

Heightened Tensions in the Strait of Hormuz: Vessel Owners and Operators Review their Options

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From my time as a Royal Navy officer navigating the busy shipping lanes of the Strait of Hormuz, I recognize the challenges of operating in and around this navigational chokepoint.

Each day, many of the largest ships in the world sail (at speed) through the two-mile wide traffic separation lanes, a multitude of smaller wooden trading and fishing dhows travel in all directions and swarms of speed boats (many apparently engaged in smuggling) cut close ahead and astern of larger vessels. To add to this complex navigational picture, simmering international tensions (including the seizure of vessels by Iran) leave crews constantly trying to determine whether any of the multitude of contacts is a risk to their vessel.

Indeed, at the time of writing, the risks (and associated costs) have grown sufficiently concerning that owners and operators, as this article will examine, have been carefully considering their options to mitigate the risk, including their ability to refuse to comply with charterer's orders requiring passage through the Strait of Hormuz. The attack on six tankers in May and June as well as the seizure and attempted seizure of three tankers in July have resulted in heightened tensions in the region (as has the shooting down of both Iranian and United States military drones). The incidents in May, June and July evidence an alarming willingness by Iran to interfere with vessels on innocent passage and has resulted in a consequential increase in insurance premiums for vessels operating in and around the Strait.

Following a review of the risks and the costs (including increased insurance premium and potential crew bonus demands), a number of significant owners and operators have decided that discretion is the better part of valour and are not offering their vessels for employment that will require passage of the Strait.

For other owners and operators with contracts of affreightment to service or other charter commitments to or from ports in the Persian Gulf, a blanket refusal to sail any of their vessels through the Strait could give rise to significant charterer claims. Instead, these owners and operators will need to carefully consider their options, including whether events in and around the Strait give rise to a right to refuse to comply with charterer's orders that would necessitate passage of the Strait. At the time of writing, and subject to the drafting of the specific charter, the common view, whether by way of war risks, unsafe port or by frustration, is that owners and operators will probably not be able to establish a right to refuse to comply with such charterer's orders.

This article examines the key rights an owner-operator typically has to refuse to comply with the orders of a charterer. Additionally, noting the challenges of invoking refusal rights on anything resembling standard charter terms, this article also examines some of the other options owners and operators may wish to consider to mitigate the risks associated with the Strait.

War Risks Clause

Relatively detailed war risks clauses are contained in most time charters (including SUPPLYTIME 2017) and voyage charters, commonly on BIMCO CONWARTIME 2013 or VOYWAR 2013 terms as appropriate. These clauses standardly have two key limbs. The first limb provides the definition of “War Risks” and the second limb sets out the basis (usually by application of an objective judgement of the owner and/or master) on which a vessel’s master and/or owner can refuse to comply with a charterer’s orders requiring the vessel’s entry into an area where there is a risk of exposure to war risks.

It is relevant for the charterer to note that in addition to affording an owner/master the ability to refuse to comply with a charterer’s order, war risk clauses usually include arrangements for the discharge of cargo (to the extent relevant) in alternative ports. Furthermore, it is also common for war risk clauses to provide that, if a vessel proceeds in an area exposed to war risks, the charterer shall reimburse the owner for additional insurance costs (both insurance premiums required by owner’s insurers and also the cost of additional insurances the owner reasonably requires) in connection with war risks and also any crew bonuses the owner may become liable to pay.

Safe Port

Charterers are obliged to order a vessel only to ports which are, at the time of the order, safe. In this context, “*a port will not be safe unless, in the relevant period of time, the particular ship can reach it, use it and return from it without, in the absence of some abnormal occurrence, being exposed to danger which cannot be avoided by good navigation and seamanship...*” Leeds Shipping v. Société Française Bunge (The Eastern City) [1958] 2 Lloyd’s Rep. 127.

The determination of whether a port is safe includes consideration of the approaches to the port. The Strait is not itself a port, but for a vessel outside the Persian Gulf ordered to a port in the Persian Gulf there is no option other than to sail through the Strait. As such, it might be argued that the Strait forms part of the approach to the relevant Persian Gulf port. However, even if the Strait was found to fall within the scope of the charterer’s obligation to order the vessel only to safe ports, as of the time of writing, the number of vessels attacked/seized is very low compared to the total number of vessels transiting the Strait each day. As such, it is unlikely (in the absence of a significant increase in incidents or frequent targeting of vessels of specific character) that the recent attacks or seizures in the Strait would be categorised as anything other than “*abnormal occurrences*.”

Frustration

Hostilities and blockades have historically been a trigger for parties to consider whether the events amount to frustration of the contract. Frustration is a doctrine that excuses parties to a contract from further performance of the contract where circumstances arise, without blame or fault of either party, which render performance impossible or only possible in a very different way from originally contemplated.

The doctrine of frustration cannot be lightly invoked and will always depend on the facts of the case, for example the length of the charter and expected duration of relevant frustrating circumstances. The fact that performance is merely more onerous is insufficient to invoke the doctrine.

The closure of the Suez Canal during the Suez Crisis of 1956 gave rise to numerous unsuccessful claims for frustration. An important factor in the failure of many of these Suez Crisis cases was that the closure of the Suez Canal did not prevent vessels being routed via the Cape of Good Hope. In

contrast, if there was an effective closure of the Strait, there would be no alternative route for vessels needing to enter or leave the Persian Gulf.

Avoid Knee-Jerk Drafting

Owners, operators and charterers alike should also note that while a declaration of war is not in and of itself a frustration event, most charter parties include a war cancellation clause whereby either party can cancel the charter if war breaks out between countries the parties have expressly listed in the charter. While there may be a temptation, when negotiating a charter party contract, to include countries such as Iran and the U.S. within the scope of the war cancellation clause, both owners and charterers will need to carefully consider how this is done to avoid unexpected cancellation rights arising. For example, if the charter provides for worldwide trading limits, would parties expect hostilities between Iran and the U.S. to trigger a cancelling right when the vessel is operating between, for example, Australia and China?

Reflagging

The attempted seizure of the tanker Mesdar and the seizure of the Stena Impero by Iranian forces in July are clearly distinguishable from the attacks in May and June. The July incidents represent targeting of vessels with UK connections (for example sailing under British flag or managed by a UK-based manager) – in an apparent reaction by Iran to the arrest of the tanker Grace 1 by Gibraltar authorities. As a result of this targeting of vessels with UK connections, a number of owners/operators of UK flagged vessels that are required to sail through the strait have been considering their choice of flag, including whether it is possible to operate temporarily under a different flag.

Whilst a vessel cannot sail under the flag of more than one state at a time, by registering a bareboat charter of the vessel with a different flag (sometimes referred to as “dual registration”), it is possible to suspend the UK flag so the vessel will fly the flag of the other state for the term of the bareboat charter. While this may offer some owners and operators a suitable means of reducing a perceived temporary, heightened risk associated with the UK flag, it is not a “one size fits all” solution. The owner (and the bareboat charterer) will have to satisfy the preconditions of both ship registers, which will include obtaining the prior consent of any mortgagee of the vessel. Additionally, the owner will need to consider the impact that suspending the UK flag might have on its ability to take advantage of certain tonnage tax regimes.

Furthermore, events in the strait have demonstrated an alarming willingness by Iran to interfere with vessels on innocent passage, and owners will have to question the practical benefit of changing flag by way of bareboat charter registration. Also, in some instances, third parties can readily discover the underlying flag by paying a fee to the bareboat charter registry.

The UK Ministry of Defence says: *“the Royal Navy has been tasked to accompany British-flagged ships through the Strait of Hormuz ... should sufficient notice be given of their passage.”*

In some quarters, this might be seen as closing the stable door after the horse has bolted. However, the intervention by the HMS Montrose while escorting the British Heritage in July demonstrated the value of an effective naval escort.

At the time of writing, the British warships HMS Montrose and HMS Duncan are both in the Middle East providing protection to British vessels transiting the strait as part (following a change in tack by the UK government) of the U.S.-led coalition effort. However, with only Australia, Bahrain and the UK joining (at the time of writing) the U.S. in the coalition, it is not clear to owners and operators to

what extent other flag states will be able (or will be willing) to provide naval escorts to vessels flying their flag. It is notable, for example, that Japan has signalled that it will not join the U.S.-led coalition but may instead deploy one of its Maritime Self-Defence Force vessels to the straits as it balances security concerns in this strategic waterway with its close ties with both Iran and the U.S.

Certainly, not all flag states will be able to provide naval escorts to vessels flying their flag. Given the hope that the release of the *Grace 1* (renamed *Adrian Darya 1*) by Gibraltar authorities will have diminished any perceived imperative in Iran to specifically target vessels with a UK connection, the broader international character of previous attacks, the potential for tensions in the region to escalate and the Royal Navy tasking (if it can be maintained), owners and operators of UK flag vessels may conclude that the risk of sailing through the strait under the UK flag does not, on balance, justify reflagging their vessels.

The incidents of May, June and July are very concerning developments in an already volatile region, however (subject to the terms of the relevant charter), they are unlikely to afford a vessel owner or operator the right to refuse to comply with a charterer's order that would require passage through the Strait. This, however, may change with further escalation, and the Iranian targeting of vessels with UK connections illustrates why, when making any assessment of whether to sail through the Strait, owners and operators need to look at the circumstances at the time and how these may apply to the particular vessel, its characteristics (including, for example, its flag) and the terms of the relevant charter.