

No. 4 - Amendment to Lloyd's Open Form – Special Compensation P&I Clause (SCOPIC)

July 1999

Dear Sirs

Amendment to Lloyd's Open Form – Special Compensation P & I Clause (SCOPIC)

An international conference in 1989 agreed a new salvage convention which made a profound change to the nature of salvage. The previous convention of 1910 had been based on a traditional principle of 'no cure no pay'. Liability for salvage awards was covered pro-rata by hull and cargo underwriters in proportion to the respective salvaged values and the clubs were not involved. The fear under the old convention was that salvors might think twice about attempting to salvage a ship where the risk of failure was great and the costs likely to be incurred also great. The intention of the Salvage Convention 1989 was to encourage salvors to act in cases where there is a threat to the environment. Under the 1989 Convention the main salvage award is still based on 'no cure no pay', but the award will take into account 'the skill and efforts of the salvors in preventing or minimising damage to the environment', as well as the traditional factors of salvaged value, danger, out-of-pocket expenses, success, time, and skill. This basic 'no cure no pay' award is dealt with under Article 13. The Salvage Convention also introduced a safety net where the salvor has worked on a ship or cargo which threatens damage to the environment and has failed to earn, under Article 13, an award which covers his costs. In such circumstances, he is entitled to special compensation under Article 14, based on the cost of his equipment and personnel used and his out-of-pocket expenses incurred plus an uplift of 30-100% if he has prevented or minimised environmental damage. The hull and cargo underwriters continue to pay Article 13 awards, even if they are increased because of environmental factors, but the clubs cover Article 14 awards.

The Convention entered into force in 1996 but had already been introduced into LOF 1990 and LOF 1995 and therefore most contractual salvages have been governed by it for some time. There have been a number of problems about the workings of Articles 13 and 14, some of which have concerned shipowners and the clubs and others which have concerned salvors. The clubs have been worried that the safety net gives the salvors an incentive to extend the work for as long as possible and allows the property underwriters to delay the decision as to whether the ship will be accepted as a constructive total loss with little that the club or the shipowner can do to control the operation. Salvors have been concerned that Article 14 only applies if there is a threat to the environment, which has to be proved, and that Article 14 is not relevant outside coastal or inland waters or areas adjacent thereto. Thus there is a geographical restriction. The salvors are also concerned by a decision of the English courts (the *Nagasaki Spirit*) that the rates for equipment and personnel should not include any element of profit. Profit is limited to the uplift which only applies if damage to the environment is minimised or prevented. All these issues have led to arbitrations concerning Article 14 being long and expensive with costs generally being for the account of shipowners and the clubs.

Negotiations took place initially between the salvors and the clubs, and subsequently including property underwriters, with a view to agreeing a simplified framework for special compensation which would promote fast response to casualties but reduce the potential for legal disputes. As a result of these discussions, the SCOPIC Clause has been developed as an alternative to Article 14 for dealing with special compensation (para 1 of SCOPIC Clause).

The idea is that for a trial period of two years the SCOPIC Clause will be incorporated by reference into LOFs signed

between members of the ISU and owners entered in an International Group club, and the clubs will recommend members to contract on these terms. If the trial period shows that the scheme works well then LOF will be formally amended. The main changes are as follows:

- i. The contractor has the option to invoke the special provisions of the SCOPIC Clause at any time of his choosing, regardless of the circumstances. He does not have to prove the environmental threat nor is he subject to any geographical restriction (Para 2). The assessment of the SCOPIC remuneration commences from the time of that notice. Prior to such invocation, salvage is undertaken on a 'no cure no pay' basis without any safety net. Under the current Article 14, calculation of special compensation commences with the start of the salvage operation.
- ii. The shipowner must provide security in the sum of US\$3m within two working days of the contractor invoking the SCOPIC remuneration provisions. If at any time thereafter the shipowner thinks that this is too much or the contractor thinks it is too little he shall be entitled to require the other to reduce or increase the security. If the shipowner does not provide security within the two working days the contractor can withdraw from the provisions of the SCOPIC Clause and revert to his rights under Article 14 (Para 3).
- iii. Rates. SCOPIC remuneration is based on time and materials, plus an uplift in all cases of 25%. The clubs have reached agreement with the ISU on rates for tugs, personnel and equipment (Appendix A). These are rates which are profitable for salvors. Charges for portable equipment are to be capped at 1.875 x the replacement cost of the equipment inclusive of the 25% uplift. If the contractor has to contract in for equipment and the price exceeds the applicable tariff rates then the contractor is entitled to the contracted-in price plus an uplift of 10% on the tariff rates, or the tariff rate plus 25%, whichever is the greater. It is impossible to tell whether these SCOPIC rates are higher or lower than the Article 14 rates, because since the decision in the Nagasaki Spirit, Article 14 rates depend on how much the tug is used in any particular year.
- iv. Salvage services will continue to be assessed in accordance with Article 13, even if the contractor invokes the SCOPIC Clause. SCOPIC remuneration will be payable only to the extent that it exceeds the total Article 13 award (Para 6). If the contractor invokes the SCOPIC Clause and the Article 13 award is greater than the SCOPIC remuneration, then the Article 13 award will be discounted by 25% of the difference between it and the amount of the SCOPIC remuneration that would have been assessed had the SCOPIC provisions been invoked on the first day of the services (Para 7). If there is no potential Article 13 award then the undisputed amount of SCOPIC remuneration is to be paid by the shipowner within one month of presentation of the claim. If there is a claim for an Article 13 award then 75% of the amount by which the assessed SCOPIC remuneration exceeds the total Article 13 security will be paid by the shipowner within one month (Para 8).
- v. The contractor can terminate the services if he reasonably anticipates that the total cost of past and future services will exceed the value of the property capable of being salvaged and his SCOPIC remuneration. Shipowners can terminate the SCOPIC agreement with five days notice (Para 9).
- vi. The shipowner has the right to send on board a casualty representative (SCR) (Para 11) and hull and cargo underwriters each have the right to send on board one special hull and special cargo representative (Para 12). The SCR will be selected from a panel appointed by a committee made up of three representatives from the International Group, three representatives from ISU, three representatives from IUMI and three representatives from the ICS. The salvage master shall send daily reports to Lloyd's and the shipowner until the SCR arrives on site, and after that only to the SCR. The SCR can disagree with the daily salvage report and prepare a dissenting report. If the SCR gives a dissenting report, then the initial payment by the Shipowners will be based only on what the SCR considers the appropriate equipment or procedures until any dispute is resolved (Appendix B).
- vii. A non-binding Code of Practice has been agreed between the ISU and the International Group. The clubs confirm that although they expect to provide security for SCOPIC it is not automatic. The clubs will not refuse to give security solely because the contractors cannot obtain security in any other way. The clubs confirm that they will be willing to consider the provision of security to a port authority to permit a ship to enter a port of refuge and will not refuse such security solely because the contractors cannot obtain such security in any other way.

The advantages for shipowners and clubs in the new SCOPIC provisions are as follows:

1. There should be little need for arbitrations in future on special compensation awards. The problem areas (environmental threat, geographical restriction, tug rates, and uplift) have all been settled.

2. Owners/clubs have much more control or at least knowledge over what happens during salvage.
3. The shipowners' right to terminate under Clause 9 of SCOPIC is clearer than the right under Clause 4 of LOF.
4. The uplift is capped at 25%.

The disadvantages for shipowners/clubs are as follows:

1. The salvors may recover more for the agreed tug rates than they would under the Nagasaki Spirit decision, but this is not certain because of the different utilisation factors.
2. Shipowners/clubs have given up the environmental threat and geographical restriction defences.

The advantages for salvors are as follows:

1. It is no longer necessary for salvors to prove environmental threat and to overcome any geographical restriction defence.
2. Salvors will be paid profitable tug rates.
3. Cash flow problems will be eased.
4. Security is more certain.

The disadvantages are:

1. Salvors can never recover more than a 25% uplift.
2. There is a risk that the owner terminates.

The new proposals have been endorsed by the boards of all the clubs in the International Group for a trial period of two years, and they have also been endorsed by the ISU and UK property underwriters. Overseas property underwriters have been kept advised and have not objected.

We enclose:

1. SCOPIC clause – final draft 24.2.99
2. Appendix A – tariff
3. Appendix B – SCR Provision
4. Appendix C – Special Representatives
5. Salvage Guarantee Form
6. Code of Practice ISU/International Group
7. Code of Practice International Group/Property Underwriters

It is recommended that SCOPIC be incorporated into all LOF contracts signed from 1st August 1999, in the following words: It is agreed that the SCOPIC clause is incorporated into this contract.

Please advise us of the name of anyone you would like to be put forward for consideration for incorporation on the SCR Panel.

All members of International Group Clubs will receive a similar circular.

Yours faithfully

The West of England Shipowners

Insurance Services Limited
(As Managers)

C.A.G. Havers
Director