Port Agreements & LNG Conditions of Use

West has a wealth of expertise in gas tankers providing us with an in-depth understanding of this trade, and the issues that gas tanker owners face in their day to day operations. In this article, we share our experience of insuring liabilities under a “Conditions of Use” agreement, or a COU as it is typically called, in the LNG trade.

A COU is a contract issued by a port to the shipowner that allocates responsibilities and liabilities during the vessel’s stay at the port.

There are a number of operations involved during such a stay including pilotage, use of harbour tugs, cargo operations, receiving provisions and fresh water, bunkering operations etc. As a result, the propensity for an incident is high and the potential consequences of a casualty with these types of vessels may be catastrophic.

Moreover, an LNG terminal is an integral part of an energy supply chain where any incident that puts the terminal out of operation, however briefly, can have a devastating effect on the supply of energy ashore and there may well be no alternative facilities available. Ports and terminals have therefore established a practice whereby the owner of a vessel calling a port is required to agree with the terms of an agreement which governs the conditions for the use of the port by the vessel and allocates responsibility for any liabilities which might arise.

Conditions of use for non-LNG terminals

But these kinds of agreements are not new and have been in existence for other types of trade for decades, especially in tanker terminals. They tend to be onerous for the shipowner, in that the shipowner is liable for all losses and damages sustained by the terminal during the vessels stay at the port, regardless of whether the shipowner was at fault or not. Also, under these contracts the shipowner is commonly held liable for third party losses even where the vessel was not involved and did not contribute to that loss.

How are losses under these agreements covered?

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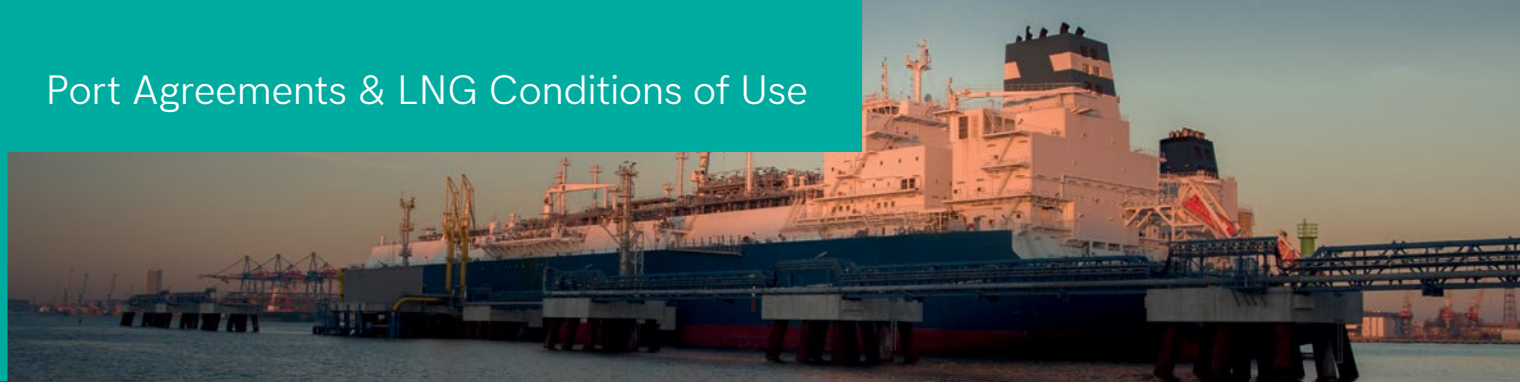

Pooling Agreement

As a Member of the International Group of P&I Clubs (IG), all Group Clubs are bound by the terms of the IG Pooling Agreement. Under the Pooling Agreement, liabilities, costs and expenses which would not have arisen but for the terms of a contract or indemnity entered into by an Insured Owner are excluded from pooling unless the terms of that contract or indemnity are permissible in accordance with the criteria set out in the Pooling Agreement.

These criteria broadly state that an Insured Owner must not assume responsibility, under contract or otherwise, for liability arising or loss resulting from any act or omission for which they would not otherwise be liable under the applicable law, or would for which they would otherwise be entitled to exclude or limit their liability.

So called “knock-for-knock” liability clauses are permitted notwithstanding these criteria, provided that the Insured Owner does not waive limitation.

However, the Pooling Agreement also states that where a contract under which services, goods or facilities are obtained for, supplied or made available to the Insured Vessel - including the provision of port services - do not comply with the above criteria, the liabilities arising thereunder can nevertheless still be pooled if the insuring Club is content that the Insured Owner has used their “best endeavours” to have the offending clauses of the contract changed to comply with the Pooling Agreement criteria.

To satisfy the best endeavours test, it is usually the case that Members must demonstrate that they have tried - even if unsuccessfully - to amend the contract to make liability fault-based, whether wholly or partially by, for example, an exclusion for the sole negligence of the terminal.

LNG conditions of use

But the same principles do not apply to liabilities incurred under LNG COU, because, as noted above, of the magnitude of the potential liabilities involved and the extremely onerous terms which these COU often contain. Indemnities in contracts relating to the use of LNG terminals are only poolable to the extent that the liabilities meet a set of requirements set out in the Pooling Agreement and would not have arisen if a limit and indemnity provisions in accordance with those requirements had been incorporated in the contract.

Those requirements are as follows:

1.

i) The contract must be subject to a statutory limit (or if there is no such limit or it is waived) a contractual limit not exceeding US$150 million or a limit equivalent to that specified under the 1976 Limitation Convention and any applicable revisions, amendments or protocols.

ii) That limit must:

a) Not be conditional on the performance of insurance or other obligations "which cannot reasonably be expected of an Insured Owner entered for full P&I cover, and complying with the terms and conditions of his entry in an Association in the International Group", and

b) Where a contractual limit exists, encompass all the liabilities arising under the COU from one event

iii) Unless on knock-for-knock terms, the indemnity provisions must exclude the Insured Owner from liability arising from the sole negligence of the party being indemnified.

2. Notwithstanding the above, if the contract does not comply with 1(ii)(b) and 1(iii) above in respect of wreck removal and crew liabilities, those liabilities shall nevertheless be eligible for pooling if the Association determines that best endeavours have been exercised to ensure that contract does so comply.

The Club is often asked to approve cover for LNG COU and we do so against these guidelines. We have a team of dedicated contract review specialists that routinely review these COU so that any gaps in cover are identified at an early stage and additional covers arranged before the vessel calls at the port.

In reviewing these contracts we consider a variety of factors, including the parties involved and their respective roles, the extent of operations that fall within the ambit of the COU, liability and indemnity for loss or damage to the crew, vessel and cargo, any indemnity for loss or damage to a third party and liability for wreck removal amongst other things.

It is usually the case that the form and content of COU have many common features based around geography. For example, there tends to be similar styles of drafting in terminal COU across China, whereas terminals in the USA have their own particular form and structure including additional notification requirements in some cases. Japanese buyers and terminals tend to draw up a multiparty agreement including buyers, sellers and shipowner, often referred to as a SSLA that allocates liability during the vessel's operations while in port.

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Key points

Below please find some key points to remember when reviewing LNG COU:

- The criteria referred to above relates to indemnities in contracts relating to the use of LNG terminals and not LNG ships. A tanker calling a multi-cargo facility which also imports / exports LNG may be exposed to the same requirements as that of an LNG tanker
- While Members are required to exercise best endeavours for indemnities related to loss or damage to the crew and wreck removal, failure to incorporate a knock for knock apportionment of liability, or in the absence of a knock for knock apportionment of liability, an exception for the sole negligence of the terminal for all other P&I related risks would render the COU non-poolable, thus requiring additional cover
- In the event that the contract does not contain any contractual or statutory limit, and/or does not include indemnities that are on a knock-for-knock basis or contain an exception for the terminal's sole negligence, additional cover would respond up to $US150 million per event. However, mutual Club cover would be available up to $US150 million where the claim is caused partly by the shipowner (i.e. in that case any additional cover would operate as an excess)
- A condition of use (COU) can also referred to as a port liability agreement (PLA), marine liability agreement (MLA), ship shore liability agreement (SSLA) or is sometimes simply included in the terminal manual
- It is not necessary that every LNG facility should have a COU or similar document. Absent a COU, liability is usually allocated as per local law and is acceptable from a pooling perspective
- Some ports and terminals which have multiple operators sometimes issue two COU to the ship, one by the port and another from the terminal at which the vessel is alongside. So long as the terms of the two contracts meet the requirements of the IG pooling guidelines, mutual cover would respond to liabilities incurred under the terms of those COU
- FSRU's are for all practical purposes treated as a terminal. A COU issued by the FSRU to an incoming vessel is covered under the Club rules, provided the COU meets the requirements of the IG Pooling Agreement as set out above.

Your Club is here to help

The conditions of use for LNG terminals pose unique challenges in their assessment for the purposes of ensuring that the operator has sufficient cover in place, with geographically disparate terminals having their own COU structure and content. The Club is familiar with these different contracts and our specialist team can provide Members with a quick and comprehensive review to ensure certainty of cover, as well as arranging additional cover where that may be necessary.

WEST

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