

***“Paper losses,
misappropriation of
commodities and passing
of risk: whose problem is it
anyway?”***

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Issues:

- Cargo All risk policy
 - subject
 - “All risks”: marine perils
 - transit clause
- ‘Paper loss’ vs physical loss/damages
- Distinguished from physical loss during voyage
- Not considering potential claim against carrier under contract of carriage

Engelhard CTP (US) LLC v Lloyd's Syndicate 1221

- Facts
 - Sale of copper ingots (containerized) on CIF basis
 - No problem with first shipment
 - Bills of lading, packing lists and quality certificates issued in respect of second shipment. At port of discharge it was discovered that contents of containers was slag.
 - No copper ingots in containers (agreed facts)
 - “Marine Cargo and Storage Insurance”
 - Open cover basis
 - Institute Cargo Clauses (A)



Engelhard CTP (US) LLC v Lloyd's Syndicate 1221

- **Main issues**

- Was paper loss covered in policy?
- Broad coverage, with wide definitions, offered to commodity traders against payment of substantial premiums

“...open cover there is an element of insurers taking the rough with the smooth. Insures offer very wide terms to cover losses which are fortuitous, in this way looking to make significant underwriting profit from very substantial premiums”.

Engelhard CTP (US) LLC v Lloyd's Syndicate 1221

Specific clauses:

“Concealed Damage Clause

It is agreed that any loss or damage discovered on removal the final packing shall be deemed to have occurred during the transit insured hereunder (and irrespective of attachment of Assured’s interest) and shall be paid for accordingly unless proof conclusive to the contrary be established, it being understood that any containers, cases and/ or packages showing signs of damage are to be opened as soon as practicable.”

“Container Clause

Notwithstanding anything contained herein to the contrary where Cargo, insured hereunder, is carried in Containers, it is agreed, as between the Assured and Insurers, that the seaworthiness and/or cargo worthiness of the Container is hereby admitted.

It is agreed that this Insurance contract is also to pay for shortage of contents (meaning thereby the difference between the number of packages as per shippers and/or suppliers invoice and/or packing list loaded or alleged to have been laden in the container and/or trailer and/or vehicle load and the count of packages removed therefrom by the Assured and/or their agent at time of container emptying) notwithstanding that seals may appear intact, and/or any other loss and/or damage including but not limited to cargo and/or container sweat howsoever arising. . . .”

Engelhard CTP (US) LLC v Lloyd's Syndicate 1221

“Fraudulent Documents

This insurance contract covers physical loss of or damage to goods and/or merchandise insured hereunder through the acceptance by the Assured and/or Shippers of fraudulent documents of title, including but not limited to Bill(s) of Lading and/or Shipping Receipt(s) and/or Messenger Receipt(s) and/or shipping documents and/or Warehouse Receipts and/or other document(s) of title.

This insurance contract is also to cover physical loss of or damage to goods insured caused by utilisation of legitimate Bill(s) of lading and/or other documents of title without the authorisation and/or consent of the Assured or their Agents and/or Shipper.”

Engelhard CTP (US) LLC v Lloyd's Syndicate 1221

- **Court**

- Approach to interpreting contracts (insurance policies)

- I. A court looks at the meaning of the relevant words in their documentary, factual and commercial context
- II. A term of an insurance contract must be construed in the context of agreement as a whole and with regard to it over all purpose

- Purpose of all risk marine cargo policy is to cover physical loss

- I. Marine Cargo Policy can extend to financial loss ('paper losses) if clear words are used.

- *Chemical Banks v Affiliated FM Insurance (USA)*

- I. Mere significant extension of cover beyond the standard entry-level all risk policy is not enough

Quadra Commodities SA v XL Insurance Company SE & Others



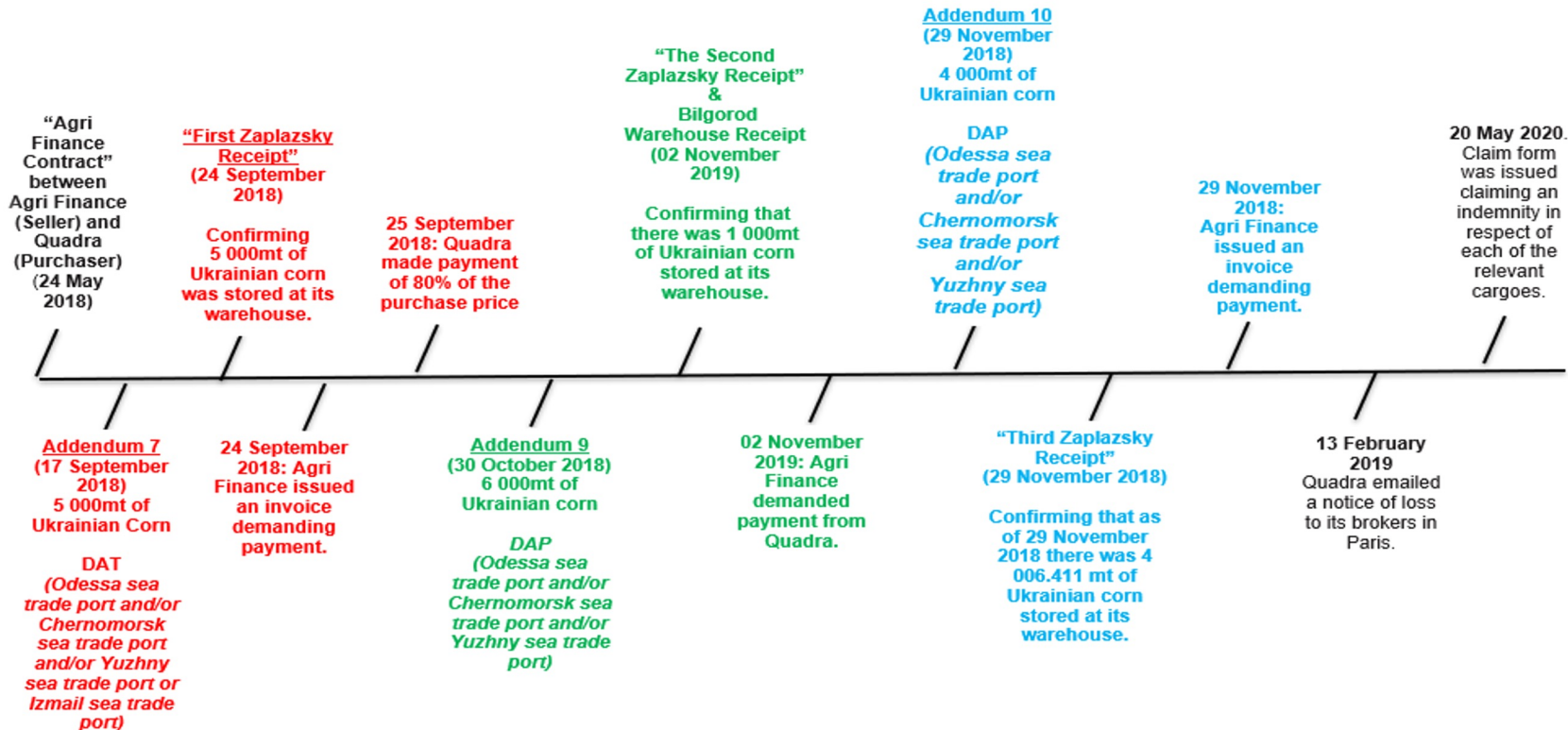
Quadra Commodities SA (cont.)

- **Facts**

- Quadra Commodities SA purchased various grains from a Ukrainian company, Agroinvest group between 2014 and 2018
- Agri Finance SA sold cargo to Quadra on DAP, Odessa sea trade port/... . Payment terms: 80% on transferring goods to internal warehouses and presentation of documents (Seller's invoice; Warehouse Receipt; Analyses card) (**Agri Finance Contracts**)
- Linepuzzle Ltd sold cargo to Quadra on delivery at warehouse (Linepuzzle contacts). Payment terms: 100% on transferring goods to internal warehouses and presentation of documents (Seller's invoice; Warehouse Receipt; Analyses card). Title to pass on payment. (**Linepuzzle Contracts**)
- Fraud: Multiple warehouse receipts in respect of same goods\
- Agroinvest group goes insolvent due to fraudulent Ponzi scheme

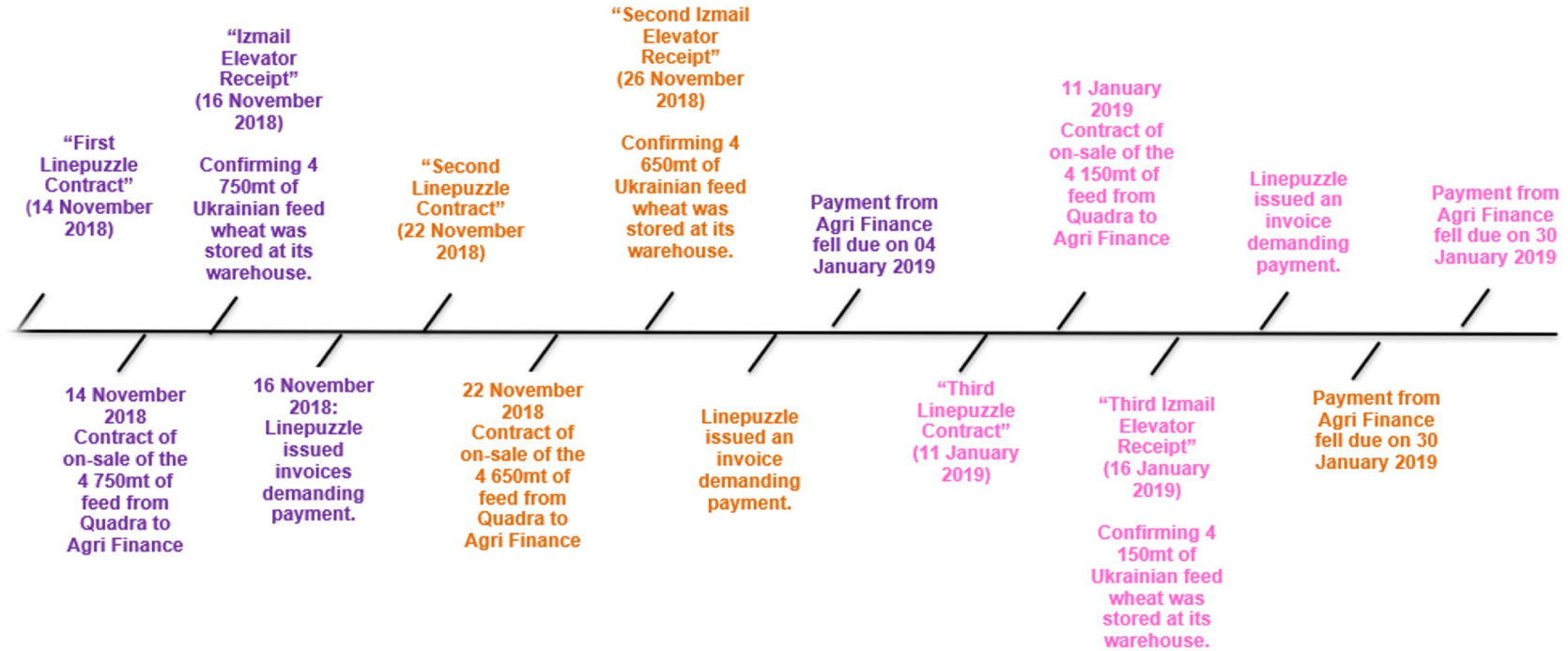
Quadra Commodities SA (cont.)

Timeline: Agri Finance Contract: Delivery: DAT/DAP



Quadra Commodities SA (cont.)

Timeline: Linepuzzle Contracts : Delivery: "...discharge of transport at the Izmail Elevator LLC (Terminal)..."



Quadra Commodities SA (cont.)

Specific clauses

“Misappropriation

This insurance contract covers all physical damage and/or losses, directly caused to the insured goods by misappropriation. By misappropriation is exclusively understood:

- 1. The use or disposal of the insured goods, in bad faith, by a contracting party (either suppliers and/or customers) of the assured and/or the policy holder or by the servant of a contracting party, with or without the involvement of the storage manager, contrary to the purpose for which he has received the insured goods, or in disregard of the instructions given to him by the assured/policy holder and/or by any other natural and/or legal person authorised to give such instructions;*
- 2. The physical or legal delivery, in bad faith, of the insured goods to any natural and/or legal person by a contracting party of the assured and/or the policy holder or by the servant of the contracting party, when this contracting party or this servant was aware or reasonably should have been aware that this natural and/or legal person was not entitled to the delivery of the insured goods.*

The risks covered under this clause will start at the time the Policy holder and/or affiliated companies assume an interest in the cargo and/or are in possession of a document of title and shall end when this interest finally ceases. The present clause shall benefit exclusively to the Policy holder and/or affiliated companies and shall prevail notwithstanding other provision agreed in the Policy.”

Quadra Commodities SA (cont.)

- Main issues
 - Subject matter of insurance
 - Existence of goods
 - Insurable interest
 - [Passing of risk]

Quadra Commodities SA (cont.)

- Main issues : Subject matter of insurance

Quadra: “...*the adventure consisting of the storage , transportation and delivery of goods which is purchased. **Alternatively**, the subject matter insured was goods*”

Quadra Commodities SA (cont.)

- Main issues : **Subject matter of insurance**

Court:

- Subject of insurance must be ascertained from terms of policy:
 - I. The policy is described as “Marine Cargo” Policy
 - II. The General Conditions of the Policy stated that the subject matter of the insurance was the cover of goods designated
 - III. The market wordings incorporated (Institute Cargo Clauses)
 - IV. Various Particular Conditions referred to the insurance being in property

Quadra Commodities SA (cont.)

Court:

- rejected argument that subject matter of policy was the success of storage operations (covered purely financial loss)
 - Subject of insurance under policy was **property**:
 - Policy (Interest Clause) covered all types of property insurance
 - Policy **did not** covers situation were no property had existed (and therefore not been lost or damaged)
- I. [This was not appealed by Quadra]

Quadra Commodities SA (cont.)

Main issues : **Existence of goods**

- Quadra had succeeded in showing that goods corresponding in quantity and description were physically present at the Elevators at the time the Warehouse Receipts were issued

- Three categories of evidence
 - I. The Warehouse Receipts and Grain Analysis Cards
 - II. The Bastico Reports (surveyors reports)
 - III. The buyers receipt of some of the grain stored in the Elevators (corroborative evidence)

“It was integral to the fraud that there should have been grain in the Warehouses, which could be inspected on behalf of traders, which matched the amount of grain which was being purportedly sold to any one trader. Were there not, then the fraud was likely to unravel at a very early stage”

Quadra Commodities SA (cont.)

Main issues: **Insurable interest**

- s 5(2) of Marine Insurance Act

Three characteristics of insurable interest:

- I. The assured may benefit from the safety of due arrival of the insured property or be prejudiced by its loss/damage/detention, or in respect of which it may incur a liability
- II. The assured stands in a legal or equitable relation to the adventure or to any insurable interest in such adventure; and
- III. The benefit, prejudice or incurring of liability must arise in consequence of the legal or equitable relation of the assured to the property or adventure.

Quadra Commodities SA (cont.)

Quadra's argument for insurable interest

- It had paid the purchase price
- It had an immediate right to possession of the goods
- It had proprietary interests in the goods

Quadra Commodities SA (cont.)

Quadra's argument for insurable interest: **paid the purchase price**

- **Cumberland Bone (USA)**

"... An equitable interest suffices"

- Approved *MacGillivray on Insurance Law* proposal:

"if neither property nor risk has passed, payment or part payment if the price will give the buyer an insurable interest, because the goods were lost or damaged and the seller was insolvent the buyer might not be able to recover any money which he had paid for them."

Quadra Commodities SA (cont.)

Quadra's argument for insurable interest: **had proprietary interests in the goods**

Court:

- Quadra did not have propriety title:
 - Title did not pass because the bulk of the which the Cargoes formed part of was not identified in any relevant contract as required by the English Sale of Goods Act 1979
 - Title was only intended to pass to Quadra (buyer) on delivery DAT or DAP (not at the Elevators) (Agri Finance Contracts)

Quadra Commodities SA v XL Insurance Company SE & Others : Court of Appeal

XL Grounds of appeal

- **The existence of the goods:** no goods corresponding in quantity and quality (i.e description) to the cargoes physically present in Elevators at the time Warehouse Receipts were issued
- **The identification of the goods:** Quadra did not have an insurable interest in the Cargoes in the circumstances they did not form part of a bulk which had been sufficiently identified.
- **The immediate right of possession:** Quadra did not have immediate right to possession
- **Practical consequences**

Quadra Commodities SA v XL Insurance Company SE & Others : Court of Appeal (cont.)

XL Grounds of appeal

- **The existence of the goods:** no goods corresponding in quantity and quality (i.e description) to the cargoes physically present in Elevators at the time Warehouse Receipts were issued

Appeal Court:

“*ample evidence*” of the existence of cargo

- Court *aquo* appreciated nature of fraud
- **Warehouse Receipts and Analysis cards** were evidence of existence of cargo in Elevators at time of issue (conceded that documents were inaccurate as to the rights they conveyed).Had been signed by numerous administrative and technical staff
- **Bastico inspection reports:** used laser meter (sufficient despite only visual inspections of surface and failure to take samples)

Quadra Commodities SA v XL Insurance Company SE & Others : Court of Appeal (cont.)

XL Grounds of appeal

- The identification of the goods: Quadra did **not have an insurable interest** in the Cargoes in the circumstances they did not form part of a bulk which had been sufficiently identified.
 - XL: The test for *identifying* bulk for purposes of assessing insurable interest should be the same as section 20A of English Sale of Goods Act 1979

Appeal Court

- No basis to impose an additional requirement- “*fundamentally unsound*”
- Additional requirement would:

“confuse the concept of an insurable interest as between insured and insurer with that of a proprietary interest as between buyer and seller, in circumstances where the authorities on insurable interest establish ... that an insured can have an insurable interest in goods even though it has no propriety interest.”

Quadra Commodities SA v XL Insurance Company SE & Others : Court of Appeal (cont.)

Appeal Court: Principle of English law:

An insured can have an insurable interest in goods even though it has **no propriety interest**.

AND

The existence of an insurable interest *“is not in any sense dependent upon the goods being ascertained or part of a sufficiently identified bulk for there to be an insurable interest”*

“This additional requirement which the insurers seek to impose is not only contrary to principle, but retrogressive. It goes against the direction of travel of the authorities on insurable interest for some 140 years, ... all of which urge the Court to lean in favour of finding that there is an insurable interest”

Walk away points

- Broad coverage for commodity traders – if this is intended, clear wording is required
- Development of insurable interest
- Distinction between passing of risk under Incoterms and insurable interest
- Incoterms
 - As between the seller and purchaser, who has what obligations under contract of sale:
 - Obligation to pay in event of loss
 - Obligation to insure
- Collection of evidence (surveyors)



Whose problem is it anyway?

... the marine cargo underwriters!

- Underwriters must manage commodity traders (insureds) expectation and provide accurate policy wording
- Underwriters must appreciate that the insured can have an insurable interest in circumstances in which risk has not passed to insured in terms of Incoterm



Quadra Commodities SA v XL Insurance Company SE & Others

Specific clauses

“Insurable Interest Clause

Notwithstanding that the interest insured may be purchased on Free on Board and/or Cost and Freight and/or Free Along Side or similar terms, it is agreed that the risk hereunder shall attach from the time of handling for the purposes of loading onto the carrying vessel at the Suppliers/Sellers tanks and/or warehouses, Underwriters being subrogated to the Assured’s right of recourse against the sellers and/or their insurers.”



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