comments in *The Sormorskiy 3068* [1994] 2 Lloyd's Rep. 266-which also deals with the position where the bill is lost.

¹⁶ *Motis Exports –v- Dampskisselskabett AF 1912* [1999] 1 Lloyd's Rep. Affirmed [2000] 1 Lloyd's Rep. 211

4. Law On LOIs

What is the extent of the Indemnity?

- A Receiver presenting an LOI (“an Indemnifier”) is liable to indemnify the carrier not only for the claim of a Bill of Lading holder but also costs incurred by the ship (i.e. provision of security, release from arrest or loss of hire¹⁷).
- If damages are an insufficient remedy, the Court can order specific performance¹⁸.
- If a Bank countersigns an LOI without qualification, it is probably signing as Indemnifiers (rather than as a verifier of their customer’s signature)¹⁹.
- Carriers should ensure that any LOI is issued with the authority of the Indemnifier.²⁰

5. How does an LOI affect the Contract?

There is no law to suggest that the contract might be affected when delivery is given to the correct party. The law relates to the situation as the contractual terms where there has been a mis-delivery.

The law on this primarily is Australian and, therefore, is only persuasive authority in England.

¹⁷ *The Stone Gemini* [1999] 2 Lloyd’s Rep. 255 (Federal Court of Australia)

¹⁸ *Leamthong –v- Artis* [2004] EWHC 2226

¹⁹ *Pacific Carriers –v- BNP Paribas* (High Court of Australia 5/8/2004)

²⁰ *Pacific Carriers –v- BNP Paribas*

- The LOI is an independent contract, but does not make an independent misrepresentation²¹.
- A carrier is entitled to rely on a Bill of Lading “time bar” even if goods are mis-delivered under an LOI²².
- A carrier which negligently delivers without production of a Bill of Lading will be able to rely on the package limitation²³.

6. How does it affect the Title Function

A Receiver taking delivery pursuant to an LOI will be entitled in English law to sue the carrier provided that he entered into a purchase contract entitling him to the eventual possession of the Bill of Lading prior to delivery of the goods to him²⁴.

²¹ *The Stone Gemini*

²² *Pacific Carriers –v- BNP Paribas* (High Court of Australia 5/8/2004)

²³ *Collern & Co. –v- China Ocean Shipping Company* [1993] P&I International 16

²⁴ Carriage of Goods by Sea Act 1992, Section 2.2(a)

D. OTHER LOIs

LOI for Change of destination

The standard form LOI for Change of destination is in substantially the same form as the LOI for non production of the B/L/

LOI for non-Presentation of Bills under a letter of credit

This is the subject of Maitre Vischer's presentation

Charles Williams

Thomas Cooper & Stibbard

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ANNEXURE

**Typical Letter of Indemnity given in return for delivery of cargo
without production of the original Bill of Lading.**

To: *[Insert name of Owners].*

The owners of the *[insert name of ship]*

Dear Sirs,

Ship: *[insert name of ship]*
Voyage: *[insert load/discharge port as stated in the Bill of Lading]*
Cargo: *[insert description of cargo]*
Bill(s) of Lading: *[insert identification number, date, place of issue]*

The above cargo was shipped on the above vessel by [insert name of shipper] and consigned to [insert name of consignee or to whose order the Bill of Lading is made out as appropriate] for delivery at the port of [insert name of discharge port stated in the Bill of Lading], but the Bills of Lading have not arrived and we, [insert name of the party requesting delivery] hereby request you to give delivery of the said cargo to [insert name of the party to whom delivery is to be made] without production of the original Bill(s) of Lading.

In consideration of your complying with our above request, we hereby agree as follows:

1. To indemnify you, your servants and agents and to hold all of you harmless in respect of any liability, loss, damage or expenses of whatsoever nature which you may sustain by reason of delivering the cargo in accordance with our request.
2. In the event of any proceedings being commenced against you or any of your servants or agents in connection with the delivery of the cargo as aforesaid to provide you or them on demand with sufficient funds to defend the same.
3. If, in connection with the delivery of the cargo as aforesaid, the ship or any other ship or property belonging to you should be arrested or detained or if the arrest or detention thereof should be threatened to provide on demand such bail or other security as may be required to prevent such arrest or detention or to secure the release of such ship or property and to indemnify you in respect of any liability, for loss, damage or expenses caused by such arrest or detention or threatened arrest or detention whether or not such arrest or detention or threatened arrest or detention may be justified.

4. As soon as all original Bills of Lading for the above cargo shall have come into our possession to deliver the same to you, whereupon our liability hereunder shall cease.
5. The liability of each and every person under this indemnity shall be joint and several and shall not be conditional upon your proceeding first against any person, whether or not such person is a party to or liable under this indemnity.
6. The liability of each and every person under this indemnity shall in no circumstances exceed 200% of the CIF value of the above cargo.
6. This indemnity shall be governed by and construed in accordance with English law and each and every person liable under this indemnity shall at your request submit to the jurisdiction of the High Court of Justice of England.

Yours faithfully,

For and on behalf of *[insert name of requestor]*

..... *[signature]*

for and on behalf of *[insert name of bank]*

..... *[signature]*