SUN MOBILITY
Insurance and Claims Services Limited

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To: Transport Industry Operators

Cargo insurance covers buyer's theft

On 3/4/2008, the Hong Kong High Court ordered a cargo insurer to compensate a seller for US$329,712.80 being the loss of goods stolen by the buyer.

The seller claimed to recover under a contract of marine insurance covering electronic goods shipped from Hong Kong to Khor Fakkan in the United Arab Emirates ('UAE'). Khor Fakkan is a small town on the East Indian Ocean coast of the Emirate of Sharjah, outside the Strait of Hormuz, at which there is a port and a container terminal. The contract of insurance was contained in an Insurance Certificate dated 23/12/1998, which was issued by the cargo insurer, pursuant to Open Cover No. HK-B1789 dated 8/8/1997; that Open Cover named the seller as one of the insured. The insurance covered some 600 cartons of electronic goods carried on board the vessel "AL SABAHIA", and expressly covered all risks as per the Institute Cargo Clauses (A) dated 1/1/1982 ('ICC (A)). By virtue of Clause 19 of the ICC (A) the contract of insurance is governed by English law. The value of the loss was US$329,712.80, and there was also claim arising from monies expended by the seller in terms of "reimbursement of all sums properly and reasonably incurred by the seller" in respect of the legal proceedings instituted in Sharjah subsequent to the loss of the goods. The electronic goods were sold by the seller to a company in the UAE, this sale being evidenced by a Commercial Invoice dated 23/12/1998. This was the first transaction which the seller had done with the buyer, which on 18/12/1998 had remitted a deposit of some US$10,000, pursuant to a sale in which D/P terms had been agreed. The electronic goods left Hong Kong on 24/12/1998 on board the vessel 'AL SABAHIA', having been loaded into a container No. CATU 3019704. A bill of lading, No SENUHKG552617, dated 24/12/1998 was issued by DSR-Senator; the Shipper was named as the seller, the Notify Party was named as the buyer, and the Consignee was named as Habib Bank. The vessel carrying these goods arrived at Khor Fakkan on 3/1/1999. The buyer obtained actual physical possession of this container from the nearby Sharjah container terminal – whence, without the knowledge of the seller, it had been transferred from the Khor Fakkan terminal on 7/1/1999.

Under the contract of sale, the buyer was to make payment for the goods by a bill of exchange drawn on the buyer, and on 30/12/1998 the seller had sent all the shipping documents to a finance house, Commonwealth Finance with a request that it purchased the bill of exchange drawn on the buyer "subject to final payment". In order to obtain discounted payment on the bill of exchange drawn on the buyer, the documents so submitted to Commonwealth Finance had included three (3) original bills of lading. Commonwealth Finance purchased the bill of exchange, and on the same day had sent the shipping documents to Habib Bank in Sharjah with the instruction that the bank deliver the documents to the buyer against payment. Habib Bank on 25/1/1999 sent a message to Commonwealth Finance that the buyer's account number as given was incorrect; the response read thus: "…The A/C number you hv mentioned is incorrect. We tried to approach the Drawee who faxed us that they will open A/C but then did not turn up. Pls instruct yr docs r held on yr risk and responsibility." On 26/1/1999, the seller asked the shipping line what had happened to its goods, and on the same day the seller was informed that the buyer had taken delivery of the container by means of an original bill of lading indorsed by Habib Bank. Habib Bank, by telefax dated 27/1/1999, claimed that the shipping documents had not been checked upon receipt but that there were only two (2) bills of lading and no packing lists; this fax concluded thus: "Please enquire from the Shipping Company how the goods were released without proper authority from the Bank as we have not endorsed any Bill of Lading. Please also note that we are holding the documents at your risk and await your immediate instruction."

The seller was obliged to repay to Commonwealth Finance the money paid by the finance house to purchase the bill of exchange; this sum, in the amount of US$284,142 was repaid on 26/2/1999. It appeared clear both to the seller and to Commonwealth Finance that the buyer had obtained delivery of the goods dishonestly by means of the presentation of an original bill of lading obtained from within the Sharjah branch of the Habib Bank. Accordingly, proceedings were taken against the HabibBank in Sharjah, and were brought in May 1999 in the name of Commonwealth Finance. The shipping line was joined as a defendant, and was ordered to produce the original bill of lading which was used to take delivery, upon the reverse of which appeared the apparent endorsement of Habib Bank; there also appeared on the reverse of the bill an indorsement by the buyer. The Sharjah proceedings took some time. A banking expert appointed by the Sharjah court, came to the startling conclusion that there was no satisfactory evidence to suggest that Habib Bank ever had received all three bills of lading, whilst a report ordered to be prepared by the Criminal Investigation Department of the Sharjah police concluded that the stamp which appeared on the reverse of the bill of lading used to

procure delivery of the goods was not taken from a stamp mould which had been proffered by the Habib Bank. On 14/12/2004 the Sharjah Court dismissed the claim as brought by Commonwealth Finance against Habib Bank, the Court finding that Habib Bank never had received the bill of lading as was used to take delivery of the goods.

In the Hong Kong proceedings, the Judge however held that an original bill of lading went missing whilst the 3 originals were in the possession of the Habib Bank, and the Judge further found that the misdelivery to the buyer of the seller's container containing the goods was a direct consequence of the buyer dishonestly obtaining one of the three original bills of lading which had been sent to Habib Bank and with which bill of lading, duly endorsed by the Bank, the buyer was able to obtain delivery absent payment. The Judge further make the inferential finding on the probabilities that the buyer had obtained one of the original bills of lading from a contact within the Sharjah branch of the Habib Bank, and that with the assistance of that contact a chop purporting to be a Habib Bank chop had been appended to the reverse of the bill of lading. The Judge found that the buyer actively was complicit with a dishonest employee within the Habib Bank who was responsible for sending to the buyer an original bill, apparently duly 'indorsed' by the bank, which then facilitated the misdelivery to the buyer of the container in question. It was by means of the presentation of that original bill that the buyer was able dishonestly to obtain physical possession of the goods without payment, whereas, had the D/P terms of the sale been honoured, the buyer could not have come into possession of the container without first making payment for the documents necessary to obtain such possession.

The Judge found that this was a CIF contract. The Judge also agreed with the submission of the seller that in fact the buyer was charged a CIF price, that risk was to pass only when the documents had been taken up and paid for, and that the buyerr was to take an assignment of the insurance, which was why the relevant policy was included among the documents as sent to Habib Bank, and which the buyer was to receive if and when it had discharged its contractual obligations and had purchased the documents. The seller patently maintained an insurable interest in the goods at the time of the loss.

It may be useful to set out Clause 8 of the ICC (A) in full:

"8 8.1 This insurance attaches from the time the goods leave the warehouse or place of storage at the place named herein for the commencement of the transit, continues during the ordinary course of transit and terminates either

8.1.1 on delivery to the Consignees' or other final warehouse or place of storage at the destination named herein,

8.1.2 on delivery to any other warehouse or place of storage, whether prior to or at the destination named herein, which the Assured elect to use either

8.1.2.1 for storage other than in the ordinary course of transit or

8.1.2.2 for allocation or distribution,

or

8.1.3 on the expiry of 60 days after completion of discharge overside of the goods hereby insured from the oversea vessel at the final port of discharge,

whichever shall first occur.

8.2 If, after discharge overside from the oversea vessel at the final port of discharge, but prior to termination of this insurance, the goods are to be forwarded to a destination other than that to which they are insured hereunder, this insurance, whilst remaining subject to termination as provided for above, shall not extend beyond the commencement of transit to such other destination.

8.3 This insurance shall remain in force (subject to termination as provided for above and to the provisions of Clause 9 below) during delay beyond the control of the Assured, any deviation, forced discharge, reshipment or transhipment and during any variation of the adventure arising from the existence of a liberty granted to shipowners or charterers under the contract of affreightment."

The Judge rejected the cargo insurer's argument, pursuant to Clause 8.1.1 of the ICC (A), namely that the Khor Fakkan Container Terminal represented "the Consignees' or other final warehouse or place of storage". Given that on arrival at Khor Fakkan this container remained at Khor Fakkan for 5 hours only, at all times under Customs Bond and was placed in Stack S41, which simply represented no more than a temporary position in an open air container stack, it was difficult to see how legitimately this might be characterized as a 'final warehouse or place of storage.' The word 'final' in Clause 8.1.1 must govern both 'warehouse' and 'place of storage' – see Arnould, Vol 3, at para 261 – and the phrase 'final … place of storage' in the Judge's view could not sensibly be construed as fitting the circumstances in which the goods were stored in Customs bond at Khor Fakkan Terminal.

The cargo insurer's next argument focused upon the provisions of Clause 8.2; in fact, this aspect of the argument, as propounded, contained two distinct elements. The first point taken by the cargo insurer was reliance as a terminating event upon the commencement of transit from Khor Fakkan to the Sharjah Terminal at 1704 hours on 4/1/1999, Clause 8.2 providing that if after discharge overside at the final port of discharge "the goods are to be forwarded to a destination other than that to which they are insured hereunder, this insurance…shall not extend beyond the commencement of transit to such other destination." The Judge did not consider that this argument successfully

availed the cargo insurer. The Judge did not read the words "are to be forwarded to" within Clause 8.2 other than as reference to a pre-planned transit with the knowledge and consent of the assured. There is support for this construction in Arnould, op cit., at para 263, wherein the learned editors state: "Clause 8.2 appears to be designed for situations where it is planned or decided that the goods should be forwarded to another destination, beyond that to which they are insured under the policy (they would normally then be covered by another policy taken out by the buyer). The words 'are to be forwarded' suggest that meaning." Accordingly, the cargo insurer's assertion that the present situation fell within Clause 8.2 was rejected also. The other limb to the cargo insurer's argument was that in any event there could have been no continued cover after the goods had left Khor Fakkan, given that Khor Fakkan was the place stipulated in the Bill of Lading as representing the port of discharge and of delivery, and that the loss namely the actual physical abstraction of the container, took place only when the goods were in Sharjah – by which time on any basis the 'all risks' cover had terminated. The cargo insurer's contention was that the 'all risks' cover was subject to specific geographical limit, and that it was clear Khor Fakkan and Sharjah are quite different places approximately 120 kilometres apart. The cargo insurer further submitted that there was no evidence that the movement of the goods from Khor Fakkan was part and parcel of the plan to steal the goods. This argument concerned the question as to where the loss actually occurred, and the Judge found that wherein there was an overwhelming inference that this was a pre-planned theft carried out at the behest of the buyer, acting complicitly with someone within the Habib Bank, a like inference legitimately might be drawn that the goods only could have been moved to Sharjah upon the specific instructions of the buyer, and thus that the loss must be taken to have occurred upon the goods leaving Khor Fakkan, even though it appeared that the buyer only obtained actual physical possession of the container in Sharjah. Such loss occurred at Khor Fakkan during the pendency of the 'all risks' cover. The seller never could have anticipated that this container legitimately would be delivered to the buyer other than at Khor Fakkan, hence the terms of the insurance as effected specifying the destination as Khor Fakkan. The fact that the buyer had contrived to cause the container to be conveyed under bond to the Sharjah terminal in the Judge's view was not to be regarded as affecting the right of the seller assured under this 'all risks' insurance cover. The Judge rejected the argument on the part of the cargo insurer that no liability enured under its Open Cover because the loss of this container was outwith the geographical limit of that cover at the time of the loss.

The scheme set out within Clause 8.1 provides for continuation of the cover during "the ordinary course of transit" and provides three alternatives in which cover may terminate "whichever shall first occur". The seller argued that if the first two alternatives within Clause 8.1 did not apply, then the 60 day provision prima facie applied, and that the words "at the final port of discharge" are to be read as governing "discharge overside…from the oversea vessel"; accordingly, the seller submitted, the period of 60 days was to run from the moment that the goods were discharged overside at the final port of discharge, and that these words could not be read as, in effect, imposing an immutable geographical limit upon the duration of the cover. It seemed to the Judge that in principle the seller's analysis was right, and that the key lay in the circumstances in which the insured goods had been caused to be transported outwith the specified geographical limit of the cover. If and in so far as such goods had been wrongly abstracted from the designated destination to which they had been sent in the 'ordinary course of transit' – the rubric within Clause 8.1 – the Judge could see no reason why the 60 day limit within Clause 8.1.3 should not continue to be applicable, and thus the Judge agreed with the seller's contentions. The goods wrongfully had been abstracted from Khor Fakkan absent the knowledge and consent of the seller, the Judge had no difficulty in holding that the 'all risks' cover over these goods indeed remained in force for 60 days from 4/1/1999, and that this would be the position even if the Judge had held (which the Judge have not) that the loss was to be regarded as having taken place at Sharjah, and not at Khor Fakkan.

The cargo insurer argued that the claim was for financial default and not for physical loss of the goods, and further that the proximate cause of the loss was the wrongful obtaining of a bill of lading, or the loss of a bill of lading, which was not a peril insured against. The Judge did not consider this to be an attractive submission. Delivery of the relevant container was obtained in an unauthorized manner. This was not merely a case of financial default. The short point was that absent payment the buyer never would have been able to get its hands on an original bill of lading, and thereafter to use that document to arrange for the wrongful abstraction of these goods. Therefore, in the Judge's judgment this 'causation argument' failed in limine.

Clause 16 of the ICC(A), which reads:

> "It is the duty of the Assured and their servants or agents in respect of loss recoverable hereunder
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> 16.1.1 to take such measures as may be reasonable for the purpose of averting or minimizing such loss, and
>
> 16.1.2 to ensure that all rights against carriers, bailees or other third parties are properly preserved and exercised
>
> and the Underwriters will, in addition to any loss recoverable hereunder, reimburse the Assured for any charges properly and reasonably incurred in pursuance of these duties."

The cargo insurer argued that the seller had pleaded that the findings of the Sharjah court were perverse and contrary to the obvious facts. Thus, the cargo insurer submitted, an appeal against the decision of the Sharjah first instance court should have been lodged, and that this was an appeal which "stood every chance of success" given the seller's pleaded contention as to the 'perversity' of the original decision. It followed, therefore, said the cargo insurer, that the failure to

appeal this Sharjah judgment, or to procure an appeal by Commonwealth Finance, represented a breach of the seller's duty under Clause 16.2 of the ICC(A), and under section 78(4) of the Marine Insurance Act 1906. If this be right, the cargo insurer continued, the seller's breach of duty would afford a complete defence as recovery of the amount claimed against the Habib Bank would extinguish the loss for indemnification under the Open Cover. Clause 16 of the ICC(A) substantially corresponds with section 78 of the Marine Insurance Act 1906. It is not a warranty, but merely a contractual stipulation, so that as the editors of Arnould express the position (see Vol 3, paragraphs 297-302): "Failure to minimize a loss or failure to protect the value of insurer's rights of subrogation, in breach of the duties under Clause 16, gives rise to no more than a cross-liability of the assured to the insurers in damages, and a potential for setting off that liability against the liability of the insurers under the policy, so as to afford them a complete or partial defence, according to the circumstances (more usually, the defence will at best be a partial defence)." The Judge accepted the submission of the seller that the only relevant question was whether there was anything which was, or was not, done by the seller which had caused the cargo insurer to lose a right of subrogation which otherwise would have been available to it. In other words, had the seller fallen short of that which a reasonable assured could be expected to have done, having regard to the interests of the insurers and of itself? In the Judge's judgment the answer clearly was 'No'. The seller, using the name of Commonwealth Finance, had pursued a claim in Sharjah against the Habib Bank, a claim in which it failed because the first instance court held that there was no proof that Habib Bank had received 3 original bills of lading. The seller decided not to pursue an appeal against this decision. In any event, as the seller pointed out, even were the underwriters to establish a breach of Clause 16, any recovery thereunder could only be upon the basis of 'loss of a chance', since there could be no certainty that any action constituted with the seller substituted as plaintiff necessarily would have succeeded, any more than there could be any certainty of a successful appeal within the context of the existing action, which itself had failed at first instance. The Judge was unable to categorize the decision of the seller not to appeal as imprudent or unreasonable in the circumstances of a case wherein an Emirates bank was being pursued its own backyard. In addition, when the seller reached its decision not to cause an appeal to be filed, the cargo insurer was offered the opportunity itself to take over the proceedings and to mount an appeal at its own cost, but declined, ostensibly on the ground that it did not have sufficient time to consider the suggestion. It seemed to the Judge that the argument as advanced by the cargo insurer was an inappropriate attempt to extend the conceptual envelope in terms of the application of Clause 16, which in the Judge's view was not intended to impose upon an assured an obligation to exhaust all alternative remedies prior to instituting any claim against underwriters; as the seller neatly expressed the position, "the contract of insurance does not become a recovery of last resort". Accordingly, the Judge also rejected the cargo insurer's Clause 16 defence of set-off based upon the Sharjah proceedings in that the Judge did not accept that a breach of Clause 16 had been established. The cargo insurer's counterclaim must be dismissed.

The seller also claimed for, "reimbursement of all sums properly and reasonably incurred by the seller in respect of the Sharjah proceedings." These related to legal fees expended in Sharjah, and to legal fees expended in Hong Kong to two firms of solicitors. These sums amounted in total to HK$593,933.84. The Judge thought that the cargo insurer's 'potential duplication' argument might have some merit, and the Judge saw no reason why the cargo insurer should be held liable to pay in full the bills from the two Hong Kong solicitors. The Judge allowed this element of the claim, subject to a notional deduction of approximately 25%, with the result that the Judge held that in terms of the 'sue and labour' quantum the seller was entitled to recover HK$450,000.

The seller had succeeded in its claim against the cargo insurer. No issue had been raised as to the indemnification sought under the policy in terms of the invoice price of the goods, less credit given for the US$10,000 deposit initially received from the buyer, which sum no doubt was the price the buyer considered worth paying in order to achieve the fraud as ultimately was practised on the seller. The Judge made the Order in favour of the seller: there be judgment for the seller against the cargo insurer in the sum of US$329,712.80 and HK$450,000 plus costs and interest.

Please feel free to contact us if you have any questions or you would like to have a copy of the Judgment.

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