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Who pays if it doesn't go to plan?

Regular columnist Simon Tatham takes a look at how changing circumstances can be costly for salvage firms, especially if salvage or wreck removal contracts are not absolutely watertight at the start of any operation

► *Simon Tatham*

Risk versus reward is key to the likely profitability – or, in a tough market, the viability – of a proposed contract. Operation costs can largely be predicted and then balanced against income to generate a potential margin. However, what happens when circumstances change adversely? Who then bears the risk? This article looks at the allocation of risk and change of material circumstances provisions in some of the industry's main contracts, including wreck removal agreements.

In long-term master contracts, typically applying terms based around Supplytime, the focus during negotiations centres upon the allocation of risk arising from unpredictable changes – for example, changes in local tax laws or regulations adversely affecting tug operation costs.

If agreed, these are catered for by an adjustment of hire provision with the ultimate sanction being arbitration. Changes within the control of the hirer are more easily dealt with, requiring perhaps a change order to be agreed in writing.

This at least allows the operator to negotiate price down the line when a working relationship has been established with the client's operations team, rather than having to deal again with the more hard-nosed procurement team.

In shorter term contracts such as Towcon, where the services are from port to port with a greater risk of the unknown occurring, the standard allocation of risk provisions throw the additional costs of local taxes and licences on to the hirer along with replacement of broken towing gear. Salvage opportunity is limited due to the obligation to attempt to reconnect in the event of line breakage.

More serious threats to the tow, which might give rise to a potential salvage claim for services outside the contemplated scope of the towage contract allowed under the standard wording (assuming English law applies), are often barred by the hirer's insistence of a no-salvage claim provision.

This can backfire on the hirer as that would not prevent the contractor from engaging independent salvors under clause 21(b) if he considers that he has little to gain from intervening himself, although since the 2008 form was introduced he must first consult with the hirer, giving underwriters an opportunity to engage on commercial rather than no-cure no-pay terms.

A good example of what is known as a subjective change of circumstances provision is the 'necessary deviation' clause 24.

This allows the tugmaster to decide on a diversion if he reasonably considers it necessary. The costs of deviation and the delay rate are then payable by the hirer. An arbitrator will be loath to challenge that decision even if circumstances later suggest that the deviation was uncalled for.

The onus of proof would also be upon the hirer to demonstrate that the decision was unreasonable, and is a difficult one to discharge. Provided the decision was honestly and rationally made, taking into account all the circumstances at the time, the tugowner will be in the clear.

Finally, under Towcon, the tugowner has the right to terminate if a sum due under the terms of the agreement has not been paid in seven running days.

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However, it is under wreck removal contracts that change of material circumstances provisions give rise to the greatest vexation.

When BIMCO's committee drafted what are now Wreckhire, Wreckstage and Wreckfixed, the standard provisions set out a procedure catering for where, without fault on the part of the contractor, there is a substantial change in the work to be done under the agreement or in the manpower and craft and equipment required to undertake the job.

This procedure can be invoked by the contractor where there is a material change in the position and/or condition of the vessel or worksite.

Material change is not defined. The classic example is where, due to adverse weather, the vessel falls off a ledge into deep water. It is designed to cater for the unpredictable event. In effect it throws the risk of increased cost onto the shipowner rather than the salvor.

P&I Clubs that pay for wreck removal will invariably seek to delete this clause or draft the scope of the services and the method of work, personnel craft and equipment in the contract annexes in such a way as to ensure the salvor contracts to remove the wreck, come what may, thus throwing the operational and commercial risk on to the contractor.

Very often things do change and frequently there is limited opportunity for contractors to fully assess those risks at the outset where a brief visit to site and examination of provided information within the short time of a tendering process are all that is on offer.

With fierce competition at the bidding stage this can be the difference between a modest profit and a very substantial loss.

A compromise, albeit one that is seldom seen in practice, is a carve-out where certain circumstances or material changes (say a tsunami or the vessel sinking into silt beyond an agreed depth) are allowed for. Such carve-outs should protect the contractor from more disastrous events, but they need to be carefully drafted.

The clever aspect of the standard provisions of the Wreckhire, Wreckstage and Wreckfixed contracts, drawing from offshore industry practices, is the procedure.

The parties must first consult, and if the additional costs cannot be agreed the issue is put to evaluation by an independent expert for determination, the objective being that this is done swiftly.

Meanwhile, there is no right to terminate and the contractor has to continue with the job. A moot point remains as to whether he is required to commit the additional resources in advance of determination – but then you have to leave something for us lawyers to think about.

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