

# BUNKERSPOT

## THE RIPPLE EFFECT

NEW REGULATIONS COME  
INTO PLAY

INSIDE:

LNG

RISK MANAGEMENT

CREDIT INSURANCE

FUEL ANALYSIS





# Breakdown cover

Steve Simms of Simms  
Showers advises suppliers  
to be forearmed ahead of  
a potential wave of claims  
over engine damage and  
failure as vessels switch to  
ECA compliant fuel

**T**he chronologically gifted readers of this article may recall the frenzy surrounding 'Y2K', or the turn of the recent millennium. Some predicted apocalypse, others economic collapse, others envisioned a new era of peace. However, 1 January 2000 arrived, the sun came up around the world, and as it turned out, with very limited exception, none of the dire predictions came to pass.

MARPOL VI Annex Regulation 18 has now been in force since 1 January 2015. Its requirement that charterers and vessel owners and operators transiting emission control areas (ECA) must use marine fuel with 0.10% sulphur content is now high on the agenda for marine fuel buyers and sellers. Preceding MARPOL VI's arrival, there was also a frenzy of concern about possible over-zealous prosecutions of shipowners or charterers, and lack of availability of compliant fuel. There were similarly dire predictions of greatly increased freight rates due to the anticipated high costs of compliant fuel.

Like Y2K, 1 January 2015 arrived, the sun rose around the world, and none of these gloomy predictions has yet come to pass. The market has responded to make MARPOL-compliant, 0.10% sulphur fuel generally available (at least in some formula). Prosecutions have increased to a degree, but only because more vessels now fall within MARPOL VI compliance requirements. Compliant fuel also costs less than predicted; it is still more expensive than non-compliant fuel but its price is lower because of the recent overall reduction in marine fuel prices.

For marine fuel suppliers, however, 1 January 2015 has brought an unaccustomed and greater probability of prosecution and liability.

Prosecution, because, for the first time, MARPOL and national regimes enforcing pollution regulations (in the United States, the *Act for Prevention of Pollution from Ships (APPS)*) are focused not only on shipowners, operators and charterers who order marine fuel, but also on those selling them marine fuel. Now, authorities will prosecute suppliers selling fuel that they wrongly describe as MARPOL VI compliant within ECAs. Fuel suppliers, again for the first time, can be the targets of whistleblowers seeing rewards through APPS prosecution (see *Bunkerspot* October/November 2014).

Liability, because now a significant amount of the world's fleet must operate on fuels which in many cases, depending on the fuel composition, a vessel's engines, or a vessel's crew, may cause engine failure and damage.

Before 1 January, there were, of course, bunker quality disputes and some situations where faulty intermediate fuel oil (IFO 380 centistoke (cst) or 180 cst) or marine gasoil (MGO) caused engine failure. Where engine failures did occur they were almost always far offshore where there was little likelihood of grounding or collision with other vessels.

Now, however, any of the world's tens of thousands of vessels transiting an ECA must first switch their fuels to MARPOL IV-compliant, ECA-suitable, low sulphur fuel. This is regardless of whether the vessel's engines are new or old, or whether the available compliant fuel may have a makeup less suitable for those engines or the vessel's fuel system.

The example of California can perhaps be seen as a predictor of the 'new' liability. For a number of years before 2015, California had its own version of MARPOL IV, requiring vessels' use of 0.10% sulphur fuel in its coastal zone (which is now included in the US West Coast ECA).

Prior to 2015 in California, there have been significant and increasing numbers of vessel engine failures attributable to otherwise environmentally-compliant, low sulphur marine fuel. Engine shut downs have occurred as vessels entered the coastal zone, switched to compliant fuel, and found that it had an insufficient flash point to fire the engines. Owners and operators found that the compliant fuel reacted with their open-ocean, higher sulphur fuel to clog filters and pumps and eventually cause engines to stop. Catalytic fines (cat fines), common to compliant fuel, damaged engines and engine systems.

As part of the fuel switch-over process,

compliant fuel, which was generally higher in viscosity, was introduced to systems which had previously been operating on higher sulphur fuels at a high temperature. This heat caused the compliant fuel to become even more viscous and to leak from the fuel system and engine seams, resulting in cases of engine seizure and fire.

Vessels went without power for hours, while engineers made attempts to re-start engines, including using non-compliant fuel. Fortunately, there are no reported collisions or groundings from these incidents. Moving forward to 2015, compared to much of 2014 and before, Californian ports are now the most congested in the United States. Vessels are delayed for weeks at offshore anchorages, all within the ECA, and they are required to burn only ECA-compliant fuel.

The liability concern therefore is not just because the risk of engine failure from ECA-compliant fuel has increased per vessel. The risk has increased significantly because of the sudden and significant increase in the number of vessels which must quickly switch to and use ECA-compliant fuel.

**'For claimed ECA-compliant fuel sources, suppliers should themselves either test their physical supplier's fuels, or ensure that they receive reliable independent tests of that fuel'**

Of course, California is not the only crowded ECA; European ports within the Baltic and North European ECAs are at least, if not more, congested. Anecdotally, since 1 January 2015, crews operating in these ECAs have also reported increasing numbers of engine failures associated with otherwise low sulphur-compliant fuel.

Even given these increasing numbers, the odds that ECA-compliant fuel will be a cause of one and probably more marine casualties are still relatively low. However, whether damages are major or minor, someone will quickly ask, 'Who is responsible?' It is unlikely that marine fuel suppliers will escape responsibility or, short of that, the need to raise a strong defence.

Historically, marine fuel suppliers

could expect to rely on their sales terms and conditions, and the accepted chain of responsibility for fuelling vessels. That is, most ocean-going commercial vessels are chartered, and charter parties make the charterer entirely responsible to the owner for supplying fuel which is suitable to the vessel. Failure to do so means that the charterer must pay the owner damages.

The charterer, as required by standard marine fuel supplier sales terms and conditions, is responsible for making sure that any fuel provided to the vessel complies with the vessel engine requirements. Well-drafted sales terms and conditions conspicuously exclude all implied or express warranties of fitness for any particular purpose, or of compliance with any particular (including MARPOL) requirements. They generally disclaim the supplier's responsibility for any aspect of the vessel fuelling, other than meeting the supplier's understanding of the buyer's specifications of the fuel (subject to the buyer's confirmation by testing). Properly drafted sales terms and conditions also strictly limit the time to lodge claims

relating to off-spec fuels and require the reliable taking and retention of fuel samples.

Let us take the example of a vessel that is about to leave an ECA. Its charterers contact their preferred supplier because the vessel is low on ECA-compliant fuel; it needs fuel to depart the ECA and also to enter its next port within an ECA. The supplier simply receives the request to quote and finds a physical supplier with the best price offering a fuel that it says is ECA-compliant. The supplier takes no note of the age of the vessel, its crew's likely experience with ECA switch-overs, or its fuel tank configuration. The supplier gives no instructions to the physical supplier about whether to load in an empty tank or to co-mingle with existing supply. The supplier obtains no information about the product

viscosity or expected temperature at loading. The supplier understands from the physical supplier that the product is ECA-compliant, but knows nothing of the product's composition.

The vessel fuels, its tugs depart and it engages its engines on the compliant fuel. The engines fail and will not re-start; the engineers attempt to re-start with high sulphur fuel, but the engine's filters and pumps are clogged. The engine temperature is too low to ignite the higher sulphur, lower viscosity fuel. As a result of the problems, the vessel collides with another vessel, both sustaining significant physical damage and loss of crew lives.

Investigators then arrive at the site and secure the shipboard fuel samples. They also locate the marine fuel supplier, and secure its samples. They quickly determine that engine failure caused the casualties, and that the otherwise compliant fuel caused the engine failure.

The shipowner demands arbitration with the charterer for the damages, including those sustained by the other vessel and for the crew death liability. The charterer claims against the fuel supplier which raised its sales terms and conditions, including limitation of liability over the cost of the fuel.

However, the owner and charterer (and through them, their insurers) of the third party (the damaged vessel, survivors and estates of the dead crew members) bring a suit against the vessel with the failed engines, its charterer, and the fuel supplier.

This scenario, post-January 2015, is a very real one for bunker suppliers, and they should prepare for this new reality of potential, and actual, liability. Preparations for such an eventuality should include the following:

#### Insurance

Suppliers must ensure that they have as much coverage in place as is economically feasible, not only for indemnity (reimbursement) but for defence (payment for legal costs) to defend against and, if necessary, pay any judgment or settlement of claims for allegedly (or actually) faulty fuel.

They should review, or ask their legal counsel or insurance brokers to assess their insurance policies, to ensure that wherever and whenever there is an allegation of loss arising out of faulty fuel, warranted or not, the insurance policy will respond to and provide a defence against that allegation.

Because of a lack of concern about potential third party (non-contractual) claims, fuel suppliers may have been generally inattentive to their insurance

coverage prior to 1 January 2015. They should examine and enhance it now.

Along with this, there should be an examination and proof of physical and any 'downstream' supplier insurance coverage. Brokers and traders buying from physical suppliers should make sure that those physical suppliers have adequate insurance coverage, in form and amount, to respond to a third party claim arising from alleged injury or damage caused by faulty, or allegedly non-compliant, fuel.

Physical suppliers, and any suppliers 'downstream' of a broker or trader, should readily provide their insurance policies, be required to confirm with each transaction that the policies continue in force, and be able to add 'upstream' suppliers as additional policy insureds. In this way, on any suit against an 'upstream' supplier by a third party, that supplier will have an insurance policy, in addition to its own, to defend and indemnify against a third party claim. Such claims may be large, and so suppliers should seek to maximise all available coverage, in addition to their own.

#### Know your physical supplier

Providing ECA-compliant fuel must not be, primarily, the function of a search for the cheapest fuel. There are many ways to achieve low sulphur fuel content, particularly using distillates and additives, which, while achieving compliance in terms of sulphur content, may cause engine damage or shutdown, or may react adversely with fuel remaining in vessel tanks or fuel systems.

A marine fuel supplier must know its supplier and its operations, and, in particular, that supplier's source of compliant fuel. You must ask yourself the questions: 'Does the supplier blend its own fuel and, if so, what are its facilities and means for blending?' and 'Does it buy low sulphur fuel and, if so, what is the source or sources of the fuel?'

Before 1 January 2015, pre-sale testing of fuel may not have been regularly needed. However, for claimed ECA-compliant fuel sources, suppliers should themselves either test their physical supplier's fuels, or ensure that they receive reliable independent tests of that fuel.

After 1 January 2015, can the supplier simply rely on its buyer to carry out testing? And can the buyer alone determine whether the ECA-compliant fuel will propel the buyer's vessel? The odds say that the supplier should not rely solely on the buyer's testing. Yes, it is the buyer (charterer, owner or operator) who specifies the fuel, decides that it is suitable

for the vessel, determines and, hopefully, has trained its crew for switch-over procedures, and to handle emergencies such as engine seizure. However, and this is important, there is only one element in the supplier's control: the fuel quality and composition.

Buyers' tests may take place frequently after the vessel is underway and the fuel switched over, just because of time and operational needs, but this may be too late to detect problems. It is better for the supplier to have conducted its own tests, and head off what problems it can, than to have to face significant liabilities later when a buyer's test may be too late or inaccurate.

In terms of your physical suppliers, check their procedures for the actual bunkering of vessels. For example, do they use the same barge tanks to deliver compliant and other fuels? Do they mix different compliant fuels in the same barge tanks? Do they have a system for cleaning valves and hoses between supplies? Is there a danger that, because of the systems that your physical supplier uses, an otherwise compliant supply could cause engine damage or failure?

Pre-sale testing and vetting of supply sources is also important to detect cat fines and other impurities which are relatively frequently found in low sulphur fuels. Again, it is better to detect the problems pre-sale and locate a suitable physical supply in advance, rather than to have an expensive contention with a customer over quality, or a defence against a third party claiming damage because of an engine shut down or disabled by faulty fuel.

If blends to reach ECA compliance are involved, using materials from multiple suppliers, then there should be tests not only of the final blend but of the main ingredients to the blend, including for their stability. Many vessels will not have dedicated tanks for low sulphur fuel, and so will experience some intermingling on switch-over. It is important for suppliers to know as best they can before fuelling that there may be an adverse reaction if there is intermingling of fuels, and avoid providing such blends to customers whose vessels may lack the ability to segregate fuels.

Also, do not be afraid to ask your suppliers what their record is on claims for non-compliant supply (whether or not that is for low sulphur fuel) and avoid suppliers which have had well-founded claims. MARPOL also provides for vessel owners or charterers to file protests with national authorities, where the owners or charterers have experienced problems with non-compliant fuel. Owners and

## 'Do your sales terms and conditions include the choice of a favourable jurisdiction's law for purposes of liability, and an option for you to choose binding arbitration in your choice of forum?'

charterers also may file a 'Fuel Oil Non-Availability Report' (FONAR), or similar document, when they believe that ECA-compliant fuel is not available. Suppliers might consider obtaining protests and FONARs, relating to those suppliers' sales areas or their physical suppliers. If customers or potential customers are contending that there are problems with a source of physical supply, then as a 'downstream' supplier, that is a source to avoid.

### Know your customers

MARPOL VI and implementing national regulations require that each vessel has a well-rehearsed and effective plan in place for switch-over to compliant fuel once within an ECA. However, despite the fact that ECAs include many well-visited ports, some vessels may not call at ECA ports frequently and therefore their crews may be unfamiliar with switch-over procedures. Older vessels are also unlikely to have dedicated tanks for low sulphur fuels and their engines may be less suited for fuels of high viscosity.

Suppliers should know the age, engine make-up and the fuel tank configuration of their customers' vessels. Given an engine's age and fuel system, will a certain fuel, which may have high viscosity, be compliant, be at the right price, or be likely to cause an engine problem? Given the increasingly well-known problems that some engines encounter with some low sulphur fuels, it is a poor defence for a marine fuel supplier to fall back on a blind reliance on its buyer to turn away an unsuitable fuel.

### Revisit terms and conditions

As a supplier, what do your present sales terms and conditions say about MARPOL compliance and about disclaiming express and implied warranties, including fitness for a particular purpose? Implied warranties, if not expressly and conspicuously disclaimed, can run to third parties. What do your sales terms and conditions say about required testing, keeping of samples, and limitation of time and format for raising claims? Do your sales terms

and conditions effectively require your buyers to indemnify you, as a supplier, against liability arising out of your fuels provision, including if from your own negligence? Do your sales terms and conditions include the choice of a favorable jurisdiction's law for purposes of liability, and an option for you to choose binding arbitration in your choice of forum? Do your sales terms and conditions limit incidental and consequential damages, and include the vessel owner, manager and charterer as bound by the sales terms and conditions?

You should ask your legal counsel to review your sales terms and conditions now to determine whether, as a supplier, they extend to you the greatest protection that they can against third party liability from engine failure or damage, and resulting casualty, from low sulphur fuel and vessel operations related to it.

At the same time, also look at your suppliers' sales terms and conditions. Do they require you to do all testing and disclaim their liability? Do they leave you any recourse if there is a claim against you as an 'upstream' supplier, because of the faulty materials which you have bought from that 'downstream' supplier? Will you be required to bring a claim – if you have a claim – in an unfavourable jurisdiction? Make sure that you, as buyer from your 'downstream' supplier, have recourse that your own supplier's sales terms otherwise do not unacceptably limit or eliminate. Make sure that your supplier has the incentive, because it retains some liability and therefore responsibility, to provide you with compliant fuel that you can then supply to your buyer.

### Prepare for the worst

MARPOL and implementing national regulations have a range of requirements relating to the provision of ECA-compliant fuel. These include keeping well-marked and properly obtained samples of each fuel supply, and of detailed bunker delivery receipts (BDR). The drafters of MARPOL and its regulations meant these requirements to relate mainly to

policing compliance, but keeping them is also good preparation for defence against any claim that, as a fuel supplier, the low sulphur fuel you have supplied has caused engine failure or damage, including damage to any third party.

In response to any such claim, you, as the supplier, should have the sample and BDR readily available, as well as any specifications that your buyer had given you prior to supply. Before 1 January 2015, retaining these samples and records was certainly important to defend against customer quality claims which, with effective contractual limitations terms, would be relatively limited. Now, however, given the high likelihood of third party claims arising from low sulphur fuel use, keeping such samples and records, required by MARPOL, is critical.

As a supplier, however, your preparation should not be limited to that. You should also document, and retain your documentation of, your verification of your suppliers, knowledge of vessel (and engine) specifications, and pre-sale testing. In the post-1 January 2015 world, for marine fuel suppliers a response of 'I relied on the buyer' may well not suffice as a defence against third party claims which may arise from allegedly problematic low-sulphur supplies.

Thankfully, at the time of writing there have been no major casualties involving engine failures from low sulphur, ECA-compliant fuel. However, with the sudden increase in the number of vessels required to use this fuel, the odds of such casualties are increasing. There is the intersection of relatively crowded maritime zones, with a range of engine types, a range of fuels, and a range of crew competencies to switch those fuels from non-compliant to compliant in a relatively short time.

 Steve Simms is a Principal of Simms Showers LLP.

 Email: [jssimms@simmsshowers.com](mailto:jssimms@simmsshowers.com)  
Tel: +1 410 783 5795