

Circular From GARD

Date: 5 August 2021

Careful drafting of LOI invocation clauses in charterparties avoids later surprises

A letter of indemnity does not need to be printed and signed to be valid and binding – in some trades it is common for charterparties to contain clauses that allow letters of indemnity to be ‘invoked’ by the charterer in an email. Whilst it does save time and administration, these clauses and their invocation do require some thought and care.

Letters of indemnity (LOIs) are common in the shipping industry and are often used to ‘oil the wheels’ where a charterer wants to do something that does not fall squarely within the terms of the charterparty. The owner may be willing to comply, as long as they are happy that the additional risks will be covered by the charterer (including potentially the loss of P&I cover). The most frequently used LOI is for delivery of cargo without presentation of an original bill of lading, and the International Group of P&I Clubs (IG) has produced its own recommended LOI wording for this.

Valid LOIs are legally binding, and (generally) completely separate contracts from the charterparty. They can give rise to substantial liabilities, so charterers and owners must use them with due care. Claims arising from delivery of cargo without production of the bill of lading are excluded from P&I cover so in those cases the LOI is the recourse available to the owners if there is later a mis-delivery claim.

When a charterer gives an LOI it will often be printed on a formal letterhead and signed by an authorised representative. However, not all LOIs are printed and signed, and in some trades it is common for LOIs to be issued by the charterer ‘invoking’ certain pre-agreed LOI wording as contained in a charterparty clause – for example, see clause 13(b) of the Shelltime4 charterparty form.

Invoked LOIs can be just as valid as printed, signed LOIs, and they have the advantage of saving the parties time and administration. However, LOI invocation is not always as straightforward as is assumed, and there

are a number of points that should be considered by owners and charterers, both when drafting the LOI invocation clause, and when the LOI is actually being invoked:

Drafting LOI invocation clauses for charterparties

- **What requests can an LOI be invoked for?** The most common requests are for delivery without original bills of lading or at a different port from the one named in the bill of lading, but others are possible, for example split delivery. An invocation clause is an agreement that the owners will comply with a (compliant) request against the LOI terms, so clarity is needed here.
- **Make sure the LOI wording is clear.** For maximum clarity, it is best to set out the full LOI text(s), either in the clause itself, or a schedule. Another option would be to refer to the IG LOI or ‘owners’ P&I club wording’. The International Group of P&I Clubs has a standard published wording for delivery without presentation of an original bill of lading and delivery at a port other than stated in the bill of lading, but there is no standard IG LOI wording for other operations, such as splitting bills of lading or switching bills of lading. The IG LOI wording may therefore need amending if the invocation clause is intended to cover a wider range of situations than the two standard IG wordings. Also check that the LOI wording is suitable for the nature of the requests.
- **Consider if there should be express restrictions on when the charterer can invoke an LOI.** Should owners have an express right to reject an invoked LOI request where there are reasonable grounds to do so? Examples of this may be if there has been a material adverse change to the charterers’ creditworthiness, or where there is a known dispute relating to the charterers’ request.
- **Consider what steps the charterers need to take to invoke the LOI.** Some clauses require the charterer to specifically refer to the clause number when invoking – that can increase certainty if it is done properly, but if the requirement is overlooked for some reason it may cause problems later on. For that reason, if there are requirements for charterers to invoke an LOI, consider giving owners a specific right to waive those steps.
- **What information should be provided when invoking an LOI?** LOIs normally have several gaps that need to be completed before being printed and signed – which of those gaps should charterers specify when invoking? Some may be obvious from the voyage, but not always.
- **When is the LOI deemed to have been issued?** Normally this would be at the time when charterers make the request to the owner, but clauses can be drafted in different ways, so check that yours is clear.
- **When should a formal signed LOI be issued?** There may be thought to be no need for this in some cases, but in others the owners may want a formal signed LOI to be issued later, when there is less time pressure.

- **Do other charterparty clauses affect the LOI wording?** Normally LOIs are viewed as separate contracts, that are dealt with on their own terms, but there can sometimes be arguments that the wording needs to be read in conjunction with other charterparty clauses.

Things to check for when an LOI is being invoked under an agreed clause

- **Does the invocation message comply with the clause?** If the invocation clause requires the party invoking the LOI to include certain information, then check it has been provided. For example, where needed, does the invocation message refer to the invocation clause number? Have all the necessary details been provided to fill in the deemed LOI? Is the requested operation covered by the invocation clause?
- **Is the request clear enough?** Has the charterer given the full name of the party they want delivery to be made to? Does the request seek to narrow the terms of the LOI? If anything is unclear, seek clarification before proceeding.
- **What needs to be done to comply with the LOI?** This is crucial or the owner will not have the benefit of the LOI. If the cargo is to be delivered to a particular party, then check they are actually the party coming forward to take delivery. If anything is unclear, check before proceeding.
- **Should the owner keep evidence of compliance?** Although claims under LOIs are relatively rare, some owners may decide to record certain information about the party taking delivery, as a standard procedure, in case it is needed later.
- **Does the party giving the LOI have a record of it?** An LOI can be considered as similar to a guarantee, with the potential to generate very large exposures. A party giving (or receiving) them may therefore wish to keep a record of when they are issued and eventually cancelled/voided. If so, there is a risk that invoked LOIs may be treated differently and not recorded in the same way as formal signed LOIs, even though they can be legally identical.
- **Are the invocation clauses back-to-back?** Invoked LOIs may make it more difficult for a charterer in a chain to know if they are back-to-back. Even though the invoked LOI wording may be back-to-back, the way in which they are invoked may not be, which can give rise to additional disputes.

Remember, LOIs are often standing in place of P&I cover for operations taking the parties outside of the Hague-Visby Rules and defences so it is critically important that the LOI, if required, will be valid and enforceable. Invoking LOIs is efficient, and they can be just as valid/enforceable as printed and signed LOIs, but the invocation process can give rise to complications, so extra thought should be put into clauses covering this procedure.

Source of Information: The Gard P&I Club

Andrew Liu & Co. Ltd