

## Incorporation of Arbitration Clauses into Bills of Lading

My purpose here today is to outline the recent developments in the incorporation of arbitration clauses into bills of lading. I will focus on two main issues: firstly, the complexities surrounding the conflict of laws rules on finding the law governing the incorporation issue and secondly the question of what words of incorporation can incorporate arbitration clauses into bills of lading.

Before discussing the conflict of laws rules on finding the governing law, I want to start by highlighting the purpose of incorporation. The incorporation issue is addressed within the realms of contract construction,<sup>1</sup> and it is important to bear in mind the commercial purpose of incorporation clauses when considering any aspect of the rules of incorporation in the context of bills of lading. In this context, the commercial purpose of the incorporation clause is in essence to enable the shipowner or the charterer, who is also the carrier under the bill of lading, to turn and face the bill of lading holder on the same terms as his/her charterparty.<sup>2</sup> On this matter, Lord Justice Oliver in *The Varenna* said:<sup>3</sup>

*The purpose of referential incorporation is not – or at least is not generally – to incorporate the intentions of the parties to the contract whose clauses are incorporated but to incorporate the clauses themselves in order to avoid the necessity of writing them out verbatim. The meaning and effect of the incorporated clauses has to be determined as a matter of construction of the contract into which it is incorporated having regard to all the terms of that contract*

The quoted part of Lord Justice Oliver's judgment in *The Varenna* provides useful guidance on the purpose of the incorporation clauses. Here the emphasis should be placed on the part where Lord Justice Oliver stresses the importance of seeing the incorporation issue as merely incorporation of the provisions themselves, in isolation from the intentions of the parties whose provisions are incorporated. The decision in *The Varenna* also establishes the key rule of incorporation: the operative words of incorporation are exclusively found in the bill of lading.<sup>4</sup> In that respect, the decision

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<sup>1</sup> *The Annefield* [1971] P 168, 179.

<sup>2</sup> For more discussions on incorporation see M. Ozdel, *Bills of Lading Incorporating Charterparties* (London: Hart Publishing, 2015).

<sup>3</sup> [1984] QB 599, 618.

<sup>4</sup> See Ozdel, *Bills of Lading Incorporating Charterparties*, above n. 2, Chapter 4.

further suggests that, when considering the effect of the words of incorporation, the key question is what a reasonable person would have understood the parties to have meant from the words of incorporation.<sup>5</sup> In other words, when deciding what charterparty provisions can be incorporated through the words of incorporation, the intention of the original parties to bills of lading that can only objectively be ascertained from the wording of the incorporation clause should be regarded as paramount.<sup>6</sup> With all these considerations in mind, we should not therefore look beyond the words of incorporation when deciding whether an arbitration clause can be incorporated through the words of incorporation. I will come back to this point when discussing the law governing the incorporation issue and the recent Court of Appeal decision in *The Channel Ranger*.<sup>7</sup>

### **Finding the law governing the incorporation issue**

Before considering the effect of the words of incorporation in more detail, it is important to take the initial step to determine the law governing the question of incorporation of arbitration agreements. The cases on the incorporation of arbitration clauses into bills of lading show that this issue is too often either neglected or not considered in sufficient detail.

Since the question of incorporation is a matter of contract construction, finding the law governing the question of incorporation might at first appear straightforward: we should refer to the applicable law of the contract. In the context of bills of lading, the reference should thus be made to the applicable law of the bill of lading when deciding whether it can incorporate an arbitration clause. However, the main difficulty here is that the applicable law of a bill of lading with an incorporation clause cannot, in most cases, be ascertained with reasonable certainty.<sup>8</sup> It is common for such a bill of lading to be silent as to its governing law and to refer to a charterparty that contains an express or an implied choice of law. At this juncture, it is important to note that arbitration clauses are usually taken as an implied choice of law in favour of the seat designated in the arbitration clause.<sup>9</sup> The charterparties referred to in bills of lading usually contain

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<sup>5</sup> See also *Chartbrook Ltd v. Persimmon Homes Ltd* [2009] 1 AC 1101, para 25.

<sup>6</sup> See Ozdel, Bills of Lading Incorporating Charterparties, above n. 2, Introduction.

<sup>7</sup> [2014] 1 Lloyd's Rep 96.

<sup>8</sup> For more discussions on this issue see Ozdel, Bills of Lading Incorporating Charterparties, above n. 2, Chapter 1.

<sup>9</sup> See *Compagnie Tunisienne de Navigation SA v. Compagnie d'Armement Maritime SA* [1970] 2 Lloyd's Rep 99 (HL), where their Lordships took the view that forum selection clauses were persuasive in determining the law applicable to the contract. This approach survives the Convention on the Law Applicable to Contractual Obligations 1980 (the Rome Convention) and the Regulation on the Law Applicable to Contractual Obligations 2008 (Rome I). See *Egon Oldendorff v. Libera Corporation* [1996] 1 Lloyd's Rep 380, where an arbitration clause providing for London arbitration was taken as an implied choice of English law,

arbitration clauses, and this situation leaves us with the difficulty of determining the governing law with reasonable certainty.

With almost all charterparties containing either an express or an implied choice of law, the applicable law of the bill of lading will depend on whether the charterparty is incorporated. And this brings with it a typical chicken and egg conundrum: which should come first, the decision on incorporation or the decision on the applicable law?

### **The use of putative thinking**

Where the applicable law of the bill of lading cannot be ascertained due to an implied or express choice of law in the charterparty referred to in the bill of lading, one solution is to determine the governing law on the assumption that the charterparty is incorporated. In other words, solving the problem of incorporation with reference to the law that would govern the bill of lading if the charterparty were incorporated. This approach was followed in two landmark decisions on incorporation: *The Heidberg*<sup>10</sup> and *The Wadi Sudr*.<sup>11</sup>

This putative line of thinking is also followed where there is only one contract and where the validity of the contract or the validity of the arbitration clause in that contract is disputed. In *The Parouth*<sup>12</sup> the dispute was whether the charterparty with an arbitration clause was valid and binding between the parties. In *The Atlantic Emperor*,<sup>13</sup> the key issue before the court was not whether there was a binding contract with an arbitration clause, but whether there was a valid arbitration clause in a binding contract of sale. In both cases, the courts applied the putative thinking and determined the governing law by asking the question of what law would govern the question of validity if the contract or the arbitration clause in that contract were valid.

### **An alternative method**

English courts have not always tackled the “chicken and egg” conundrum with reference to the putative applicable law of the bill of lading. As is clear from the English cases on incorporation, there is also an alternative method to the use of putativity. Where the bill of lading does not contain an express or an implied choice of law, in some decisions,

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in the absence of any “compelling indications to the contrary in the other terms of the contract or the surrounding circumstances of the transaction”.

<sup>10</sup> [1994] 2 Lloyd’s Rep 287.

<sup>11</sup> [2009] 1 Lloyd’s Rep 666, reversed on other grounds by the CA in [2010] 1 Lloyd’s Rep 193.

<sup>12</sup> [1982] 2 Lloyd’s Rep 351 (CA).

<sup>13</sup> [1989] 1 Lloyd’s Rep 548 (CA).

most notably, in *The Njegos*,<sup>14</sup> the courts raised the inference that the original parties to the bill of lading intended that the applicable law of the bill of lading would be the same as that of the charterparty referred to. The main justification for this inference was that the charterparty and the bill of lading were considered to be “closely related contracts”. In terms of the result it creates, this method is not in fact distinct from the use of putative applicable law of the bill of lading, but the reasoning behind the method is, with respect, not easy to justify: it is difficult to hold the bill of lading holder bound by the intentions of the original parties to the bill of lading, where that intention cannot reasonably be ascertained from the provisions in the bill of lading. This proposition takes us back to what Lord Justice Oliver said in *The Varenna*: the importance of seeing the incorporation issue in isolation from the intentions of the parties whose provisions are incorporated.

The good news is that, despite its recent application by the High Court of Singapore in *Dolphina*,<sup>15</sup> this mechanical inference has not been adopted in recent English cases on incorporation. As will be recalled, this line of thinking was not adopted in two key cases on the law governing the question of incorporation, namely *The Wadi Sudr*<sup>16</sup> and *The Heidberg*.<sup>17</sup>

### **The description test**

Moving on to the description test, in other words, to the question of what words of incorporation can incorporate an arbitration clause, the law was not sufficiently clear prior to the decision in *Habas Sinai ve Tibbi Gazlar v. Sometal SAL*.<sup>18</sup> The case hinged on whether a sale contract incorporated the arbitration clause provided in other sale contracts previously made between the same parties. There were general words of incorporation in the sale contract under which the dispute arose. In other words, there was no express reference to “arbitration” in the relevant incorporation clause. Mr. Justice Christopher Clarke held that general words of incorporation were apt to incorporate an arbitration clause, although the arbitration clause was ancillary to the subject matter of the sale contract.<sup>19</sup> He took the view that the case was different from those bill of lading cases, which he described as “two-contract” cases, where incorporation is concerned with contracts made between different parties. In so doing, he drew a line between “two-contract” cases and those “one-contract” cases where the

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<sup>14</sup> [1935] 53 Ll. L Rep 286.

<sup>15</sup> 2011] SGHC 283; [2012] 1 Lloyd’s Rep 304.

<sup>16</sup> See fn 11.

<sup>17</sup> See fn 10.

<sup>18</sup> [2010] EWHC (Comm) 29.

<sup>19</sup> *Ibid.*

contract refers to a set of terms that are readily accessible to both parties. The case at hand was clearly a one-contract case, and therefore the general words of incorporation were sufficient to incorporate the arbitration clause.

Given the reasoning of Mr. Justice Christopher Clarke in *Habas*, the landmark decision in *Thomas & Co v. Portsea Steamship Ltd*<sup>20</sup> still remains intact. In the context of bills of lading, general words of incorporation are, prima facie, apt to incorporate only those charterparty provisions that are germane to shipment, carriage and discharge of the cargo. It is clear that special words of incorporation are needed to incorporate an arbitration clause into a bill of lading.

After deciding that special words of incorporation are needed in bill of lading cases and in other types of two-contract cases, we then need to consider the required degree of specificity in the special words of incorporation. How specifically should the arbitration clause be referred to in the incorporation clause? Should we expect to see “a spot on” reference to the arbitration clause in the relevant charterparty, telling us exactly what kind of dispute resolution clause is round the corner, or do the courts give some latitude about the ways in which the dispute resolution clause in the relevant charterparty can properly be described for incorporation purposes? At this juncture, the Court of Appeal in *The Channel Ranger* is of great assistance.<sup>21</sup> There, the reference in the bill of lading was to the “Law and Arbitration” clause of the charterparty, although the relevant charterparty provided for English law and jurisdiction. Following the decision of Males J in the first instance, the Court of Appeal found this reference apt to incorporate the English jurisdiction clause in the charterparty.

Following the recent Court of Appeal decision in *The Channel Ranger*, I think it is safe to say that the issue of incorporation is considered as one of contract construction. The decision also makes it clear that the key is to determine “what a reasonable person would have understood the parties to have meant from the special words of incorporation in the bill of lading”, with due consideration of business common sense and the commercial purpose of the incorporation clauses. The decision raises the following three main points.

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<sup>20</sup> [1912] AC 1.

<sup>21</sup> [2014] EWCA Civ 1366.

Firstly, as long as the reference in the bill of lading alerts the holder to the possible incorporation of at least one kind of dispute resolution clause, it can be read as extending to another type of dispute resolution clause in the charterparty. This flexibility is necessary given that the particular dispute resolution method provided in the relevant charterparty may not coincide with the reference in the incorporation clause. Considering the increasing sophistication of the dispute resolution clauses in charterparties, we certainly need this flexibility in the description test in order not to make the inquiry excessively technical. For all these reasons, I am pleased this reasoning of the court in *The Channel Ranger* now helps us reach the desired flexibility in the application of the rules of incorporation.

Secondly, the other reasoning of the court, which was based on business common sense and the canons of construction under general contract law, also has much to commend it. However, I believe that the courts should exercise caution when applying this tool to the question of incorporation in a maritime context. The court's reliance on the aids to construction under general contract law should not be taken to mean that we should now look afresh at the question of incorporation and purely pursuant to the aids to construction under general contract law. The rules of incorporation are peculiar to maritime law, and they should be applied to the question of incorporation.<sup>22</sup>

I am least comfortable with the third reasoning that the reference to litigation in the incorporation clause could be rectified to "arbitration", considering the intention of the original parties to the bill of lading. In support of this rectification, the Court of Appeal took the view that, had the case *The Merak*<sup>23</sup> been decided today, it would have been decided differently. In *The Merak*, the incorporation clause in the bill of lading mistakenly referred to "clause 32" of the relevant charterparty instead of "clause 30", which was the arbitration clause. The Court of Appeal refused to correct the mistake and treated the reference merely as surplus. Nonetheless, they held in favour of incorporation for two main reasons: the comprehensiveness of the word "clause" in the incorporation clause; and the reference in the charterparty arbitration clause to disputes "arising under bills of lading".

The case of *The Merak* would have been decided differently today on the grounds that the word "clause" in an incorporation clause is not apt to incorporate an arbitration

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<sup>22</sup> On this issue, see M. Özdel, *Incorporation of Charterparty Clauses into Bills of Lading: Peculiar to Maritime Law?* in M.A. Clarke (ed.), *Maritime Law Evolving* (Oxford: Hart Publishing, 2013), p. 181 et seq.

<sup>23</sup> [1965] P 223.

clause. However, the point raised in *The Merak* that the words of incorporation in the bill of lading should not be rectified still holds true. Rectification entails reframing the contract pursuant to the actual intention of the parties, and this does not sit comfortably with the nature of bills of lading as transferable instruments. Bills of lading usually pass through the hands of numerous traders. This makes it necessary for the courts to give effect only to the intention of the original parties to the bill of lading that can objectively be ascertained from the wording of the incorporation clause.

In light of the explanations above, the following conclusions can be drawn from the decision in *The Channel Ranger*:

- If a reference to arbitration is apt to incorporate a charterparty jurisdiction clause, a reference to “litigation” in a bill of lading incorporation clause should equally be treated as a proper reference to arbitration. Hence, where the relevant charterparty contains an arbitration clause, as opposed to a jurisdiction clause, the word “litigation” should be apt to incorporate the arbitration clause.
- The question as to the required degree of specificity in the incorporation clause is one of construction. In this context, the courts and tribunals should consider “what a reasonable person would have understood the parties to have meant from the words of incorporation in the bill of lading”, with due consideration of business common sense and the commercial purpose of the incorporation clauses.

It is also important to highlight what conclusions should *not* be drawn from the decision:

- The question of incorporation should not be looked at afresh and purely pursuant to the aids to construction under general contract law.
- This recognised flexibility in the description test should not be treated as tantamount to rectification of the reference in the bill of lading. While the decision in *Thomas v. Portsea* establishes the rule that special words of incorporation are needed to incorporate arbitration and similar clauses, the required degree of specificity is left to be determined on the basis of contract construction. As long as the reference in the bill of lading alerts the holder to the

possible incorporation of one type of dispute resolution clause, the reference should be construed as apt to incorporate the actual dispute resolution clause. This should be done so with due consideration of business common sense and the commercial purpose of the incorporation clauses.

With the increasing interaction between the rules of incorporation and the issue of enforcement of forum selection clauses in bills of lading, these specific questions of incorporation will no doubt continue to keep the minds of arbitrators and judges busy. Time will tell how the courts will define the limits of this flexibility in the description test.

Melis Özdel