International Trade and Commodities Legal Update

March 2011

Contents

Introduction 2

Sale of goods

New Incoterms 2010 – a summary of the principal changes to Incoterms 2000 3

GAFTA 49 and FOB sale contract – Court of Appeal construes "readiness to load" - *Soufflet Negoce v Bunge SA* 4

Court of Appeal decision on implied terms as to quality in FOB sale contract – *The Mercini Lady* - *KG Bominflot Bunkergesellschaft fűr Mineraloele mbH & Co v Petroplus Marketing AG* 6

Litigation and arbitration

Commercial Court reviews law on breaking the chain of causation, mitigation and remoteness of damage - *Borealis AB v Geogas Trading SA* 7

Court of Appeal upholds GAFTA jurisdiction finding - *Broda Agro Trade (Cyprus) Ltd v Alfred C Toepfer International GmbH* 8

The *Fiona Trust* litigation and the Bribery Act 2010 10

Stringent requirements apply where a party seeks security for the amount awarded in arbitration pending an appeal to the court - *A v B* 11

Commercial

Court of Appeal clarifies and restates test for repudiatory breach of contract - *Eminence Property Developments Ltd v Kevin Christopher Heaney* 12

Iranian Trade Sanctions - an update 14

Contacts 19

Introduction

This is the third issue of our re-launched International Trade and Commodities Legal Update and we hope you find its contents informative and interesting. Once again, we have focused on recent English court decisions (a fair number of them Court of Appeal decisions) and international trade developments that will be relevant to our readers.

The new Incoterms 2010 came into force at the beginning of this year. Our article on the new Rules summarises the principal changes to Incoterms 2000. Of particular interest is that the "ship's rail" as the point at which risk passes in FOB, CFR and CIF sales has now been replaced with the goods being delivered when they are placed "on board" the vessel. Additionally, certain terms have been deleted and replaced with other terms: DAF, DES and DDU have been replaced by DAP (Delivered at Place) and DEQ (Delivered ex Quay) has been replaced by DAT (Delivered at Terminal).

Our article on the Court of Appeal decision in *The Mercini Lady* follows on from our article on the first instance decision in the February 2010 Legal Update. The Court of Appeal has allowed the seller's appeal and held that there is no implied term in a sale contract that goods will remain "on spec" for any time after loading – and thus if the cargo meets the spec on loading (or is deemed to be on spec by virtue of a certificate final provision) the seller's obligation with regard to quality will have been met. This may not be the final word, however, as it has been reported that this case might go to the Supreme Court on appeal.

In another Court of Appeal decision, *Soufflet Negoce v Bunge SA*, the Appeal judges construed "readiness to load" in a sale contract in GAFTA 49 form with amendments. They agreed with the GAFTA Appeal Board and the first instance judge that the sellers were in breach of contract for non-delivery of goods. The fact that the vessel's holds may have needed some cleaning on arrival did not mean that the sellers could terminate the sale contract on the basis that no vessel had arrived during the period fixed for delivery.

Borealis AB v Geogas Trading provides a useful review of the law relating to recovery of damages, including when an innocent party's actions will be considered to have broken the "link" or chain of causation between the contract breaker's conduct and the loss or damage that is sustained.

In *Eminence Property Developments v Heaney*, the Court of Appeal made it clear that an innocent mistake by a party to a contract will not automatically result in a finding of repudiatory breach of contract against it. Deciding which party breached a contract first can be quite tricky under English law and it is not unknown for one party to try and "set up" the other party. Great care also has to be taken that a party is not premature in holding its counter-party in repudiatory breach, terminating the contract as a result and then finding that it has placed itself in repudiatory breach.

This Legal Update also covers a few decisions relating to jurisdiction and procedural points. In the October 2010 issue, we covered the first instance decision in *Broda Agro Trade v Alfred Toepfer*. This issue contains an article on the Court of Appeal decision in that case, which upheld the GAFTA jurisdiction finding and the decision of the lower court. This case highlights to international traders the importance of getting early legal advice on English law, including on procedure and applicable time limits, when faced with a commercial dispute that is subject to English law.

A v B was an Ince & Co case involving an application to the court for security for the amounts awarded in FOSFA arbitration pending an appeal from the FOSFA arbitration awards to the court. The Commercial Court made it clear that such security (unlike applications for security for costs which are made frequently and are often successful) will only rarely be ordered.

Although implementation of the Bribery Act 2010 is now delayed beyond its original implementation date of April 2011, our article on the *Fiona Trust* litigation and the Bribery Act remains topical because the Act is nonetheless likely to come into force later on this year. For a more general and detailed review of the *Fiona Trust* litigation, please see the article on our website. The article in this Legal Update focuses on the distinction between the civil law concept of bribery and the criminal offences contained in the Act.

Finally, we include with this Legal Update a copy of our latest Update on Iranian trade sanctions, which will be of interest to the trade, shipping and insurance sectors. The Sanctions Update covers among other things the EU Sanctions Regulation of 27 July 2010 and discusses its implications.

We would welcome your feedback on this publication. Please let myself, your usual contact at Ince & Co or our marketing department know if you have any comments or suggestions.

Stuart Shepherd
Partner, London
stuart.shepherd@incelaw.com

Sale of goods

New Incoterms 2010 – a summary of the principal changes to Incoterms 2000

Introduction

On 1 January 2011, the ICC's Incoterms 2010 came into force. These are the eighth revision of the Incoterm Rules, with the last revision dating back to 2000. The new Rules have been revised to take into account developments in international trade over the past 10 years as the volume and complexity of global sales have increased, to address security issues arising in recent times and to provide for the ongoing changes in electronic communication. The new Rules also recognise the growth of customs-free areas.

One of the principal concerns with regard to the Incoterms has been that often the wrong term is selected for use by the parties. The Introduction to the new 2010 Rules stresses the need to use the term appropriate to the goods, to the chosen means of transport and to whether or not the parties intend to impose additional obligations on the seller or buyer. In addition, there are Guidance Notes (and a diagram) at the front of each Incoterms Rule containing information to assist in making a choice on which Rule to use. We summarise below the principal changes to the 2000 version.

Reclassification of Rules

The new Rules have been separated into two classes: (i) Rules for use in relation to any mode or modes of transport, which can be used where there is no maritime transport at all or where maritime transport is used for only part of the carriage and (ii) Rules for sea and inland waterway transport, where the point of delivery and the place to which the goods are carried to the buyer are both ports.

FAS, FOB, CFR and CIF belong to the second class of Rules. In respect of FOB, CFR and CIF, reference to the "ship's rail" has now been deleted and this has been replaced with the goods being delivered when they are "on board" the vessel.

Rules apply to domestic as well as international trade

The Incoterms have traditionally been used for international sale contracts even though some trade blocs, such as the European Union, have minimised the significance of border formalities. The new Rules now recognize that they can also be used for domestic sale contracts and reference is made in a number of the Rules that export and import formalities will only need to be complied with where applicable. It is anticipated that this change may encourage greater use of the Rules in the USA in place of the former US Uniform Commercial Code.

Two new terms replace four previous terms

Incoterms 2000 contained 13 Rules, which have been reduced to 11 terms in Incoterms 2010. This has been achieved by introducing two new Rules to replace four current Rules. The two new Rules may be used irrespective of the mode of transport selected and under both new Rules, delivery takes place at a named destination. In essence, the "D" (Delivered) terms under the 2000 Rules have been consolidated to reduce the number of terms that were considered to have little real difference between them.

DAT (Delivered at Terminal) replaces DEQ (Delivered ex Quay). DAT may be used irrespective of the mode of transport selected and may also be used where more than one mode of transport is employed. "Delivered at Terminal" means that the seller delivers when the goods, having been unloaded from the arriving means of transport, are placed at the buyer's disposal at a named terminal at the named port or place of destination. DAT requires the seller to clear the goods for export where applicable but the seller has no obligation to clear the goods for import, pay any import duty or carry out any import customs formalities. It was considered that DAT would prove more useful than DEQ in the case of containers that might be unloaded and then loaded into a container stack at the terminal, awaiting shipment. There was previously no term clearly dealing with containers that were not at the buyer's premises.

DAP (Delivered at Place) replaces DAF, DES and DDU. The arriving "vehicle" under DAP could be a ship and the named place of destination could be a port. Consequently, the ICC considered that DAP could safely be used instead of DES and that it would make the Rules more "user-friendly" if they abolished terms that were fundamentally the same. Again, a seller under DAP bears all the costs (other than any import clearance costs) and risks involved in bringing the goods to the named destination.

String sales

Commodities are often sold several times over before or during transit through a string of sale contracts. There will therefore be more than one seller and only the first seller will have been responsible for shipping the goods. The new Rules have been amended to reflect this. For example, CIF and CFR now refer to an obligation to "contract or procure a contract for the carriage of the goods..."

Terminal handling charges

Under certain Incoterms 2000 Rules (e.g. CIF/CFR), the buyer potentially faced paying for the same service twice. The seller was including freight costs as part of the sale price, yet the buyer was sometimes expected by the carrier or terminal operator to pay the costs of handling and moving the goods within the port or container terminal facilities. Incoterms 2010 seek to avoid this potential double exposure by clearly allocating such costs under the relevant Rules.

Insurance cover and security related clearances

The new Rules take into account the 2009 revision of the Institute Cargo Clauses and expressly provide for information duties relating to insurance. They also allocate obligations between the buyer and seller in respect of obtaining or assisting in obtaining security-related clearances for the goods in question.

Electronic communication

The previous Rules provided for the use of Electronic data interchange (EDI) messages, where the parties had agreed to use them. Given the evolution of new electronic procedures and the likelihood that such procedures will continue to evolve, Incoterms 2010 provide instead for the use of paper communications or "equivalent electronic record or procedure" where agreed or customary.

Application of Incoterms 2010

As with the previous versions of Incoterms, if parties wish the Incoterms 2010 to apply to their sale contract, they should expressly provide for this in the contract. "Incoterms 2010" rather than just "Incoterms" should be referred to in the sale contract if it is the intention to incorporate the latest version, so as to avoid any subsequent dispute as to which set of Rules applies. If the parties wish to incorporate a specific Rule from Incoterms 2000, or all of Incoterms 2000, again, they should make specific reference to this in the contractual document.

Stuart Shepherd
Partner, London
stuart.shepherd@incelaw.com

Ted Graham
Partner, London
ted.graham@incelaw.com

GAFTA 49 and FOB sale contract – Court of Appeal construes "readiness to load"

Soufflet Negoce v Bunge SA. [2010] EWCA Civ 1102

In a classic FOB sale contract, the risk of loss or damage to the goods passes from the sellers to the buyers on the loading of the goods onto the vessel. The sellers will have no real interest in what happens after that, particularly where the sale contract provides for weight, quality and condition of the cargo to be final at the load port as per surveyors' certificates (and assuming there is no issue as to security of payment). In this dispute, the sellers argued that they had been entitled to refuse to load the cargo of Ukrainian feed barley onto the buyers' nominated vessel because the cargo holds were allegedly not fit to receive or carry the cargo due to coal residue. The matter went through the GAFTA arbitration procedure and then to the courts, right up to the Court of Appeal, where the sellers lost.

Background

The sale contract provided for delivery to be "*between 9th - 22nd October 2006 at Buyers' call both dates included (no extension)*". It was also agreed that weight, quality and condition were to be final at load port as per surveyors' certificates "*sellers' option and costs*". All other terms and conditions not inconsistent with the sale contract were to be "*as per GAFTA 49*" (standard form of GAFTA contract for delivery of goods from Eastern Europe in bulk or bags on FOB terms). Clause 6 of GAFTA 49 provides that "*the sellers shall have the goods ready to be delivered to the buyers at any time within the contract period of delivery...... provided the vessel is presented at the loading port in readiness to load within the delivery period, sellers shall if necessary complete loading after the delivery period...*".

The sale contract also contained "*shipping terms*" which included laytime and demurrage provisions expressly requiring a valid tender of a notice of readiness (NOR) and stating "*all other terms and conditions as per relevant c/p*".

NOR was not given until 0520 hrs on 22 October, which meant that the buyers required the sellers to complete loading after the delivery period had expired. However, the sellers' surveyors issued a certificate on that same day saying the vessel's holds were not fit to receive and carry the cargo due to coal residue (the buyers' surveyors had meanwhile issued a certificate of cleanliness). The next morning, the Master advised that the vessel's holds were ready for re-inspection. By that time, the sellers had already declared the buyers

in default of the sale contract on the grounds that the vessel had not been presented ready to load within the delivery period. The buyers sued the sellers for damages for non-delivery of the goods.

GAFTA arbitration proceedings

The first-tier GAFTA tribunal found in favour of the sellers but that decision was reversed by the GAFTA Board of Appeal. The Appeal Board said it was the buyers' responsibility to provide a vessel for shipment within the time agreed at the place agreed for shipment but that *"as long as it was physically and legally possible for sellers to load, on the nominated ship, the agreed goods at the agreed place within the agreed time, then buyers would have discharged that responsibility and sellers were under a duty to load"*.

On appeal to the Court

Mr Justice David Steel dismissed the sellers' appeal but gave them leave to appeal to the Court of Appeal because GAFTA 49 is commonly used in the grain market and its construction was considered to be of general interest for grain traders.

The Court of Appeal dismissed the appeal. The appeal judges distinguished NOR within a charterparty/shipping context from *"readiness to load"* in an FOB sale contract. *"Readiness to load"* did not mean a valid NOR must have been given or must have been capable of being given by the ship-owners, because that was not what GAFTA 49 said. Rather, the reference in the shipping terms of the sale contract to an NOR being given was only relevant in relation to the commencement of laytime.

According to Lord Justice Longmore, all that had to happen within the delivery period was that the vessel had to be presented in readiness to load at some time between 00.01 hours on 9 and 24.00 hours on 22 October. The fact that the holds may have needed some cleaning on arrival did not mean that the sellers could terminate the sale contract on the basis that no vessel had arrived during the period fixed for delivery. Lord Justice Toulson highlighted the fact that this was not a demurrage dispute (where, under the sale contract, the sellers would not be liable for demurrage unless a valid NOR had been tendered) but rather a simple claim under the contract for failure to load by the shipment date.

Comment

This is another in a number of recent cases which have gone on appeal to the courts from commodity arbitrations but the appeals have been dismissed.

Here, the Court of Appeal upheld the GAFTA Board of Appeal's analysis of the "fundamental commercial dynamic" of an FOB sale, which meant that if goods were damaged by shipment into unclean holds, the shipment was the buyers' decision and at their risk.

Daniel Jones
Partner, Hamburg
daniel.jones@incelaw.com

Reema Shour
Professional Support Lawyer, London
reema.shour@incelaw.com

Court of Appeal decision on implied terms as to quality in FOB sale contract – *The Mercini Lady*

KG Bominflot Bunkergesellschaft fűr Mineraloele mbH & Co v Petroplus Marketing AG (The Mercini Lady) [2010] EWCA Civ 1145

The dispute

KG Bominflot were the FOB Buyers of a cargo of gas oil from Petroplus. Although the load port inspector found that the *"Total sediment"* was within the contractual specification limits at the load port, Bominflot were more than a little put out when four days later, following an unremarkable voyage, the cargo failed the sediment test at the discharge port and was rejected by their receivers. Bominflot claimed in excess of US$3 million from Petroplus, for the difference in the value of the cargo, freight and other consequential losses.

The Commercial Court decision

The parties agreed that it might save them both time and costs to have the Commercial Court decide various questions by way of preliminary issue as opposed to having a full trial. As often happens, this best of intentions probably had quite the opposite effect. Nevertheless, as we reported in our February International Trade Update, this resulted in some interesting questions being posed to Mr Justice Field. In a nutshell, at first instance the Judge decided that a term should be implied into the original FOB contract that the goods would be of satisfactory quality, not only when delivered onto the vessel but also for a reasonable time thereafter. The Judge found that it was appropriate for terms to be implied both at common law and under Section 14 of the Sale of Goods Act 1979 and that the absence of a reference to *"conditions"* in the express exclusion clause failed to stop such terms being incorporated. The Sellers appealed.

The Court of Appeal decision

Lord Justice Rix gave the judgment of the Court. Running through the judgment, there appears to be a slight expression of frustration on the Judge's part that the case came to Court as an appeal on preliminary issues rather than following a trial and with an explanation as to how the sediment in a cargo of gas oil could change from within specification to off specification after an unremarkable four day voyage. It was common ground between the parties that the load port inspection was not invalid as a result of *"fraud or manifest error"* (both of which would have prevented its finding being final and binding) and no point was taken in this case by the Buyers about the fact that the load port inspectors did not use the contractual test method. Further, the Buyers made it clear that they did not allege that the cargo was off spec at the time of delivery. However, as indicated above, Field J had held that the contract contained an implied term that the goods should have been *"capable of remaining"* within specification and/or of satisfactory quality during the voyage and for a reasonable time thereafter. Both Courts recognised the difficulties this posed, particularly in FOB sales, where frequently the Seller has no idea how long the intended voyage for the cargo is.

Rix LJ found it impossible to see how a cargo of gas oil which was admitted to be within specification on loading and delivery could nevertheless be delivered in breach of contract in a matter going to its specification. He found that the implied statutory condition of satisfactory quality arising from Section 14 of the 1979 Act applied only at the time of delivery and not thereafter although it may well be that whether or not the goods have a reasonable *"durability"* is part and parcel of determining whether or not they are of satisfactory quality.

Rix LJ disagreed with Field J that a further term should be implied into the contract at common law to the effect that the goods should *"remain on specification for a reasonable time after delivery"*. As his Lordship pointed out, to find otherwise would effectively remove any certainty enjoyed by a seller who has agreed a final and binding inspection clause with his buyer. In making this finding, he recognised that there may be cases where a cargo has a latent inherent vice which could not have been picked up by the quality inspection. Field J had, for his part, also recognised that the load port inspection was only final and binding as to matters actually found, and there was nothing in the Court of Appeal judgment to suggest that this was wrong.

The second question related to the contractual exclusion clause in the contract. This said that the contract contained *"no guarantees, warranties or misrepresentations, express or implied,* [of] *merchantability, fitness or suitability of the oil for any particular purpose or otherwise…"*. Rix LJ clearly had some sympathy with the Sellers' argument that most people reading this would assume that the parties had intended to exclude implied terms regarding *"merchantability, fitness or suitability"*. Nevertheless, in one of those *"hard cases"* decided for the benefit of certainty of English law, he agreed that he was bound by the same long line of authority as Field J. Since the exclusion clause does not specifically exclude

"conditions" and since the implied terms of the Sale of Goods Act are conditions, the clause did not operate so as to exclude the Act. Equally, there was nothing in the specification clause and the inspection clause which was inconsistent with implication of the statutory conditions.

Comment

The Court of Appeal judgment is a reminder to traders of the crucial importance of the correct drafting of exclusion clauses. It has also shut the door that was opened by the first instance decision on possible arguments that cargoes delivered "on spec" but arriving "off spec" may have breached an implied term that they would remain on spec for a *"reasonable period"* (however long that might be).

Ted Graham
Partner, London
ted.graham@incelaw.com

Scarlett Henwood
Solicitor, London
scarlett.henwood@incelaw.com

Litigation and arbitration

Commercial Court reviews law on breaking the chain of causation, mitigation and remoteness of damage.

Borealis AB v Geogas Trading SA [2010] EWHC 2789 (Comm)

The Dispute

G sold a cargo of butane to B to be used as feedstock by B in its plastics production plant. The butane was contaminated with fluorides, which cracked during processing to form hydrofluoric acid, which in turn triggered a pH alarm at the plant. B took no action in response to the alarm. The acid in the system caused substantial physical damage to the plant, in particular corrosion to the heat exchangers, causing a gas leakage. Production time was lost in the immediate aftermath whilst damaged parts were refitted and at further times during the following year. B claimed loss of profits from plant down time.

G admitted that the contaminated butane was not fit for its purpose and that it had breached the supply contract. However, G argued that its breach did not cause B's loss. Rather, it contended that B's actions (or inactions) in failing to respond to the pH alarm, investigate the problem and take steps to prevent the damage, broke the chain of causation, such that the loss suffered was actually caused by B's own failures, rather than G's breach. Alternatively, on the same facts, G argued that there was a failure by B to mitigate its losses and that those losses were consequently not recoverable.

The Commercial Court decision

Causation

Under English law, establishing causation is a question of fact, involving a practical enquiry into the effect of the breach and the innocent party's subsequent conduct, including the innocent party's state of knowledge. Generally, the innocent party would be given the "benefit of the doubt". To break the chain of causation, the innocent party's actions would have to have been such as to *obliterate* the effects of the original breach. This is a high standard. If the breach remained *an effective cause*, the chain is unlikely to be broken. Unreasonable conduct on the part of the innocent party is unlikely to be sufficient to break the chain of causation, it would probably need to have behaved recklessly.

In this particular case, B's failure to react to the alarm was criticised by the Judge. However, he noted that the purpose of the alarm was not to detect the presence of contaminants in feedstock. Furthermore, on the evidence, B had no knowledge of, or reason to suspect, the presence of fluorides in the cargo. Therefore, even if with hindsight B might have done more, the Judge concluded that B's actions at the time did not obliterate the effect of the original breach by G and break the chain of causation.

Remoteness of damage

The Judge also held that B's losses were not too remote. His view was that they were losses of a type that could be expected, even those claimed for down time a year after the original breach – remoteness in time was not determinative of remoteness of damage in law. The Judge said that it was "perfectly likely" that production would be lost whilst B had equipment inspected and replaced.

Mitigation

Finally, just as the Judge considered that B's conduct did not break the chain of causation, he also found that B had not failed to mitigate its losses such that they were the "authors" of the loss. Rather, the Judge commented that whilst it is often easy, after an emergency, to criticise the steps which have been taken to meet it, such criticism does not come well from those who have themselves created the emergency.

Comment

This case sets a high burden where a contract breaker wishes to argue that it should be relieved of liability because the innocent party's actions broke the chain of causation. The Judge held that the innocent party's actions must "obliterate" the effect of the original cause of the loss. It should be noted, however, that the test is likely to be different where it is claimed that the actions of a third party, or the occurrence of an extraneous event, broke the chain of causation.

Will Marshall
Partner, London
will.marshall@incelaw.com

Jamila Khan
Solicitor, London
jamila.khan@incelaw.com

Court of Appeal upholds GAFTA jurisdiction finding

Broda Agro Trade (Cyprus) Ltd v Alfred C Toepfer International GmbH [2010] EWCA Civ 1100

Background

The background to this litigation arose out of a claim in GAFTA arbitration proceedings by Toepfer against Broda for alleged breach of a contract for the supply of milling wheat. Broda had initially argued that there was no validly concluded contract between Toepfer and themselves for the supply of milling wheat, so that they were not bound by the GAFTA arbitration clause in the alleged contract. The first tier GAFTA tribunal issued an Interim Award, concluding that there was a binding contract between Broda and Toepfer and that disputes thereunder were subject to GAFTA jurisdiction. Broda went on to participate in the arbitration proceedings in relation to Toepfer's claim for breach of contract and were found liable by the GAFTA tribunal in its Final Award on liability and ordered to pay damages.

In addition to appealing to the GAFTA Board of Appeal to set aside the Final Award on liability, Broda also sought relief from the Commercial Court under sections 72 and 67 of the Arbitration Act 1996. Section 72 allows a person to seek a declaration that an arbitral tribunal lacks jurisdiction but it can only be relied upon by a person who has taken no part in the arbitration proceedings. Section 67 allows a person to seek to set aside an arbitration award on the grounds of the tribunal's lack of jurisdiction but, pursuant to section 70(3) of the Arbitration Act 1996, an application under section 67 must be made within 28 days from the award and Broda were well out of that time-frame (by about 14 months) in making their application. They therefore sought an extension of time from the Court under section 80(5) of the Arbitration Act 1996 to apply for relief under section 67.

Mr Justice Teare in the Commercial Court dismissed Broda's claims. He held that Broda had taken part in the arbitration proceedings and could not therefore seek relief under section 72. He also refused to exercise his discretion to grant Broda an extension of time to make their section 67 application. However, he granted Broda permission to appeal.

The Court of Appeal decision

The Court of Appeal has dismissed Broda's appeal. Lord Justice Stanley Burton gave the leading judgment and his reasons for dismissing the appeal can be summarised as follows.

Application under section 72 of the Arbitration Act 1996

In the Commercial Court, the Judge had held that Broda had taken no part in the arbitration proceedings leading up to the tribunal's Interim Award on Jurisdiction but they had participated in the arbitration proceedings on the merits (i.e. the substantive proceedings relating to alleged breach of the contract). In Mr Justice Teare's opinion, it followed that Broda could not challenge the Interim Award under section 72.

Before the Court of Appeal, Broda argued that the reference in section 72 to a *"person who takes no part in the proceedings"* related only to participation in the proceedings relating to the tribunal's determination of its substantive jurisdiction. In other words, the fact that Broda had participated in the arbitration by defending Toepfer's claim for breach of contract should not disqualify them from relying on section 72. Significantly, there is apparently no previous case-law on this exact point.

Mr Justice Stanley Burton concluded that there was no basis to restrict the words "takes no part in the proceedings" to the proceedings relating to the determination of the substantive jurisdiction of the arbitrators. He added that a person who considers he has not entered into an arbitration agreement is entitled to ignore the arbitration proceedings and he can then claim relief from the Court afterwards under section 72 because he did not participate in those proceedings. However, where he chooses to participate in the proceedings, whether in relation to the jurisdiction of the arbitrators or in relation to the arbitrators' exercise of their substantive jurisdiction to decide the dispute on its merits, and is disappointed by the arbitrators' decision, he can then challenge the arbitration award under section 67 within the time-limit set i.e. 28 days.

Extension of time to apply to the Court under section 67 of the Arbitration Act 1996

The Court of Appeal had to consider whether Mr Justice Teare had erred in the exercise of his discretion by refusing to extend time for Broda's application under section 67. The appeal judges concluded that he had not. In the words of Mr Justice Stanley Burton, *"indeed, it is difficult to see the practical point of a time limit if an extension as long as that required in the present case should be given to a commercial organisation such as Broda, which, faced with a very substantial claim in London, did not see fit to consult an English lawyer"*. This was in reference to the fact that Broda had apparently relied on Russian lawyers to advise them and on Cypriot lawyers to check documents drafted by the Russian lawyers for errors of grammar and syntax, to sign the documents and send them to GAFTA. English lawyers were not instructed until five months after the GAFTA tribunal's Final Award on liability. Mr Justice Teare's refusal to extend time to Broda was therefore upheld.

Comment

The Court of Appeal's decision serves as a stark warning to international traders who are faced with a commercial dispute that may be governed by English law to get English legal advice early in the day, particularly with regard to (i) applicable time limits and (ii) procedural requirements, as well as on the merits of the substantive dispute.

Max Cross
Partner, Hong Kong
max.cross@incelaw.com

Reema Shour
Professional Support Lawyer, London
reema.shour@incelaw.com

The *Fiona Trust* litigation and the Bribery Act 2010

Fiona Trust & Holding Corporation and others v Privalov and others [2010] EWHC 3199 (Comm)

Anyone considering a civil claim for corruption or fraud will need to consider the impact of the Bribery Act 2010 ('the Act') and of the *Fiona Trust* decision. In fact, the judgment in *Fiona Trust* provides a timely illustration of the distinction between the civil law concept of bribery and the criminal offences contained in the Act. Parties will need to keep a weather eye on its provisions, although the Act will not now come into force in April 2011 (but instead, three months after the publication of the delayed government guidelines on anti-bribery procedures) and as the discussion below shows, its impact on civil claims is likely to be minimal. Conversely, the civil law is unlikely to provide any significant pointers as to how the Bribery Act might be applied.

The key mischief, which both the civil and criminal law address, is the conflict between the interests of a principal and the interests of his agent where a third party makes an undisclosed payment (or confers a benefit, and reference to payment or payor below includes the conferring of benefits) to the agent personally. Under the Act, the intention of the payer as to the expected behaviour of the agent will be critical; for there to be an offence, the payer must intend to induce or reward *improper performance* of the agent's functions.

However, as the cases cited in *Fiona Trust* establish, in civil law an entirely "innocent" payment may have the same consequences as one made dishonestly. It is enough that a payment to an agent creates a potential conflict of interest between the agent's fiduciary duties to his principal, and his own interests. Because the principal is entitled to the undivided loyalty of his agent, the fact of the payment is enough to entitle the principal to set aside transactions the agent arranges between the principal and the payer, and the payment to be characterised as a "bribe" even if the payer and agent were entirely innocent of any dishonest intent, and both saw the payment as entirely innocuous; there is a presumption that the payment is influenced the payee's conduct. (See e.g. *Ross River v. Cambridge City Football Club Limited*).

In the *Fiona Trust* litigation (as explained in our article on that decision in our January 2011 Shipping e-brief and also on our website at www.incelaw.com), the Claimants alleged that companies in the Sovcomflot group had entered into a series of disadvantageous and uncommercial transactions as a result of a dishonest conspiracy between Mr Dimitri Skarga, Sovcomflot's Director-General, and Mr Yuri Nikitin, the alter ego of the Standard Maritime group of companies. It was alleged that Mr Nikitin paid bribes to Mr Skarga and that those bribes evidenced dishonesty and the existence of a conspiracy. The benefits (which the Judge found as a fact to have been proved) took the form of payments to Mr Skarga by Mr Nikitin for holidays, and the provision to Mr Skarga of a credit card serviced by one of Mr Nikitin's companies. The benefits were delivered in various jurisdictions, raising the question of the applicable law.

Under the Act, considerations as to local law are of very limited relevance. The Act gives the UK Courts jurisdiction over payments made anywhere in the world if those payments would constitute bribes under the Act and the person concerned had a 'close connection' (as defined) with the UK.

However, in civil cases the applicable law will remain a primary consideration. In *Fiona Trust*, the Judge decided the alleged bribes were governed by Russian law. This made a significant difference because, as the Judge found, Russian law does not contain any presumption that the payment of a bribe would influence conduct. Rather, under Russian law, a claimant would have to show a causal connection between the payment and the transaction complained of. Such differences between English law and that of other jurisdictions in cases will continue to have a significant impact on civil cases involving cross-border corruption.

Despite his finding as to the applicable law, the Judge went on to address the question whether under English law the benefits provided by Mr Nikitin constituted bribes and, in particular, the arguments raised by the Defendants as to, first, the recipient's expectations and, secondly, the recipient's capacity.

As to the first point, the Defendants argued that Mr Skarga was *"accustomed to receiving generous hospitality in the course of [his] work and so the less likely to be impressed by such hospitality"*, and that against that background, the holidays provided were of insufficient value to create a real risk of a conflict of interest. While the Judge accepted that Mr Skarga's expectations were a relevant consideration, he went on to hold that the provision of holidays was capable of giving rise to a conflict of interest and therefore, in English law, to constitute a bribe.

Secondly, the Defendants argued that the benefits conferred were simply a continuation of benefits provided by Mr Nikitin on a friendly basis before Mr Skarga took up his post with Sovcomflot. In

other words, they were not made to Mr Skarga in his capacity as employee of Sovcomflot and therefore not made to an agent "as such". The Judge accepted that under English law, a payment has to be made to an agent "as such" and further accepted that the provision of neither the holidays nor the credit card were because of Mr Skarga's appointment or position. Even so, the Judge held, these benefits still created a conflict of interest and infringed the "inflexible" equitable rule against such payments in the absence of full disclosure – i.e. disclosure not only of the benefit itself but to the source. It was enough that Mr Skarga was a fiduciary and in a position to profit personally.

Neither of these points are likely to feature in prosecutions under the Act. In considering hospitality payments, what will be relevant, if anything, will not be the recipient's subjective experience or expectations but first, the payer's intentions (as outlined above), and, perhaps (this remaining untested) objective industry norms as to what entertainment or hospitality is reasonable and proportionate. Similarly nice considerations as to the capacity in which the payee receives a benefit are likely at most to be a sideshow to the focus on the payer's intention.

While the Judge's approach in *Fiona Trust* opens up the possibility of a wider ranging enquiry in civil cases, the decision at the same time suggests that the impact of such points will be limited, as the Courts will be quick to identify the potential for a conflict of interest, which will trump questions of the recipient's expectations or capacity.

Having reached the conclusion that, in English law, the holidays and credit card constituted bribes, the Judge found that there was no necessary causal link between those benefits and the transactions complained of, as required by Russian law. In contrast, as explained above, under English law, *the fact* of the bribes would be enough to entitle a claimant to set aside the transactions arranged by the agent. Here, at least, the Act does parallel the civil law in that the criminal offence lies in providing (or accepting) an advantage intending to procure improper performance, and it is irrelevant whether the briber achieves his objective.

Andrew Ottley
Partner, London
andrew.ottley@incelaw.com

Stuart Shepherd
Partner, London
stuart.shepherd@incelaw.com

Stringent requirements apply where a party seeks security for the amount awarded in arbitration pending an appeal to the court

A v B [2010] EWHC 3302 (Comm)

Background

This case came before the Commercial Court on appeal from two FOSFA arbitration awards. The awards were made in respect of disputes relating to two contracts for the sale of Kazakh rapeseed that were allegedly entered into by A as the sellers and B as the buyers. The rapeseed was not delivered and B claimed damages for non-delivery. A argued that no binding contracts had been concluded and that consequently, the FOSFA tribunal had no jurisdiction in respect of the dispute. The matter went from the FOSFA First Tier arbitrators to the FOSFA Board of Appeal, which found that the arbitrators did in fact have jurisdiction, that binding contracts had been concluded and that B's claim for damages succeeded.

A applied to the Court to challenge these awards on the alternative grounds that the arbitrators had no jurisdiction and / or that they had made an error of law. B sought and obtained security for their costs of opposing A's application to the Court challenging the FOSFA Tribunal's jurisdiction. However, B also applied to the Court, seeking security for the sums that had been awarded to them by the FOSFA Board of Appeal by way of damages.

The legal issue

The issue for the Commercial Court was to clarify the circumstances in which the Court can or should order the amount awarded to the successful claimant in an arbitration to be secured by the respondent pending the respondent's challenge to the tribunal's jurisdiction or its application for permission to appeal a question of law.

Section 70(7) of the Arbitration Act 1996 (the "Act") provides that, in the event of a challenge to an arbitration award, the Court may order that any money payable under the award is to be brought into Court or otherwise secured, pending the determination of the application or appeal. However, earlier conflicting Commercial Court decisions on the issue meant that

there were differing views as to the nature and purpose of this provision and the relevant test to be applied under it.

The Commercial Court decision

Mr Justice Flaux highlighted the fact that, in challenging the arbitrators' jurisdiction, the applicant argues that the arbitration award has no presumptive validity and that it has only participated in the arbitration under protest, whilst reserving its position as to the tribunal's jurisdiction. Consequently, there must be a complete rehearing on appeal rather than a mere review of the tribunal's decision.

In those circumstances, he concurred with the view of Mr Justice Tomlinson in *Peterson Farms v. C & M Farming Ltd* [2004] 1 Lloyd's Rep 614. In that case, Mr Justice Tomlinson concluded that there is a threshold requirement under section 70(7), namely that the party seeking such security should show that the challenge to the tribunal's jurisdiction was "flimsy" or lacking in substance. Mr Justice Flaux said that this threshold requirement should apply in most cases.

Having reviewed the evidence before him, the Judge found that, in this case, the threshold requirement had not been demonstrated by B and that, on that ground alone, the application should fail. He nevertheless went on to consider what, if any, other criteria might apply in determining the issue at hand. The Judge commented that it was inadvisable and inappropriate to lay down hard and fast rules as to the circumstances in which it would be appropriate to order security under section 70(7) of the Act. However, he observed that, as a general principle, the Court should not order security in the amount awarded by the arbitrators unless the applicant can demonstrate that the challenge to the arbitration award will prejudice its ability to enforce the award, for example where the appeal might be used as a delaying tactic and lead to some risk of dissipation of the assets against which an award could be enforced. Interestingly, the Judge added that this general principle applied not only in cases where the appeal involved challenging the tribunal's jurisdiction, but also where the appeal involved (as here) an allegation that the arbitrators had made an error of law.

In this case, the Judge said that there was no evidence before him that A's applications to the Court would prejudice B's ability to enforce the award in due course. In fact, B had already obtained enforcement orders from the Court in Kazakhstan in relation to the arbitration awards against A, which orders had immediate effect. There was also no evidence before the Judge which suggested to him that A was in financial difficulties or that its assets might be diminished if the applications proceeded. He therefore dismissed B's application.

Comment

Based on this decision, it appears that the cases in which the Court will consider it appropriate to grant security under s. 70(7) are likely to be few and far between.

Stuart Shepherd
Partner, London
stuart.shepherd@incelaw.com

Jane Fitzgerald
Solicitor, London
jane.fitzgerald@incelaw.com

Commercial

Court of Appeal clarifies and restates test for repudiatory breach of contract

Eminence Property Developments Ltd v Kevin Christopher Heaney [2010] EWCA Civ 1168

The English Court of Appeal has held in this case that an innocent mistake made by a party in its grounds for declaring contracts for the sale and purchase of property to be at an end was not a repudiatory breach of contract because it did not demonstrate a clear intention by that party to abandon the contracts and/or refuse altogether to perform them.

Background to the dispute

Between the time the contracts were concluded and the time for completion, the UK property market suffered a severe downturn. The purchaser struggled to raise the capital to complete on the contracts and entered into negotiations with the vendor to try and reduce the purchase price. The negotiations failed and the day after the contractual completion date had passed, the vendor's solicitors served notices to complete on the purchaser's solicitors. However, in drafting the notices, they made a "human error" and

incorrectly calculated the final date for completion, stating that it was 15 December when, in fact, it should have been 19 December 2008. The purchaser took no steps to complete.

On 17 December, the vendor's solicitors served notices of rescission in respect of the contracts on the purchaser and sought to exercise the vendor's termination rights under the contracts, including claiming damages and retaining the deposits. On 18 December, the purchaser's solicitors wrote back, alleging that the vendor's act of rescinding the contracts amounted to a repudiatory breach of contract which was consequently accepted by the purchaser, who then elected to rescind the contracts to consider himself discharged from all obligations under the contracts. The first instance judge agreed with the purchaser. The vendor appealed.

The Court of Appeal

The Court of Appeal allowed the appeal, holding that the notices of rescission did not constitute a repudiatory breach of the contracts. In essence, the Appeal judges held as follows:

(1) The legal test for repudiatory breach is whether, looking at all the circumstances objectively from the perspective of a reasonable person standing in the position of the innocent party, the contract breaker has shown an intention to abandon and altogether refuse to perform the contract or to deprive the innocent party of a substantial part of the benefit to which he/she is entitled under the contract.

(2) The question of whether there has been a repudiatory breach is highly fact sensitive and comparison with other cases is of limited value. Therefore, the application of the legal test to the facts of a particular case may not always be easy to apply.

(3) In the present case, the vendor was willing and able to complete. Furthermore, the purchaser's solicitors knew, and a reasonable person would have realised, that the vendor's solicitors had made something similar to a clerical error. Objectively, the mistake was "*screamingly obvious*" and had it been pointed out to them, the vendor's solicitors would have acknowledged that they had made a mistake. Instead, the purchaser's solicitors chose to do nothing but wait for the opportunity to extricate their client from a bad bargain.

(4) The first instance judge had erred in focusing solely on the rescission notices issued by the vendor. Rather, all the circumstances must be taken into account insofar as they reflect on what, objectively, the vendor could be taken to have intended. In this case, the economic reality was that the downturn in the property market had made it highly advantageous for the vendor and equally disadvantageous for the buyer to perform their respective contractual obligations. Therefore, it was impossible on the facts clearly to find any intention on the part of the vendor to abandon and refuse to perform the contracts.

(5) The notices of rescission were stated to be served in accordance with the terms of the contracts and purported to exercise the vendor's remedies under those contracts. Far from seeking to repudiate the contracts, therefore, the vendor was intending to implement the contractual procedure for terminating the contracts and exercising the remedies specified in the contracts. The fact that the service of the notices of rescission was inconsistent with those contracts because it was premature did not mean that the vendor was demonstrating an intention to abandon and refuse to perform the contracts.

Comment

Contracting parties can draw some comfort from this judgment that innocent mistakes will not automatically give rise to a finding of repudiatory breach. That said, the vendor's mistake in this case was obvious. Other types of mistake may not be. Therefore, any party seeking to terminate a contract should continue to exercise extreme caution in the way it does so and should seek legal advice before taking any steps that may in due course prejudice its own position.

Elliot Woodruff
Partner, London
elliot.woodruff@incelaw.com

Chris Ward
Trainee Solicitor, London
chris.ward@incelaw.com

Iranian Trade Sanctions - an update

Introduction

In September 2010, we published a detailed overview of international trade sanctions against Iran. That overview can be accessed via our website. This article is intended to summarise the principal developments in this area since that overview, primarily with regard to the enactment by the European Union of new measures aimed at preventing the acquisition of Nuclear weapons by Iran. The latest sanctions are contained in "Council Regulation (EU) No. 961/2010 of 25 October 2010 (the 'Regulation') on restrictive measures against Iran and repealing Regulation (EC) No. 423/2007".

Background to the Regulation

On 31 August 2010, the EU published a draft of the proposed implementing Regulation to supplement the EU Council Decision of 26 July 2010 which we discussed in out last overview. As then worded, the draft provisions of the Regulation caused some concern in the shipping, trade and insurance sectors. After a consultation period involving submissions by various interested groups in those affected industries, the final version of the Regulation was passed. Below is our review of some aspects of the Regulation, with a particular emphasis on how it may affect those in the shipping, insurance and energy industry.

European Union Regulation No. 961/2010

The Regulation entered into force on 27 October 2010, the date of its publication in the Official Journal of the European Union. The Regulation states that it is binding in its entirety and directly applicable in all Member States – no further domestic legislation is required to bring it into force.

Who is subject to the Regulation?

Article 39 sets out the application of the Regulation to those with an EU nexus as follows:

"This Regulation shall apply:

a. within the territory of the Union, including its airspace;

b. on board any aircraft or any vessel under the jurisdiction of a Member State;

c. to any person inside or outside the territory of the Union who is a national of a Member State;

d. to any legal person, entity or body which is incorporated or constituted under the law of a Member State;

e. *to any legal person, entity or body in respect of any business done in whole or in part within the Union."*

Given the broad application of the Regulation, it is important that all Companies that are registered within the EU, employ EU nationals or those companies that transact business within the EU consider the scope of the latest restrictions. As such, international trade transactions which on their face appear to have no link to the EU, because for example they are between two companies based outside of the EU such as Singapore and Dubai, may be subject to the EU jurisdiction, through the employment of EU nationals involved in taking various decisions in the transaction process.

What are the aims of the Regulation?

The sanctions imposed by the Regulation are far wider in scope than those set out by the UN in the Council decision of 26 July 2010. The Regulation seeks to restrict investment in Iran and to restrict trade with Iran with a particular focus on the Iranian oil and gas industry. In addition, the Regulation sets out restrictions relating to the provision of insurance/reinsurance to Iranian entities; restricts transfers of funds from/to Iranian entities; restricts the provision of financial services and, imposes restrictions on transport. We comment on some of the key provisions below.

Shipping

Export and Import Restrictions

In the various Annexes to the Regulation, a number of items are listed which are subject to export and import restrictions. These are mainly military and dual use items as well as items that might be used for "internal repression". Care should therefore be taken if a transaction involves one of these listed items as the sale, supply, transfer or export, directly or indirectly, to any Iranian person of such items for use in Iran is prohibited. Further, participating, knowingly and intentionally, in activites the object or effect of which is to circumvent this prohibition is prohibited. A shipment of 'seals' may appear to be a legitimate cargo but dependent on the exact specifications of the 'seals' these could be prohibited listed items intended to assist the Nuclear industry in Iran.

It is worth bearing in mind that even when items which are not included in the Annexes are supplied to Iran they may be converted and used in the military industry in Iran. Although the supplier and shipper may have no specific knowledge or suspicion that this could happen at the time that the transaction takes place and

efforts may have been made to ensure that the relevant sanctions are being complied with, the possibility of negative media and commercial coverage is another factor to consider. There have already been examples where the media have shown pictures of a truck (displaying a company name/logo) adapted to carry ballistic missiles in Iran even though the vehicle was originally sent to Iran as a commercial truck. This may have a damaging impact on the commercial reputation of a company.

Parties involved in the shipment of goods that fall within the Annexes must take great care to ensure that they carry out adequate checks to identify the precise nature of the cargo and where it is intended for as well as the parties involved to avoid breaching the Regulation. In relation to some goods authorisations can be obtained from the competent authority of the relevant Member State.

Oil and Gas shipments

It has been widely reported that US legislation has targeted the refined petroleum industry in Iran and in particular has placed restrictions on the importation into Iran of refined petroleum. The EU, although targeting the Oil and Gas industry with a number of specific restrictions relating to the supply of materials to that sector has noted in the preamble to the Regulation that the restrictive measures should not prevent the import or export of oil or gas to and from Iran including payment for those goods. This demonstrates a difference between the EU and US approach in relation to the supply to Iran of Oil and gas. However, given the scope of international business with the US and payments in the US Dollar, it is important that companies still assess the impact of the US sanctions if they are considering supplying oil or gas to Iran.

Freezing of Funds and Economic Resources

Under Article 16, all funds and economic resources belonging to or held by designated individuals listed at Annex VII and VIII are frozen. In addition to this, no funds or economic resources are to be made available directly or indirectly for the benefit of those bodies or persons listed in Annex VII and VIII. This restriction is important for those involved in providing cargo to Iran especially where a third party such as an Iranian bank which has been designated in the Regulation may be listed as the consignee.

The definition of "economic resources" in the Regulation is wide so that material items which can be used to obtain funds, goods or services are classified as an economic resource. Given the wide definition of the Regulation it is important that those in the shipping industry consider all contracts and Bills of Lading to ensure that no listed person is the consignee of a cargo. A number of Iranian Banks are listed in Annexes VII and VIII of the Regulation and Iranian entities may list these as consignees under Letter of Credit arrangements. Although the cargo itself might be permitted, it is possible a document with a listed entity as the consignee could be enough to fall foul of this provision.

Restrictions on Transport

Article 27 requires that all goods being transported between the EU and Iran (significantly, not just goods that might be covered by the prohibited categories) have the requisite pre-arrival/pre-departure information so that this can be submitted to the relevant customs authorities in the Member State. Where this information provides reasonable grounds to believe the vessel in question is carrying prohibited goods, the cargo may be inspected and, if necessary, seized or disposed of (Article 28). Article 28(1) further states that EU nationals are prohibited from providing bunkering or ship supply services to vessels owned or controlled, directly or indirectly, by an Iranian person, entity or body where they have information, including information from the customs authorities, which provides reasonable grounds to believe the vessels are carrying prohibited goods.

The implementation of the EU Advance Cargo Declaration Regime on 1 January 2011 for the shipping industry provides for the submission of Cargo information to a Customs office in relation to the import or export of goods from the EU. This article does not consider the detailed provisions of this Regime but it is important that aside from the restrictions on Iran, ship operators are complying with this Customs Regime. Many shippers will already be familiar with a similar customs regime in the US. Under the Regime, the ship operator is the person liable to declare the cargo information in advance to the Customs office. As a result, the Owner and Charterers should ensure that it is clearly stated in the Charterparty or other contractual document who is going to submit the information to the relevant authorities and any allocation of liability as a result of incorrect submission of documentation. This Regime should enable the EU Customs authorities to gather the required information necessary to ensure that goods to or from Iran can be appropriately assessed and supports the provisions of the Regulation pertaining to transport.

Insurance

Article 26 of the Regulation prohibits the provision of insurance or re-insurance to Iranian companies, to a company owned or controlled by an Iranian company, to subsidiaries of Iranian companies outside Iran and to natural persons acting on behalf of such companies or entities. However, the ban does not apply to the insurance or reinsurance of vessel owners or charterers that do not appear on the EU "blacklist" (Article 26(3)). Article 26(3) also allows insurance / re-insurance to be provided to vessels which are only docking, loading, unloading or transiting "temporarily" in Iranian waters.

While many involved in the insurance industry have ceased any involvement with Iranian entities especially in the renewals of insurance policies, dangers can still arise in relation to the provision of insurance to bodies acting on behalf of an Iranian entity. It is possible that a company could be set-up in a third country which is owned entirely or by a majority Iranian entity. The risk is that the provision of insurance / re-insurance to this company could breach Article 26 of the Regulation.

The exact application of this restriction to the variety of roles active in the insurance industry is unclear. For example, there is no clear guidance on how these insurance provisions affect the role of brokers who are not actually insuring the underlying risks but placing the risk in the market. While there is little guidance from the authorities and given the wide scope of the legislation, it would be advisable to remain vigilant when looking at any insurance or reinsurance policies which are linked to Iran.

Restrictions on Transfers of Funds and on Financial Services

It is not the purpose of this update to give a detailed review of the various provisions in relation to financial transactions and investment. In broad terms, however, the new Regulation implements the financial restrictions set out in the Council Decision of 26 July 2010, which we summarised in our previous overview. It also clarifies the obligations of financial institutions in relation to record-keeping and reporting requirements regarding Iranian-related banks, as well as the opening of accounts, the establishment of correspondent or joint venture banking relationships with Iranian-related banks and the opening of new offices, branches or subsidiaries in Iran.

Restrictions are placed on the transfer of funds to and from an Iranian person, entity or body where that payment is over EUR 40,000. (Transfers below that sum must, however, still be notified to the competent authorities of the relevant Member State). To prevent circumvention, the Regulation applies to those transactions which appear to be linked and so therefore parties are unable to reduce the size of the payments under the threshold amount in order to try to avoid the sanctions. Where any payment is being received or paid to an Iranian entity the restrictions should be complied with. This could include the payment of a claim under an Insurance policy, payment of money under a Charterparty and also payments from Iranian businesses for cargo.

Further practical difficulties may be encountered when the payment is processed by a financial institution. The major financial institutions have sophisticated software to detect where payments are being made to Iran or companies associated with Iran. Although the payment may be legal under the various sanctions, delays could still be encountered while the financial institution carries out its own compliance checks. Financial institutions may even refuse the payment if they believe there is a risk that it breaches their own compliance procedures.

Energy

This update is not intended to provide a detailed analysis of the new EU Regulation in relation to the energy industry. However, the Regulation confirms restrictions on trade in key equipment and technology for, and restrictions on investment in the Iranian oil and gas industry (Articles 8 and 9). Whilst these restrictions do not apply to trade contracts concluded before the Council Decision of 26 July 2010 came into force, or to investments in Iran made before 26 July 2010, those engaging in relevant transactions or providing assistance to them will still have to notify the relevant authorities of what they are doing at least 20 working days in advance.

Is there any defence to an allegation of breach of the Regulation?

Article 32 of the Regulation provides a defence to liability where the person or body '*did not know, and had no reasonable cause to suspect, that their actions would infringe these prohibitions*.' It remains to be seen what this will mean in practice and there is, as yet, no guidance. As such, we recommend that careful checks are carried out and procedures put in place by those who are transacting business with an Iranian connection. Equally, given that some parties may seek to avoid the sanctions by disguising the true end user or destination for goods, if you have suspicions extra checks should be carried out and records kept of those checks. Organised record keeping of checks that have been made on transactions and entities will be important should any authorities later investigate a transaction that has taken place in the past.

Diversion Countries

A number of countries have become known as 'diversion risks' whereby Iranian companies are using third party companies in a number of countries to purchase goods before sending them onto Iran. With the third party acting as a front for an Iranian business the transaction may appear to have no connection to Iran and so therefore sanctions issues may not be considered. It is important however that where there is a suspicion that Iran may be involved all the entities in the transaction are considered and checks carried out where possible. For instance, a warning sign could be that a small company in Country X is ordering a large amount of restricted items under the Regulation when it would appear to have no use for this quantity of goods. It could be purchasing the items on behalf of an Iranian sanctioned individual. If the goods are supplied and the third party was known as a suspicious Iranian front company, it may be deemed that it should have been known that the sanctions would be breached.

There have already been reports of bill of lading scams and other methods being used to evade the trade sanctions. For example, it was recently mentioned in the maritime press that there have been a number of documented instances where cargoes are being loaded in Iran but shipped to a second country in the Middle East Gulf region. The original bill of lading is then altered to indicate that the cargo was loaded in that second country. It was also been reported that Iranian products, such as petrochemicals, were being shipped from Iran under doctored bills of lading which stated that the products emanated from another source of origin, such as India.

UK legislation update

On 11 December 2010, the UK implemented 'The Iran (European Union Financial Sanctions) Regulations 2010. This Statutory Instrument includes provisions preventing the circumvention of restrictions and most importantly imposes penalties for any breach. These can include a fine or in certain cases imprisonment. Given that the penalties are now imposed in domestic legislation, it is even more important that applicable sanctions are complied with.

The Financial Restrictions (Iran) Order 2009, which we summarised in our last briefing, has now expired after having been in force for one year. However, the new EU Regulation applies in the UK as of 27 October 2010. HM Treasury has now issued a Financial Sanctions/Counter Illicit Finance Notice, available from the Treasury's website, providing a detailed commentary on and guidance to complying with the EU Regulation. HM Treasury is the competent authority in the UK for issuing licences, giving notifications and making requests for authorisation relating to the transfer of funds subject to reporting requirements. Any existing licences issued by HM Treasury under the previous legislation will now be deemed to have been issued under the new Regulation and remain valid. New licences will be issued pursuant to the requirements under the new Regulation.

As well as the UK Treasury a number of other government bodies are responsible for the application and enforcement of the Regulation and UK sanctions policies. Both the Department for Business, Innovation and Skills and Her Majesty's Revenue and Customs deal with the enforcement of sanctions and in particular the provision of certain materials to Iran. Should a licence be required for transactions involving Iran, this must be obtained from the relevant Government department.

Export Controls

It is important that companies are aware of the relevant export controls applicable in the jurisdictions relevant to their transactions. Although the various international sanctions legislation may be complied with, this does not automatically mean that the relevant export legislation has also been satisfied. Licences may be needed from the relevant government departments and in some cases the penalties for a breach of export legislation are similar to a breach of sanctions and include large fines and possibly imprisonment. Export controls are specific to each jurisdiction and even where there is no physical export from the country, the arrangement of transfers between third party countries may still be subject to Export legislation, especially where one of the third party countries is sanctioned by that jurisdiction. It is advisable that export controls are considered in tandem with sanctions legislation by those involved in international trade matters.

Specially Designated Nationals

The US Treasury Department's Office of Foreign Assets Control (OFAC) still maintains a list of Specially Designated Nationals (SDNs) with whom dealings are prohibited. The EU and UK also maintains a similar list of SDNs. All the lists are maintained by the relevant State authority and reflect the latest additions to sanctioned persons. Where a transaction with Iran is taking place we would advise that these lists are checked both prior to the transaction and indeed at regular times during the course of a transaction. In addition to the US, EU and UK lists other jurisdictions may maintain similar lists of individuals and entities who trade is restricted with.

US enforcement

On 28 September 2010, the US Treasury's Office of Foreign Assets ("OFAC") published a final rule amending the Iranian Transactions Regulations to remove two general licences authorising the importation into the US of, and dealings in, certain foodstuffs and carpets of Iranian origin and related services. As of that date, imports into the US of Iranian-origin foodstuffs and carpets is prohibited without a specific license which is unlikely to be granted absent special circumstances.

This final rule also implements certain import and export prohibitions contained in the Comprehensive Iran Sanctions, Accountability and Divestment Act 2010 ("CISADA") Relating to importation of goods or services of Iranian origin directly or indirectly into the US and on US origin goods, services or technology from the US or a US person in Iran.

The US has targeted those companies that are used by Iran as front companies. A particular target of the sanctions has been IRISL. As recently as 13 January 2011 a number of shipping companies in Hong Kong were sanctioned as being linked to IRISL. Although there have not been any recent actions against major international companies it is unlikely that this enforcement will take place immediately and it will take the authorities a period of time to gather evidence by which to sanction various companies.

Sanctions Clauses

With the increase in international sanctions many parties are now incorporating sanctions clauses into their contracts. These clauses are designed to protect against a breach of sanctions and allocate any subsequent liability. Where a Contract incorporates a sanctions clause it is advisable that should there be any subsequent contracts, for example in a chain of charterparties, there is equivalent protection from sanctions at each stage to ensure that if a breach occurs, a party in the chain of contracts will not suffer another party's breach of sanctions as a result of a failure to ensure back to back provisions (or at least wider protection) throughout the chain.

In relation to shipping, BIMCO has introduced a sanctions clause for Time Charters. Although a number of clauses have been produced in this area, we would advise that any sanctions clause should be adapted to cover the specific risks that you or your business is trying to protect. Not all contracts will be the same and given the wide scope of international sanctions, there may be specific concerns with certain sanctions legislation. Care should be taken when incorporating or accepting any sanctions clauses in contracts.

Michelle Linderman
Partner, London
michelle.linderman@incelaw.com

Reema Shour
Professional Support Lawyer, London
reema.shour@incelaw.com

James Rose
Trainee Solicitor, London
james.rose@incelaw.com

Contacts

London

Stuart Shepherd (Head of Group)
stuart.shepherd@incelaw.com
+44 20 7481 0010

Steven Fox
steven.fox@incelaw.com
+44 20 7481 0010

Tony George
tony.george@incelaw.com
+44 20 7481 0010

Jonathan Lux
jonathan.lux@incelaw.com
+44 20 7481 0010

Jeremy Farr
jeremy.farr@incelaw.com
+44 20 7481 0010

Joe O'Keeffe
joe.okeeffe@incelaw.com
+44 20 7481 0010

Nick Burgess
nick.burgess@incelaw.com
+44 20 7481 0010

Ted Graham
ted.graham@incelaw.com
+44 20 7481 0010

Ian Cranston
ian.cranston@incelaw.com
+44 20 7481 0010

Christian Dwyer
christian.dwyer@incelaw.com
+44 20 7481 0010

Will Marshall
will.marshall@incelaw.com
+44 20 7481 0010

Jonathan Goldfarb
jonathan.goldfarb@incelaw.com
+44 20 7481 0010

Dubai

Graham Crane
graham.crane@incelaw.com
+971 (0) 4 359 8982

Hamburg

Daniel Jones
daniel.jones@incelaw.com
+49 (0) 40 38 0860

Hong Kong

Andrew Chan
andrew.chan@incelaw.com
+852 2877 3221

Max Cross
max.cross@incelaw.com
+852 2877 3221

Kelvin Lee
kelvin.lee@incelaw.com
+852 2877 3221

Paris/Le Havre

Fred Vroom
fred.vroom@incelaw.com
+33 1 5376 9100

Jérôme De Sentenac
jerome.desentenac@incelaw.com
+33 2 3522 1888

Piraeus

Jonathan Elvey
jonathan.elvey@incelaw.com
+30 210 429 2543

Shanghai

Paul Ho
paul.ho@incelaw.com
+86 (0) 21 6157 1212

Singapore

Denys Hickey
denys.hickey@incelaw.com
+65 6538 6660

John Simpson
john.simpson@incelaw.com
+65 6538 6660

Ince & Co is an international commercial law firm which practises in seven broad strands:

AVIATION | BUSINESS & FINANCE | COMMERCIAL DISPUTES | ENERGY & OFFSHORE | INSURANCE & REINSURANCE | INTERNATIONAL TRADE | SHIPPING

Dubai	Hamburg	Hong Kong	Le Havre	London	Paris	Piraeus	Shanghai	Singapore
T:+971 4 3598982	T:+49 40 38 0860	T:+852 2877 3221	T:+33 2 35 22 18 88	T:+44 20 7481 0010	T:+33 1 53 76 91 00	T:+30 210 4292543	T:+86 21 6157 1212	T:+65 6538 6660
F:+971 4 3590023	F:+49 40 38 086100	F:+852 2877 2633	F:+33 2 35 22 18 80	F:+44 20 7481 4968	F:+33 1 53 76 91 26	F:+30 210 4293318	F:+86 21 6170 3922	F:+65 6538 6122

E: firstname.lastname@incelaw.com
24 Hour International Emergency Response T +44 20 7283 6999

The information and commentary herein do not and are not intended to amount to legal advice to any person on a specific matter. They are furnished for information purposes only and free of charge. Every reasonable effort is made to make them accurate and up to date but no responsibility for their accuracy or correctness, nor for any consequences of reliance on them, is assumed by the firm. Readers are firmly advised to obtain specific legal advice about any matter affecting them and are welcome to speak to their usual contact.

© 2011 Ince & Co International LLP, a limited liability partnership registered in England and Wales with number OC361890. Registered office and principal place of business: International House, 1 St Katharine's Way, London, E1W 1AY.

LEGAL ADVICE TO BUSINESSES GLOBALLY FOR OVER 140 YEARS